CTJ Citizens for Tax Justice

June 12, 2009
Contact: Steve Wamhoff
(202) 299-1066 x33

Caviar, Cruises, and Cocaine: Summary

Read full the full report: www.ctj.org/pdf/afbfreports.pdf

A duo of new "studies" commissioned by a foundation established to promote repeal of the estate tax claim that eliminating this tax on the wealthiest few is crucial to our economy. The reports use one-sided analysis to produce the conclusions that their funders desire.

One study, released a few months ago by Douglas Holtz-Eakin and Cameron Smith, claims that repealing the federal estate tax would create 1.5 million jobs. The other, by Stephen Entin, claims that repealing the estate tax would actually result in *increased federal revenue*, not to mention higher gross domestic product (GDP).

1. The estate tax is a very progressive and important source of revenue, but it impacts few people and produces a small fraction of total federal revenue.

The studies paint the estate tax as having a major impact on the economy, even though less than one percent of deaths result in estate tax liability, and the estate and gift taxes combined only produce 2 percent of the total federal revenue.

2. The studies rely on one-sided models of the economy that consider the costs allegedly imposed by estate taxes without considering the benefits of the public services that estate taxes make possible.

The authors of the "studies" model the impact of taxes on the economy by considering the alleged costs of taxes but ignore the benefits. The benefits of taxes — the public services like roads, schools, law enforcement, national defense and other services that taxes make possible — are simply ignored.

Since the authors assume that tax dollars are collected and then simply disappear, of course they can come to no other conclusion but that taxes (including the estate tax) are always a drain on the economy. But this is obviously incorrect.

3. The study by Holtz-Eakin and Smith misrepresents previous research.

Holtz-Eakin and Smith rely on a 2000 study concluding that increases in the estate tax were correlated with decreases in *reported* estate values from 1916 to 1996. They assume this means *actual* estate values decreased as the estate tax was increased.

If you look at the part of this 2000 study that Holtz-Eakin and Smith do not cite, you find its authors are uncertain how much of this is due to tax avoidance practices which reduce *reported* estate values, but not *actual* wealth. In fact, the title of the 2000 study is "The Impact of the Estate Tax on the Wealth Accumulation *and Avoidance Behavior* of Donors."

4. The study by Entin uses discredited "dynamic analysis" to conclude that repealing the estate tax will actually result in *increased* government revenue.

Entin uses what is called "dynamic analysis" that accounts for the increases in income and profits that allegedly result from a tax cut. Entin claims to find that repealing the estate tax would cause incomes and profits to increase so much that the government would collect more revenue overall than it would if the estate tax is left in place.

But the facts have shown consistently that tax cuts cannot possibly lead to increased revenue. President George W. Bush's Treasury eventually concluded that tax cuts do not pay for themselves. And Holtz-Eakin, as head of the Congressional Budget Office, used dynamic analysis and eventually found that the positive revenue effects of tax cuts were tiny and could never offset but a fraction of the revenue losses that resulted.

5. Both studies rely on illogical assumptions about the way the estate tax affects the behavior of wealthy people.

The studies simply assume that the estate tax causes people to work less, as well as save and invest less of their money.

In fact, the estate tax could just as easily cause rich parents to work *harder* to accumulate whatever they believe is the optimal after-tax estate to pass on to their children. And studies show that the estate tax almost certainly causes the *children* of rich parents to work *harder* since it reduces their inheritances.