

A REPORT OF THE HERITAGE CENTER FOR DATA ANALYSIS

THE ECONOMIC AND FISCAL EFFECTS OF
REPEALING FEDERAL ESTATE, GIFT,
AND GENERATION-SKIPPING TAXES

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THE ECONOMIC AND FISCAL EFFECTS OF REPEALING FEDERAL ESTATE, GIFT, AND GENERATION-SKIPPING TAXES

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On June 7, 2001, President George W. Bush signed into law the Economic Growth and Tax Reform Reconciliation Act of 2001 (EGTRRA),¹ a package of tax reductions and policy changes that include temporary reductions in three federal estate transfer taxes (FETTs). The law mandates the phaseout of the federal estate tax and the federal generation-skipping tax by January 1, 2010, and the reduction of the federal gift tax. The provisions of the law, however, are scheduled to expire on January 1, 2011, at which time all three federal estate or wealth transfer taxes will return to their 2001 pre-tax cut levels.

Analysts in the Center for Data Analysis (CDA) at The Heritage Foundation estimated the effects of an immediate and permanent repeal of all three federal estate transfer taxes. These effects include changes in tax revenue, gross domestic product (GDP), interest rates, employment levels, personal income, and inflation. Any of these macroeconomic changes could affect tax revenues significantly.

The findings of the CDA analysis show that eliminating the taxes entirely would yield strong economic and fiscal benefits for the country. Immediate and permanent repeal of the FETTs would improve the nation's eco-

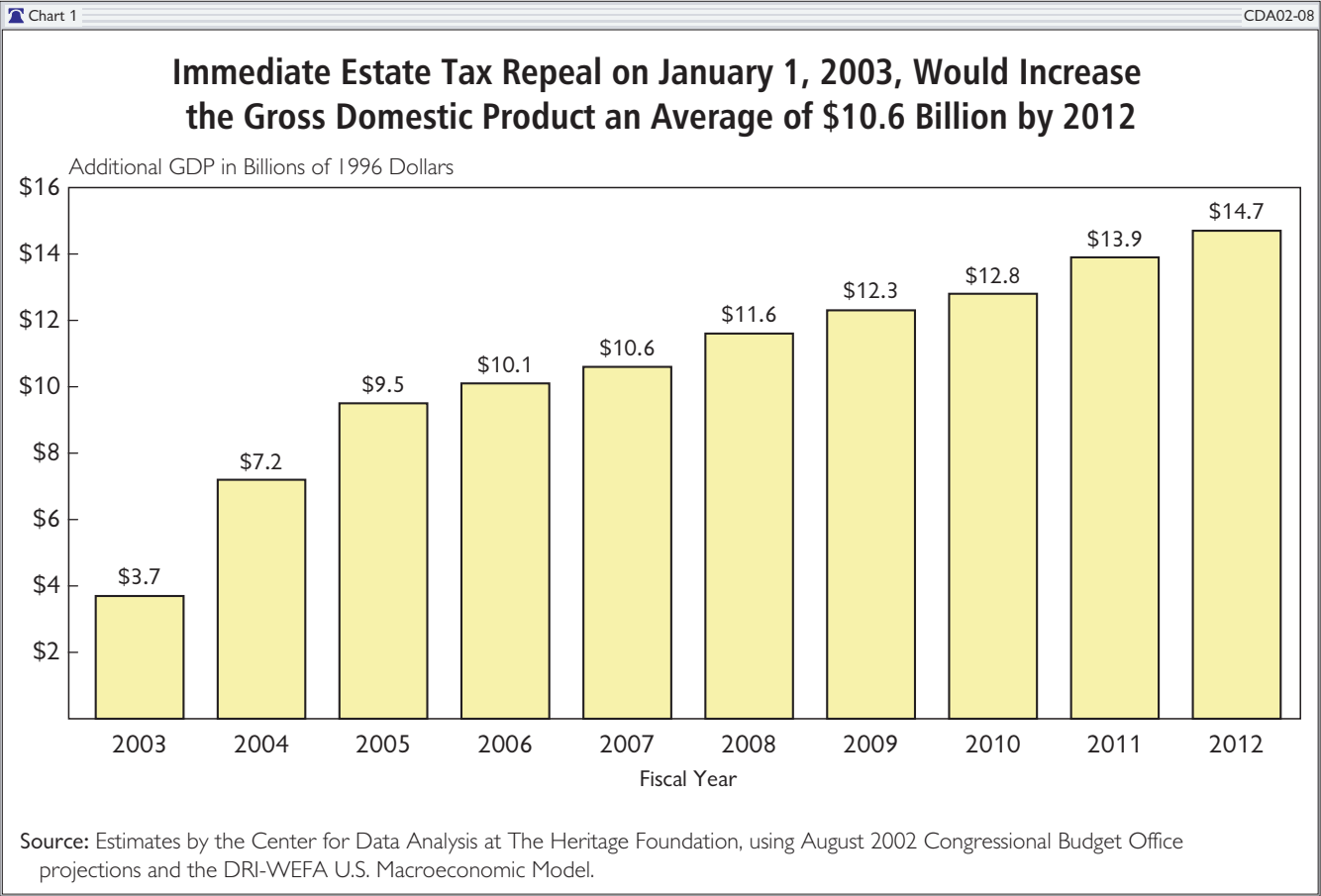
nomics performance over the next 10 years, create thousands of jobs, and raise disposable income without increasing cumulative federal deficits or publicly held debt by the end of the 10 years. Moreover, under the current tax code, repealing the FETTs would, over the following 10 years, not reduce federal revenues, but would increase them and provide further opportunity for additional tax relief.

Specifically, compared with what would occur under the current law, an immediate and permanent repeal of the three FETTs on January 1, 2003, would have the following beneficial effects. For example, in fiscal year (FY) 2012 alone, repeal would:

- **Add** \$14.7 billion (adjusted for inflation)² to the GDP;
- **Add** 118,000 jobs to the U.S. economy;
- **Reduce** nationwide unemployment by 27,000 persons;
- **Raise** U.S. personal disposable income by an inflation-adjusted \$11 billion;
- **Increase** non-residential net capital stock by \$25.1 billion and lower the user cost of capital by 0.3 percent;

1. Public Law 107-16.

2. All inflation-adjusted dollars referenced in this report are indexed to the 1996 overall price level and thus represent 1996 dollars.



- **Leave** relative price levels and key interest rates unaffected, in spite of the stimulating effect repeal would have on economic activity; and
- **Reduce** the nation's publicly held debt by \$5.7 billion.

The current plan to restore the FETTs in 2011 will substantially curtail these substantial benefits.

HOW ESTATE TRANSFER TAXES AFFECT ECONOMIC BEHAVIOR

Several studies have found that the federal estate transfer taxes reduce economic growth. For example, in a 1998 study, former DRI/McGraw-Hill economists Richard F. Fullenbaum and Mariana A. McNeill cited three reasons for this overall effect.³ According to these experts, the FETTs:

- **Cause** considerable resources to be diverted away from economically productive activities and toward tax avoidance activities;
- **Raise** the user cost of capital, biasing affected owners of capital toward consumption and away from investment; and
- **Reduce** labor force participation.⁴

Henry J. Aaron, a Brookings Institution scholar, and Alicia Munnell, a former Clinton Administration economic adviser, pointed out in 1992 that the FETTs created substantial rewards for tax avoidance activities. They echoed Columbia law school professor George Cooper's description of the levies as "voluntary taxes." Out of \$123 billion transferred across generations in 1986, a mere \$36 billion was reported on estate tax returns, resulting in \$6 billion in federal collections that year. "Informed observers," these experts noted, "think

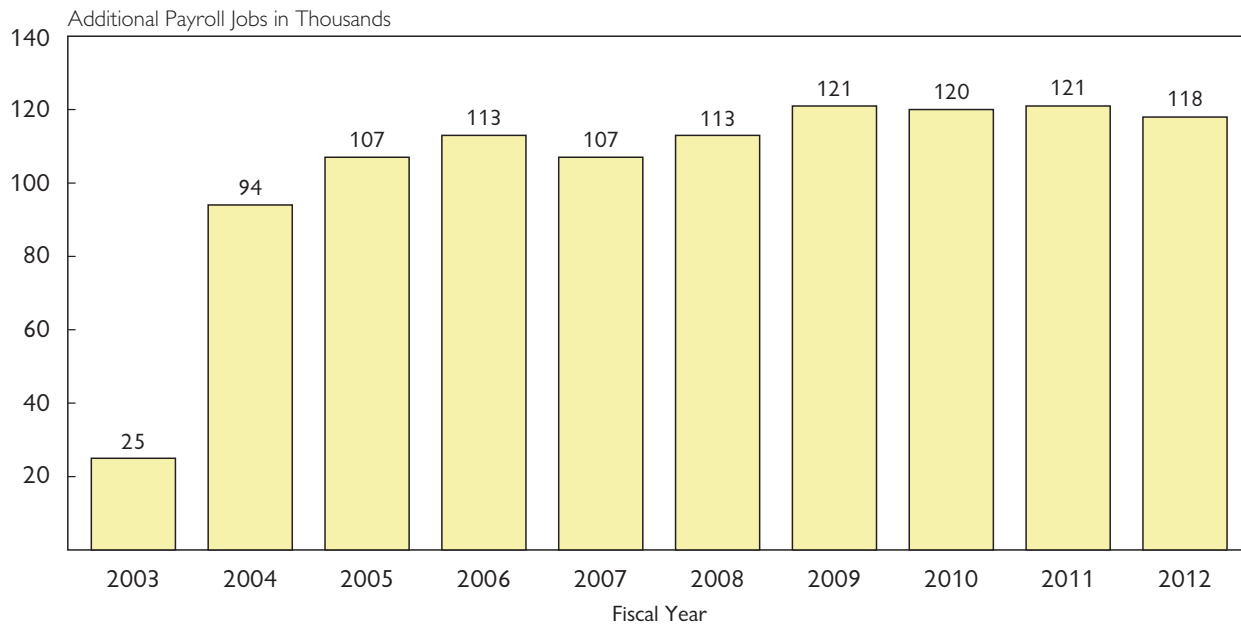
3. Richard F. Fullenbaum and Mariana A. McNeill, "The Effects of the Federal Estate and Gift Tax on the Aggregate Economy," Research Institute for Small and Emerging Business, *Working Paper Series* No. 98-01, 1998, pp. 10-11.

4. William W. Beach, "The Case for Repealing the Estate Tax," Heritage Foundation *Backgrounder* No. 1091, August 21, 1996, p. 26, at <http://www.heritage.org/Research/Taxes/BG1091.cfm>.

Chart 2

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Immediate Estate Tax Repeal on January 1, 2003, Would Bolster Employment an Average of 104,000 Additional Jobs

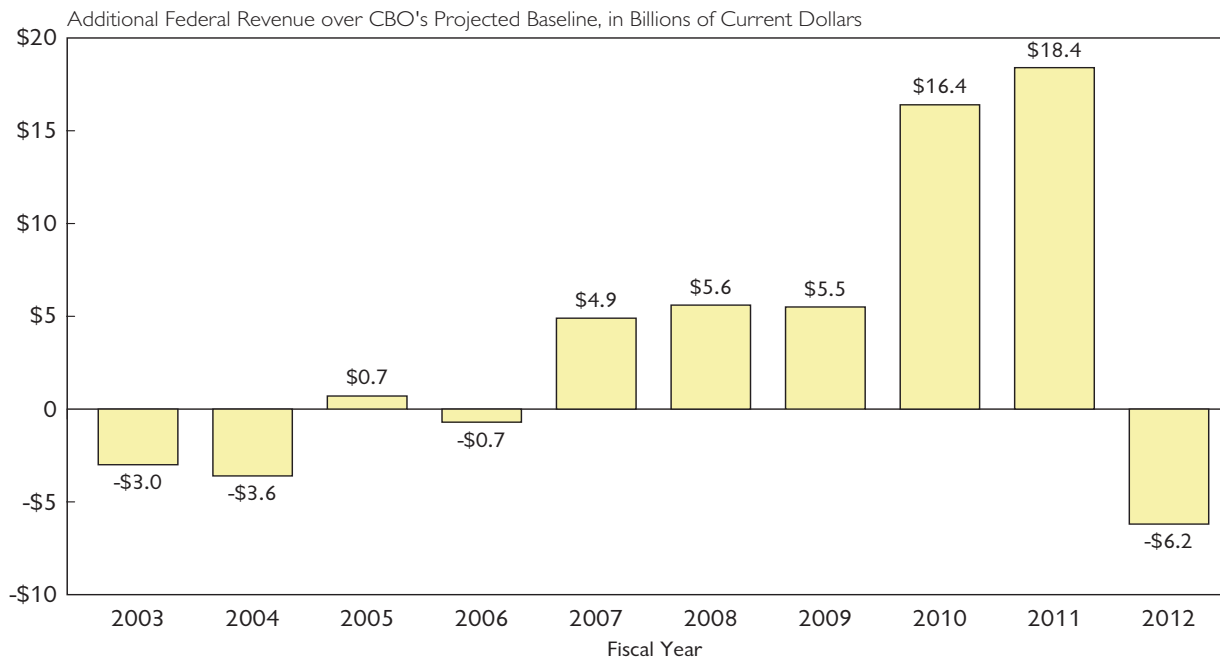


Source: Estimates by the Center for Data Analysis at The Heritage Foundation, using August 2002 Congressional Budget Office projections and the DRI-WEFA U.S. Macroeconomic Model.

Chart 3

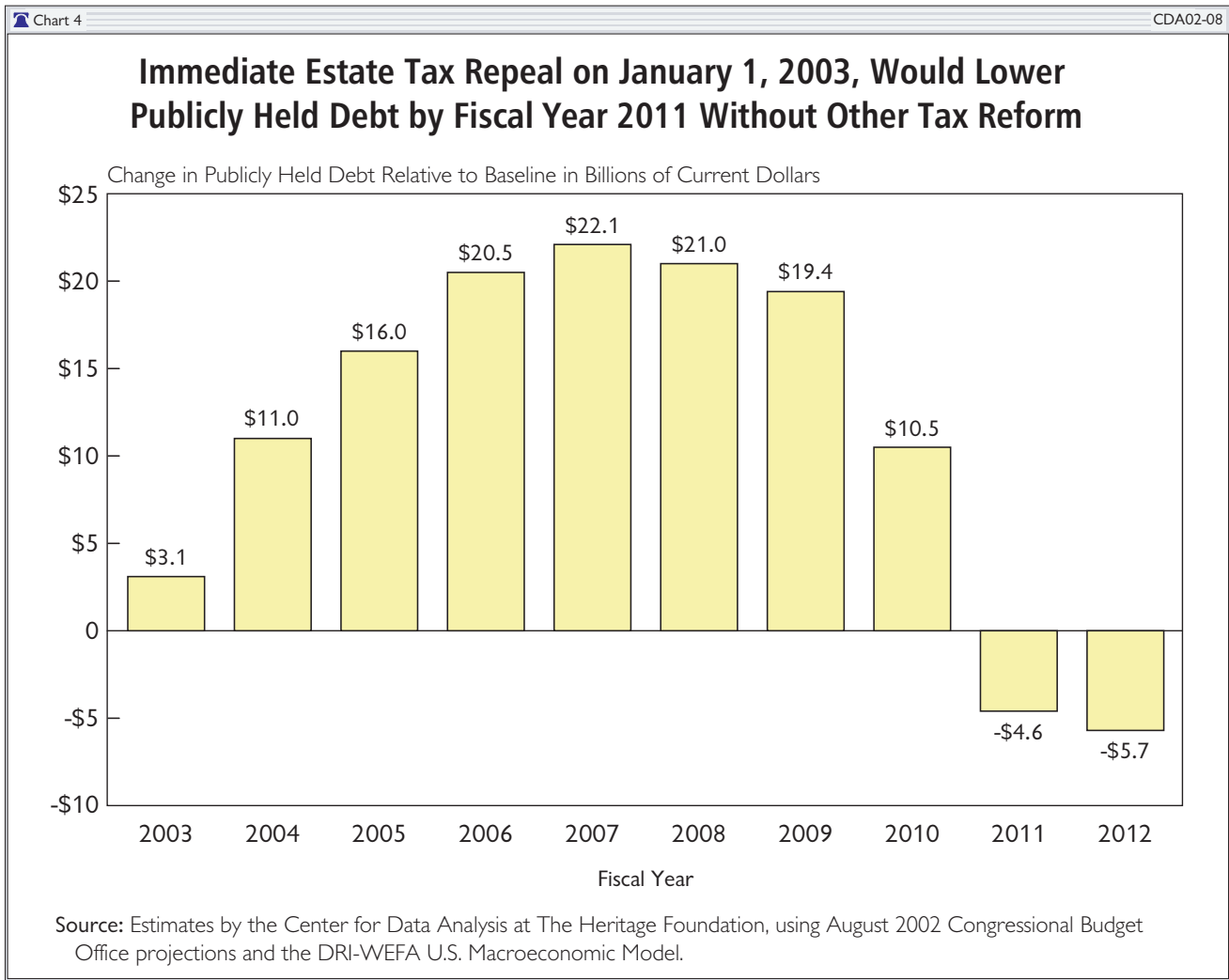
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Immediate Estate Tax Repeal on January 1, 2003, Would Boost Federal Revenue Without Other Tax Reforms



Note: The CBO projected baseline includes the currently scheduled restoration of federal estate transfer tax policy as it was prior to 2001, which explains the negative bar in 2012.

Source: Estimates by the Center for Data Analysis at The Heritage Foundation, using August 2002 Congressional Budget Office projections and the DRI-WEFA U.S. Macroeconomic Model.



that decedents could have avoided even this modest toll if they had taken the time to do so.”⁵

Tax avoidance requires the services of skilled estate planners. The federal estate transfer taxes nurture an industry that employs thousands of highly educated and highly remunerated professionals. In the early 1990s, the American Bar Association reported that approximately 16,000 (5 percent) of its members described their area of concentration as trust, probate, and estate law. This total does not include the number of account-

ants and financial planners who offer estate-planning services.⁶

Tax avoidance activity has several facets. All involve reducing the size of the estate by the time the property owner dies to avoid the death tax—basically a second tax on assets purchased with after-tax income. Common methods of tax avoidance include making direct transfers from the estate to such legal entities as trusts or limited partnerships, or as carefully planned gifts.⁷ Another is replacing monetary compensation for

5. Henry J. Aaron and Alicia Munnell, “Reassessing the Role for Wealth Transfer Taxes,” *National Tax Journal*, Vol. 45, No. 2 (June 1992), pp. 133–134, at [http://ntj.tax.org/wwwtax/ntjrec.nsf/D4945A8128C6353F8525686C00686E24/\\$FILE/v45n2119.pdf](http://ntj.tax.org/wwwtax/ntjrec.nsf/D4945A8128C6353F8525686C00686E24/$FILE/v45n2119.pdf).

6. *Ibid.*, p. 138.

7. A number of financial counseling firms list transfers to trusts and carefully planned gifts on their Internet sites as key estate planning techniques. See, for example, Prudential Financial at <http://www.prudential.com/productsAndServices/0,1474,intPageID%253D1350%2526bInPrinterFriendly%253D0,00.html>; Dana S. Beane & Company, P.C., at <http://www.dsbc-pas.com/estatetaxplanning/estateplanningtech.html>; and Deborah A. Malkin, Attorney at Law, at <http://www.malkintrust.com/Avoid-Estate-Taxes.htm> (October 25, 2002).

highly paid corporate executives with life insurance. Yet another is the use of experts to procure a low estimate of the value of the estate.⁸

Heritage economist William Beach argues that the FETTs are a significant determinant of the cost of capital—the higher the level of such taxes, the higher the required rate of return on capital investments. The reason, he explains, is that “when individuals begin to see that their income and investment efforts will produce a future taxable estate, they...increase their earnings requirements to build the funds needed to pay the future wealth transfer taxes.”⁹

This higher earnings requirement can be observed in the national economy as a higher user cost of capital than would otherwise prevail. The higher user cost of capital discourages investment and creates a bias among affected property owners in favor of consumption. MIT economist James M. Poterba estimates that federal estate transfer taxes add at least 1.3 percent to the cost of owning capital in the United States.¹⁰

Fullenbaum and McNeill describe estate transfer taxes as reductions in the after-tax wages of affected workers.¹¹ Economic theory suggests that, all other things being equal, public policies that broadly reduce after-tax wages reduce labor force participation rates.¹² According to Beach, this reduction reached 97,200 persons in 1996.¹³

Eliminating the FETTs permanently and immediately would reverse these damaging effects on the national economy. Thousands of federal estate tax lawyers would be freed to engage in activities more closely associated with economic growth; the

user cost of capital in the national economy would fall, making more types of investment immediately attractive and thus spurring investments overall; and a disincentive that keeps thousands of Americans out of the labor force would disappear.¹⁴

The 2011 phaseout and restoration of the federal estate tax (FET) and the federal generation-skipping tax (GST) enacted in last year's tax cut law will do very little to alter the tax avoidance behaviors described above. No estate holder with a reasonable expectation of living past January 1, 2011, will expect to realize the tax relief, since the phaseout affects only the estates of those who die before that date. A person expecting to live past 2010 will adjust his economic behavior as if the FET and the GST had not changed at all.

Consequently, the smaller the share of prospective estate tax filers expecting to die between 2002 and 2010, the less the national economy will benefit from the one-year repeal. CDA analysts estimate that under current law at least 3 million FET returns will be filed during the period 2003–2027.¹⁵ Of these returns, less than 16 percent are expected to be filed before 2011.¹⁶

Thus, EGTRRA provides no estate tax relief at all for the vast majority of taxpayers who should expect to be affected by FETTs, in addition to which the bulk of potential economic benefits that the nation could see from estate tax reform will not be observed under the current law. However, Congress could unlock these effects through an immediate and permanent repeal of the federal estate transfer taxes.

8. Aaron and Munnell, “Reassessing the Role for Wealth Transfer Taxes,” pp. 135, 137.

9. Beach, “The Case for Repealing the Estate Tax,” p. 24.

10. James M. Poterba, “Estate Tax and After-Tax Investment Returns,” in Joel M. Slemrod, ed., *Does Atlas Shrug?* (Cambridge, Mass.: Harvard University Press, 2000), p. 339. Beach estimates that the FETTs add 3 percent to the cost of owning capital. See Beach, “The Case for Repealing the Estate Tax,” p. 24.

11. Fullenbaum and McNeill, “The Effects of the Federal Estate and Gift Tax on the Aggregate Economy,” p. 10.

12. All other things held constant, economic theory suggests unambiguously that reductions in after-tax wages reduce the number of participants in the labor force, since both the wealth and the substitution effect reinforce one another, rather than offset one another, in this case.

13. Beach, “The Case for Repealing the Estate Tax,” p. 24.

14. *Ibid.*

15. Estimated by extrapolating unpublished projections for estate tax filings by fiscal year performed by the Statistics of Income Program of the Internal Revenue Service.

16. Projections for estate tax filings through 2010 from unpublished Statistics of Income Program projections.

THE HERITAGE ANALYSIS OF FETT REPEAL

In addition to these behavioral aspects of tax policy changes, the CDA analysts considered the interaction between FETT repeal and capital gains tax collections, as well as between FETT repeal and federal spending.

Capital Gains Offset. Without further tax reform, repealing the FETTs immediately and permanently would mean higher capital gains tax revenues. The reason: The current statute regarding the FETTs exempts inheritors from taxes on gains unrealized, during the decedent's lifetime, on the transferred property. Inheritors are allowed to raise the base value of the transferred property to its fair market value at the time the decedent dies. This exemption is known as the "step-up" of the basis on transferred property. According to the Joint Committee on Taxation (JCT), this exemption would amount to \$216.6 billion in uncollected capital gains tax revenue in the five years from 2002–2006.¹⁷ The mere repeal of the FETTs would abolish this capital gains tax exemption and could subject the inheritors to this increased tax levy.

To relieve the tax burden at death and reduce the need for the heir to liquidate assets prematurely, CDA analysts incorporated a capital gains exclusion of \$1 million on transferred estates and a \$3 million exclusion on spousal transfers. Such a provision severs "the link between payment of the tax and death and allows heirs to select the timing of the realization of capital gains."¹⁸ CDA analysts estimated the amounts of this exclusion for the years 2003–2012 using JCT estimates and incorporated them into the economic impact study of

FETT repeal. (These estimates are shown in Table 1 in the Appendix.)

Congress could eliminate this capital gains offset, of course, by repealing the capital gains tax or, at a minimum, ensuring that any additional tax revenue arising from the capital gains offset is used for further tax relief.

Federal Spending. CDA analysts assumed that overall federal government spending would be adjusted according to changes in tax collections caused by eliminating the FETTs. This assumption assures that there would be virtually no change in the cumulative federal surplus during the 10-year period from fiscal years 2003–2012.¹⁹ Year-to-year variations in surpluses do occur. CDA analysts channeled these spending changes through adjustments in federal non-defense spending and federal grants-in-aid to state and local governments.

A Dynamic Analysis of Immediate FETT Repeal

CDA analysts used the DRI–WEFA U.S. Macroeconomic Model to conduct the dynamic simulation of the elimination of the FETTs.²⁰ They performed the simulation using a version of the September 2002 DRI–WEFA long-term forecast, which they modified to incorporate the economic and budgetary assumptions published by the Congressional Budget Office (CBO) in August 2002.²¹ This adapted forecast can be used to find the effects of policy changes on the economy and the federal budget through a dynamic rather than a static analysis.

A static analysis of the potential effects of a tax policy change would examine only its effects on tax collections. This method could omit important effects that changes in tax policy exert on the econ-

17. Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2002–2006," January 17, 2002, p. 23, at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=2002_joint_committee_on_taxation&docid=f:76452.pdf.

18. Fullenbaum and McNeill, "The Effects of the Federal Estate and Gift Tax on the Aggregate Economy," p. 9.

19. See Appendix, Table 2.

20. The Center for Data Analysis used the Mark 11 U.S. Macroeconomic Model of DRI–WEFA, Inc. (now known as Global Insight), to conduct this analysis. The model was developed in the late 1960s by Nobel Prize–winning economist Lawrence Klein and several colleagues at the University of Pennsylvania. It is widely used by *Fortune* 500 companies, prominent federal agencies, and economic forecasting departments. The methodologies, assumptions, conclusions, and opinions herein are entirely the work of Heritage Foundation analysts. They have not been endorsed by, nor do they necessarily reflect the views of, the owners of the model.

21. Congressional Budget Office, "The Budget and Economic Outlook: An Update," August 2002, at <http://www.cbo.gov/showdoc.cfm?index=3735&sequence=0>.

omy. For example, if a proposed tax reduction is likely to improve national economic performance, that performance could in turn increase tax collections, which could partially offset the federal revenue losses caused by the tax reduction. Static analysis would be likely to omit the policy's beneficial effect on the economy and therefore overestimate the cost of that particular tax reduction. A dynamic analysis, which considers the effects of the tax policy change on the economy, would more accurately estimate the overall effects of the tax policy change on both the national economy and on tax collections.²²

Heritage economists performed a dynamic analysis of FETT repeal by changing policy-related variables²³ in the adapted DRI-WEFA model to simulate the effects on the national economy. They then conducted an economic simulation using the adapted model and the changed policy-related variables to find the effects of the policy change on the U.S. macroeconomy. They compared the values of key macroeconomic quantities before and after simulation, attributing the observed differences to the policy change. This method allowed CDA analysts to identify the effects on the national economy of that change, in this case FETT repeal. (See Appendix, Table 2.)²⁴

Take, as an example, the dynamic analysis of a hypothetical tax policy change. Suppose the simulation corresponding to that policy change yields a GDP for 2005 that is \$1 billion higher than its value in the original CBO projection. In this case, the tax policy change would be said to have added \$1 billion to the GDP for 2005. In other words, one may say that the GDP would be \$1 billion higher in 2005 under the tax policy than without it.

BENEFITS OF ELIMINATING ESTATE TRANSFER TAXES

Table 2 in the Appendix displays the difference in economic results between the policy of repeal and the current-law policy as reflected in the adapted DRI-WEFA model. The table shows that immediate and permanent FETT repeal would increase the nation's economic growth compared with what would happen under the currently planned temporary phaseout of such taxes. In the absence of further tax reform, immediate and permanent repeal would increase federal revenues over the following 10 years as well as:

- **Strengthen economic growth.** By the end of FY 2012, GDP would be \$14.7 billion higher (after adjusting for inflation) under FETT repeal than it would under current law (as projected by the CBO). Moreover, average GDP between 2003 and 2012 would run \$10.6 billion higher.
- **Create more job opportunities.** With the FETTs eliminated, the economy would support 118,000 more jobs by 2012 than it would under current law. Between 2003 and 2012, the average national employment level would run 104,000 jobs higher under repeal than it would otherwise.
- **Reduce unemployment.** Immediate and permanent repeal of the FETTs also would reduce unemployment by 27,000 persons in 2012. The average number of unemployed for the 10 years following repeal would be 13,000 lower than without repeal.
- **Raise disposable personal income.** Under elimination of the FETTs, personal disposable income would be \$11.0 billion higher by the end of FY 2012, with immediate repeal, than it would without it. Average personal disposable income during 2003–2012 would be \$10.3 billion higher under repeal.

22. For a discussion of the shortcomings of static analysis of the effects of tax policy changes, see Daniel J. Mitchell, "The Correct Way to Measure the Revenue Impact of Changes in Tax Rates," Heritage Foundation *Background* No. 1544, May 3, 2002, at <http://www.heritage.org/Research/Taxes/BG1544.cfm>; see also "The Argument for Reality-Based Scoring," Heritage Foundation *Web Memo* No. 92, March 29, 2002, at <http://www.heritage.org/Research/Taxes/WM92.cfm>, and Daniel R. Burton, "Reforming the Federal Tax Policy Process," *Cato Policy Analysis*, forthcoming December 2002.

23. The variables changed in this simulation for the purpose of modeling FETT repeal are enumerated in the Appendix.

24. Table 2 shows year-by-year estimates of how repeal of the FETTs would likely change major economic indicators.

- **Increase non-residential investment.** Repeal of the estate tax would improve the investment environment enough to raise investment by \$7.3 billion (adjusted for inflation) by 2012. Non-residential capital stock would be \$25.1 billion higher. The user cost of capital would be 0.3 percent lower by 2012 than it would be if the FETTs were not eliminated.
- **Leave relative price levels and key interest rates unaffected.** In spite of the stimulating effect FETT repeal would have on economic activity, it would not significantly affect either the consumer price index (CPI) or key government interest rates.
- **A slight decline in the federal publicly held debt during 2012.** During the first years after repeal of the FETTs, the decline in federal revenue would raise the federal publicly held debt above where it would be under current law, reaching an inflation-adjusted \$22.1 billion above the CBO's projection for 2007. This margin would then decline, reaching \$5.7 billion *below* the CBO-projected level by 2012.

CONCLUSION

The tax cuts President Bush signed into law last year incorporate the phasing out and temporary abolition of the federal estate tax (FET) and generation-skipping taxes (GST). This move signaled Congress's willingness to consider key reforms of this tax.

However, the law allows the FET and other estate or wealth transfer taxes to return in 2011. These estate taxes have damaging economic effects, slowing economic growth and reducing potential increases in employment. A temporary phasing out of the federal estate transfer taxes will not address either of these detriments.

As this CDA analysis shows, after just 10 years, an immediate and permanent repeal of the FET and other federal estate transfer taxes would strengthen economic activity, create hundreds of thousands of new jobs, bolster disposable income by \$11 billion, reduce unemployment, and raise revenue while leaving the nation with a lower federal publicly held debt by FY 2011.

—Alfredo B. Goyburu is a Policy Analyst in the Center for Data Analysis at The Heritage Foundation.

APPENDIX

METHODOLOGY

Heritage Foundation economists in the Center for Data Analysis (CDA) followed a two-step procedure in identifying the 10-year economic and budgetary impact of an immediate and permanent repeal of the federal estate transfer taxes (FETTs) effective January 1, 2003.

First, CDA analysts applied Congressional Budget Office (CBO) projections for FETT collections under current law.²⁵ As a working assumption, they used the negative of these collection estimates as a preliminary estimate of the federal revenue that would be lost under FETT repeal. To this estimate, CDA analysts applied a projection of the additional capital gains taxes that would be collected as a result of an FETT repeal, with a first \$1 million exemption plus a \$3 million spousal exemption, which produced a modified preliminary estimate for federal revenue loss. (See Table 1.)²⁶

Using this modified preliminary estimate as an ultimate forecast of the federal revenue loss resulting from FETT repeal, however, would be to implement an erroneous static approach to an analysis of the effects of that tax policy change. The more correct (dynamic) approach is to take account of the macroeconomic effects of the tax policy change. These effects include changes in gross domestic product (GDP), interest rates, employment levels, personal income, and inflation. Any of these macroeconomic quantities could affect tax revenues significantly.

Second, CDA analysts introduced the modified preliminary estimate of tax revenue change into an especially adapted version of the DRI-WEFA U.S. Macroeconomic Model.²⁷ They then processed the simulation and noted changes in key macroeconomic and budget variables compared with their values in the original adapted version of the model. Differences in these key variables were

Fiscal Year	In Billions of Dollars									
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Static FETT Revenue Loss	\$17.3	\$24.0	\$21.0	\$24.0	\$20.0	\$21.0	\$23.0	\$14.0	\$14.0	\$41.0
Capital Gains Tax Collections Increase After Repeal, January 1, 2003	\$13.4	\$19.2	\$20.6	\$22.2	\$23.8	\$25.6	\$27.5	\$29.6	\$31.8	\$34.2
Net Static Change	-\$3.9	-\$4.8	-\$0.4	-\$1.8	\$3.8	\$4.6	\$4.5	\$15.6	\$17.8	-\$6.8

Note: The first line ("Static FETT Revenue Loss") shows revenue changes under current law. This baseline assumes the currently scheduled re-instatement in 2011 of FETT tax policy as it was prior to 2001, which explains the large number in 2012.

Source: August 2002 Congressional Budget Office projections and calculations performed by the Center for Data Analysis at The Heritage Foundation, using data from the Internal Revenue Service Statistics of Income Program.

25. Congressional Budget Office, "The Budget and Economic Outlook: An Update," p. 48.

26. CDA economists applied a staged process to calculate the additional capital gains tax collections. The first stage was to combine historical averages on federal estate tax returns from the IRS Statistics of Income Program and modified projections from the Joint Committee on Taxation on the current-law capital gains tax exclusion at death. These together yielded a projection of the amount of taxable capital gains held in estates over and above the \$1 million exemption, without taking into account the higher spousal exemption. The second stage was for CDA analysts to use historical averages to find how much the higher \$3 million spousal exemption would subtract from the first projection of taxable capital gains. The final stage involved applying the long-term capital gains tax rate to the modified projection for non-exempt taxable capital gains to create a projection of the additional capital gains tax collections under FETT repeal.

27. This version of the model is especially adapted to embody economic and budgetary projections published by the CBO in August 2002.

attributed to the response of the U.S. economy and federal budget to the tax policy change—that is, the dynamic response. (See Table 2.)

The Simulation²⁸

The DRI–WEFA model contains a number of variables used to simulate policy changes. CDA analysts introduced static tax revenue and economic behavior change estimates to the model in order to find the dynamic responses of the U.S. economy and federal budget during 2003–2012 to immediate and permanent repeal of the FETTs. These include:

- **Civilian Labor Force.** Heritage economist William W. Beach estimated in 1996 that the FETTs reduced the labor supply by 97,200 in 1996.²⁹ CDA analysts revised this estimate to 103,900 using more recent information on the nation’s civilian labor force growth rate from the Bureau of Labor Statistics. They adjusted the variable controlling labor supply in the model accordingly, phasing in the 103,900-worker increase over two years.
- **Non-NIPA³⁰ Federal Government Revenue.** This variable measures taxes paid to the federal government not coming from income flows in the economy, such as the estate tax and the capital gains tax. CDA economists adjusted this variable according to the net static change in federal collections of these two types of tax resulting from the tax policy reform.
- **Business Sector Price Index.** CDA analysts reduced this variable during the forecast period in order to reflect lowered compliance costs for the business sector resulting from FETT repeal. The adjustments corresponded to a reduction in business sector costs of 30 cents for every dollar that would have been collected in federal estate transfer taxes. This ratio is based on previous research cited by former DRI/McGraw-Hill economists Richard Fullenbaum and Mariana McNeill.³¹
- **Corporate AAA Bond Rate.** MIT economist James M. Poterba estimated in a 2000 study that eliminating wealth transfer taxes would reduce the required yield on investment by at least 1.3 percent.³² CDA analysts lowered the corporate AAA bond rate within the model in order to reflect this 1.3 percent reduction.
- **Federal Non-Defense Spending Variables.** CDA economists adjusted federal spending in order to compensate for the projected changes in federal collections resulting from FETT repeal. This adjustment assured that the tax policy reform would not cause a substantial change in cumulative federal deficits during the forecast period. The adjusted variables controlled direct federal non-defense spending and federal grants-in-aid to state and local governments.

28. Readers interested in replicating this analysis should contact the author for further information on how the model was applied.

29. Beach, “The Case for Repealing the Estate Tax,” p. 26.

30. NIPA stands for National Income and Product Accounts.

31. Fullenbaum and McNeill, “The Effects of the Federal Estate and Gift Tax on the Aggregate Economy,” pp. A1 and A2. These two authors cited four sources for this estimate. The first estimate, by Guest and Associates, L.L.C., was based upon survey data to find the amount that estate holders spent on federal estate tax planning and preparation during 1995; this amount was compared with 1995 FETT collections and yielded a ratio of 30 percent. The second estimate was based upon calculations for FETT compliance costs by Kennesaw State University scholars Joseph Astrachan and Craig Aranoff; the cost was divided by an annual FETT collection total, resulting in a ratio of 32 percent. The third estimate was from Christopher E. Erblich of the Tax and Estate Planning Practice Group, who calculated both compliance and economic disincentive costs resulting from the U.S. federal tax system; Erblich’s amount was divided by an annual total for FETT collection, yielding a ratio close to 31.2 percent. Finally, CDA economist William W. Beach provided an estimate of the 1995 cost of compliance with FETT that, when compared to 1995 FETT collections, resulted in a ratio of 29.8 percent.

32. Poterba, “Estate Tax and After-Tax Investment Returns,” p. 339.

How Immediate and Permanent Estate Tax Repeal on January 1, 2003, Would Affect Selected Economic Indicators Without Additional Tax Reform

Economic Indicator	(Fiscal Year End) ¹										(Average) 2003-2012	
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011		2012
Gross Domestic Product												
With Immediate Repeal	\$9,364.8	\$9,637.9	\$9,956.4	\$10,271.9	\$10,597.4	\$10,937.4	\$11,287.9	\$11,650.3	\$12,014.2	\$12,387.7	\$12,763.1	\$11,150.4
Current Law	9,364.8	9,634.2	9,949.2	10,262.4	10,587.3	10,926.8	11,276.3	11,638.0	12,001.4	12,373.8	12,748.4	11,139.8
Difference	0.0	3.7	7.2	9.5	10.1	10.6	11.6	12.3	12.8	13.9	14.7	10.6
Total Employment												
With Immediate Repeal	130,784	132,699	135,023	136,738	138,017	139,459	141,051	142,379	144,268	146,181	148,128	140,394
Current Law	130,784	132,674	134,929	136,631	137,904	139,352	140,938	142,258	144,148	146,060	148,010	140,290
Difference	0	25	94	107	113	107	113	121	120	121	118	104
Total Unemployment												
With Immediate Repeal	8,580	8,526	8,010	7,721	7,861	7,938	8,008	8,070	8,135	8,184	8,194	8,065
Current Law	8,580	8,515	8,017	7,724	7,870	7,946	8,023	8,092	8,158	8,211	8,221	8,078
Difference	0	11	-7	-3	-9	-8	-15	-22	-23	-27	-27	-13
Disposable Personal Income												
With Immediate Repeal	\$7,033.1	\$7,244.1	\$7,393.0	\$7,515.1	\$7,690.9	\$7,883.0	\$8,095.2	\$8,322.7	\$8,529.5	\$8,690.1	\$8,893.8	\$8,025.7
Current Law	7,033.1	7,238.8	7,383.8	7,504.8	7,680.5	7,872.3	8,084.1	8,311.1	8,518.0	8,678.7	8,882.8	8,015.5
Difference	0.0	5.3	9.2	10.3	10.4	10.7	11.1	11.6	11.5	11.4	11.0	\$10.3
Disposable Income Per Capita												
With Immediate Repeal	\$25,178	\$25,726	\$26,043	\$26,258	\$26,662	\$27,112	\$27,615	\$28,158	\$28,625	\$28,924	\$29,360	\$27,448
Current Law	25,178	25,707	26,010	26,222	26,626	27,075	27,577	28,119	28,587	28,886	29,324	27,413
Difference per Person	0	19	33	36	36	37	38	39	38	38	36	35
Difference for Family of Four	0	76	132	144	144	148	152	156	152	152	144	140
Non Residential Investment												
With Immediate Repeal	\$1,182.7	\$1,260.1	\$1,412.6	\$1,504.7	\$1,594.6	\$1,702.8	\$1,817.8	\$1,947.6	\$2,078.8	\$2,220.0	\$2,369.9	\$1,790.9
Current Law	1,182.7	1,258.9	1,410.9	1,502.4	1,591.9	1,699.6	1,813.8	1,943.1	2,073.4	2,213.4	2,362.6	1,787.0
Difference	0.0	1.2	1.7	2.3	2.7	3.2	4.0	4.5	5.4	6.6	7.3	3.9
Net Capital Stock - Nonresidential												
With Immediate Repeal	\$9,688.6	\$9,999.6	\$10,416.0	\$10,908.4	\$11,441.1	\$12,025.6	\$12,666.6	\$13,368.5	\$14,135.4	\$14,973.5	\$15,894.5	\$12,582.9
Current Law	9,688.6	9,998.9	10,413.8	10,904.3	11,435.0	12,017.4	12,655.9	13,354.8	14,118.5	14,952.8	15,869.4	12,572.1
Difference	0.0	0.7	2.2	4.1	6.1	8.2	10.7	13.7	16.9	20.7	25.1	10.8
User Cost of Capital												
With Immediate Repeal	97.4	101.6	104.2	103.5	104.3	105.1	105.8	106.5	106.7	106.9	107.4	105.2
Current Law	97.4	101.9	104.4	103.7	104.4	105.4	106.1	106.8	107.1	107.5	107.7	105.5
Difference	0.0	-0.3	-0.2	-0.2	-0.1	-0.3	-0.3	-0.3	-0.4	-0.6	-0.3	-0.3

Continued

Index: 100 = 2nd quarter 1999

How Immediate and Permanent Estate Tax Repeal on January 1, 2003, Would Affect Selected Economic Indicators Without Additional Tax Reform

More Economic Indicators	(Fiscal Year End) ¹							(Average) 2003-2001					
	2002	2003	2004	2005	2006	2007	2008		2009	2010	2011	2012	
Consumer Price Index													
With Immediate Repeal	1.6%	2.4%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%
Current Law	1.6%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%
Difference	0.0%	-0.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Treasury Bill, 3 Month													
With Immediate Repeal	1.6%	3.1%	5.0%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.7%
Current Law	1.6%	3.1%	5.0%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.7%
Difference	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Treasury Bond, 10 Year													
With Immediate Repeal	4.9%	5.5%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%
Current Law	4.9%	5.5%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%
Difference	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net Publicly Held Federal Debt													
With Immediate Repeal	\$3487.8	\$3679.1	\$3816.0	\$3878.0	\$3885.5	\$3851.1	\$3778.0	\$3658.4	\$3486.5	\$3162.4	\$2652.3	\$3584.7	
Current Law	3487.8	3676.0	3805.0	3862.0	3865.0	3829.0	3757.0	3639.0	3476.0	3167.0	2658.0	3573.4	
Difference	0.0	3.1	11.0	16.0	20.5	22.1	21.0	19.4	10.5	- 4.6	- 5.7	11.3	
Net Publicly Held Federal Debt Share													
With Immediate Repeal	33.8%	34.1%	33.7%	32.5%	30.9%	29.1%	27.1%	24.9%	22.5%	19.4%	15.5%	27.0%	
Current Law	33.8%	34.1%	33.6%	32.4%	30.7%	28.9%	26.9%	24.7%	22.4%	19.4%	15.5%	26.9%	
Difference	0.0%	0.0%	0.1%	0.1%	0.2%	0.2%	0.2%	0.2%	0.1%	0.0%	0.0%	0.1%	
Consumption Expenditures													
With Immediate Repeal	\$6,629.5	\$6,793.3	\$6,982.7	\$7,208.8	\$7,430.7	\$7,637.1	\$7,854.6	\$8,092.8	\$8,333.7	\$8,595.5	\$8,858.1	\$7,778.7	
Current Law	6,629.5	6,791.5	6,979.1	7,203.9	7,425.1	7,631.0	7,848.0	8,085.9	8,326.6	8,588.3	8,850.9	7,773.0	
Difference	0.0	1.8	3.6	4.9	5.6	6.1	6.6	6.9	7.1	7.2	7.2	5.7	
Personal Savings													
With Immediate Repeal	\$204.0	\$243.9	\$193.6	\$77.9	\$14.8	-\$15.3	-\$33.8	-\$54.6	-\$96.5	-\$201.3	-\$266.5	-\$13.8	
Current Law	204.0	240.4	188.2	72.7	9.9	-19.8	- 38.3	-59.0	-100.8	-205.4	-270.2	-18.2	
Difference	0.0	3.5	5.0	5.2	4.9	4.5	4.5	4.4	4.3	4.1	3.7	4.5	

Continued

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Table 2 - continued

How Immediate and Permanent Estate Tax Repeal on January 1, 2003, Would Affect Selected Economic Indicators Without Additional Tax Reform

Federal Budget Indicators	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2003-2012 (Total)
							(Fiscal Year End) ¹					
Federal Tax Revenue							In Billions of Dollars*					
With Immediate Repeal	\$1,880.6	\$1,953.0	\$2,077.4	\$2,241.7	\$2,382.3	\$2,523.9	\$2,668.6	\$2,818.5	\$2,986.4	\$3,263.4	\$3,518.8	\$26,434.0
Current Law	1,880.6	1,956.0	2,081.0	2,241.0	2,383.0	2,519.0	2,663.0	2,813.0	2,970.0	3,245.0	3,525.0	26,396.0
Difference	0.0	-3.0	-3.6	0.7	-0.7	4.9	5.6	5.5	16.4	18.4	-6.2	38.0
Change in Federal Tax Revenue Under Repeal							In Billions of Dollars					
Static Estimate	\$0.0	-\$3.9	-\$4.8	-\$0.4	-\$1.8	\$3.8	\$4.6	\$4.5	\$15.6	\$17.8	-\$6.8	\$28.7
Dynamic Estimate	0.0	-3.0	-3.6	0.7	-0.7	4.9	5.6	5.5	16.4	18.4	-6.2	38.0
Revenue Feedback	0.0	0.9	1.2	1.1	1.1	1.1	1.0	1.0	0.8	0.6	0.6	9.3
Feedback Percent	--	--	31.6%	22.7%	287.3%	58.6%	25.9%	21.0%	17.8%	3.8%	3.4%	32.6%
Federal Spending							In Billions of Dollars*					
With Immediate Repeal	\$2,031.9	\$2,108.1	\$2,198.2	\$2,287.2	\$2,372.4	\$2,467.3	\$2,577.2	\$2,682.8	\$2,795.3	\$2,926.3	\$3,007.1	\$25,421.9
Current Law	2,031.9	2,105.0	2,194.0	2,283.0	\$2,368.0	2,463.0	2,573.0	2,679.0	2,792.0	2,924.0	3,005.0	25,386.0
Difference	0.0	3.1	4.2	4.2	4.4	4.3	4.2	3.8	3.3	2.3	2.1	35.9
Federal Surplus/Deficit							In Billions of Dollars*					
With Immediate Repeal	-\$151.3	-\$155.1	-\$120.7	-\$45.5	\$9.9	\$56.5	\$91.4	\$135.6	\$191.1	\$337.1	\$511.7	\$1,012.0
Current Law	-151.3	-149.0	-113.0	-42.0	15.0	56.0	90.0	134.0	178.0	321.0	520.0	1,010.0
Difference	0.0	-6.1	-7.7	-3.5	-5.1	0.5	1.4	1.6	13.1	16.1	-8.3	2.0
Federal Net Interest Paid							In Billions of Dollars*					
With Immediate Repeal	\$212.9	\$209.1	\$238.4	\$258.8	\$266.1	\$268.2	\$268.1	\$265.9	\$260.5	\$251.6	\$236.4	\$2,523.1
Current Law	212.9	209.0	238.0	258.0	265.0	267.0	267.0	265.0	260.0	252.0	237.0	2,518.0
Difference	0.0	0.1	0.4	0.8	1.1	1.2	1.1	0.9	0.5	-0.4	-0.6	5.1

Note: 1. All rows without asterisk denote fiscal year end.
 *Denotes a four-quarter average calculated at fiscal year end.
 Some figures may not sum due to rounding.
 Source: Center for Data Analysis at The Heritage Foundation.