Order Code RS20853
Updated July 14, 2003



# State Estate and Gift Tax Revenue

Steven Maguire
Economic Analyst
Government and Finance Division

## Summary

P.L. 107-16, the Economic Growth and Tax Relief Reconciliation Act of 2001, repeals the federal estate tax for decedents that die in 2010. In addition, the Act repeals the credit for state estate taxes for decedents dying after December 31, 2004 and replaces the credit with a deduction. In most states, the repeal of the tax and the significant increase in the federal exclusion, will also repeal or diminish state estate, inheritance, and gift taxes. Some state budgets depend on the estate tax more than others. As a percentage of total tax revenue collected from FY1992 to FY2002, state estate tax contributions ranged from 0.16% in Alaska to 3.62% in New Hampshire. As of June 2003, 29 states, including Alaska and New Hampshire, will have estate taxes that will be repealed in 2005 when the federal "credit for state death taxes" is changed to a deduction. This report will be updated as events warrant.

The federal estate tax will be repealed gradually by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). Repeal of the federal estate tax and increase of the exclusion amount (or its credit equivalent) as prescribed by EGTRRA will also repeal or diminish most state estate, inheritance, and gift taxes.[1] In FY2002, state estate and gift tax revenue was 1.38% of total state tax revenue, but there was considerable variation among the states.[2] This report will briefly describe the federal credit for state estate taxes and provide data on the relative importance of estate, inheritance, and gift taxes to each state and the District of Columbia.

[1] For the remainder of the report, all state taxes that are triggered by death will be referred to as "state estate taxes." Thus, "state estate taxes," will included state inheritance taxes, succession taxes, and estate taxes.

[2] U.S. Census Bureau, Governments Division, *State Government Tax Collections*, Web site [http://www.census.gov/govs/statetax/0200usstax.html] visited July 1, 2003.

## Background

The federal credit for state estate taxes first appeared in the Revenue Act of 1924, some eight years after the introduction of the federal estate tax. The Act stipulated that estates could claim a credit for state estate taxes up to 25% of the federal estate tax liability. After numerous modifications since its introduction, the federal credit is now a schedule of 21 gradually increasing rates beginning at 0% and eventually reaching 16%.[3] The rates are levied on the value of the net federal estate[4] less a $60,000 exemption (the remainder is called the adjusted taxable estate). The top credit rate of 16% applies to adjusted taxable estate values over $10,040,000.

**Changes under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).** Because many state tax codes are linked directly to federal tax code, changes in federal law also affect the state tax codes. Two parts of EGTRRA affect the tax revenue generated by state estate taxes. First, EGTRRA phases out the federal credit for state death taxes for deaths occurring before December 31, 2004 and replaces the credit with a deduction beginning in 2005. The phase-out began in 2002 when the credit was reduced by 25%; by 50% in 2003; and by 75% in 2004. In 2005, when estates deduct state estate taxes, the value of the deduction (in terms of reduced tax liability) is the top marginal federal estate tax rate (45% or 47%) multiplied by state estate taxes paid. In contrast, before EGTRRA, the value of the credit was 100%, or it reduced federal tax liability dollar-for-dollar. Thus, post-EGTRRA, state estate taxes impose a "real" tax liability or burden.

In addition, the applicable exclusion amount for federal estate taxes increased to $1 million for 2002 and 2003 and to $1.5 million in 2004. The increase in the applicable exclusion amount is important to many states because it also serves as the filing threshold for the federal estate tax. Some states require estates to file a *state* return only when a federal return is required. If fewer federal estate tax returns are filed then fewer state estate tax returns would be filed.

States could avoid losing revenue by decoupling from the federal tax code, as some have since EGTRRA became law. However, the changes enacted by EGTRRA will necessarily create state estate tax burdens if states decouple from the federal tax code and collect estate tax revenue. The next section provides data on state estate tax revenue as reported by the U.S. Census Bureau. The contribution of the estate tax to a state's finances may well influence the decision about decoupling.

For more information on the federal estate tax and the credit equivalent, see CRS Report RL30600, *Estate and Gift Taxes: Economic Issues*, by Jane Gravelle and Steven Maguire. For more background on the interdependence of federal and state taxes, see CRS Report RL30817, *Federalism Through Tax Interdependence: An Overview*, by Steven Maguire.

---

[3] The "Federal Credit of State Death Taxes" is 26 U.S.C. 2011.

[4] The "net federal estate" is the estate less funeral expenses, etc.

## State Estate and Gift Tax Revenue

States generally impose a death-triggered tax in one of two ways. The majority of states and the District of Columbia pick up the federal credit for state estate taxes as described above. Others collect an independent inheritance (or succession tax) and in most cases impose an additional estate tax to absorb any remaining federal credit. The following explanation of the Florida estate tax, which is an exclusively "pick up" state, appears on the Florida Department of Taxation official website:[5]

> Florida's estate tax system is commonly referred to as a "pick up" tax. Florida picks up all or a portion of the credit for state death taxes allowed by the federal government. Under this system, Florida estate tax is not due unless an estate is required to file a federal estate tax return.

In states with estate tax laws similar to Florida's, the state estate tax will be repealed when the federal credit is repealed. Those states are identified in Table 1 by a "no" in the column reporting the existence of state estate taxes in 2005.

In contrast, the states that impose an independent estate tax will lose only the portion of their estate tax that relies on the existence of the federal credit.[6] In these states, the law is usually constructed to pick-up any federal estate tax credit remaining after a state estate tax is imposed. Generally, if the maximum *federal* credit for state death taxes for the estate is greater than the estate tax due to the state, the state law directs the executor of the estate to remit the difference to the state. The state has effectively "sponged-up" the remaining federal credit. The potential revenue loss from federal repeal will likely be smaller in these states relative to states with only the dependent tax.

For example, Pennsylvania maintains an inheritance tax which is applied with graduated rates and depends on the relationship of the heir to the decedent (lower rates for closer relatives). After paying the inheritance tax, a separate estate tax is then imposed to "sponge-up" the remainder. Pennsylvania describes the "sponge" tax on its official website as:[7]

> a "pick-up" tax imposed to absorb the maximum amount of credit allowed by federal estate tax law toward state death taxes. For residents, the estate tax represents the difference between the Pennsylvania inheritance tax plus death taxes paid to other states and the maximum federal credit for state taxes allowed by federal estate tax law.

When the estate tax is repealed, taxpayers in the states like Pennsylvania with stand-alone estate taxes would lose the federal credit along with the federal liability. However, the state inheritance tax would still generate tax revenue. Because of this, political pressure to repeal state inheritance taxes upon repeal of the federal estate tax might be greatest in states with an independent inheritance tax like Pennsylvania's. States with

---

[5] The citation is from the website: [http://sun6.dms.state.fl.us/dor/taxes/estate_tax.html], site visited July 1, 2003.

[6] For more, see Federation of Tax Administrators Bulletin, *Repeal of Federal Estate Tax Would Have Effect on States*, Feb. 22, 2001, Washington, D.C.

[7] The site is [http://www.revenue.state.pa.us/revenue/cwp/view.asp?a=3&Q= 69002&subID=I].

laws similar to Pennsylvania's and states that link to the federal tax code as it existed on a specific date (most often a date predating passage of EGTRRA) are identified in Table 1 with a "yes" in the column reporting the existence of state estate taxes in 2005.

## Table 1. State Death and Gift Tax Revenue: Average for 1992 to 2002

| State | State Revenue from Estate and Gift Tax 1992 to 2002 Average (in $000s) | Estate and Gift Taxes as Percentage of Total Tax Revenue 1992 to 2002 Average | State Estate Tax in 2005 | Reliance on Estate and Gift Taxes Rank |
|---|---|---|---|---|
| Alabama | 45200 | 0.008 | no | 33 |
| Alaska | 2136 | 0.0016 | no | 50 |
| Arizona | 61233 | 0.0088 | no | 31 |
| Arkansas | 31153 | 0.0079 | no | 34 |
| California | 709395 | 0.0108 | no | 24 |
| Colorado | 52074 | 0.0093 | no | 30 |
| Connecticut[a] | 230180 | 0.0282 | yes | 4 |
| Delaware | 34478 | 0.0197 | no | 8 |
| Dist. of Columbia[b] | 38915 | 0.0139 | yes | n/a |
| Florida | 518516 | 0.0242 | no | 5 |
| Georgia | 87215 | 0.0077 | no | 35 |
| Hawaii | 19807 | 0.0064 | no | 40 |
| Idaho | 12576 | 0.0064 | no | 41 |
| Illinois | 240084 | 0.0125 | no | 18 |
| Indiana | 120645 | 0.0138 | yes | 14 |
| Iowa | 84621 | 0.0187 | yes | 9 |
| Kansas | 67206 | 0.0166 | yes | 11 |
| Kentucky | 82980 | 0.0126 | yes | 17 |
| Louisiana[c] | 70889 | 0.0127 | no | 16 |
| Maine | 23200 | 0.0101 | no | 27 |
| Maryland | 120155 | 0.0134 | yes | 15 |
| Massachusetts | 212788 | 0.0169 | yes | 10 |
| Michigan | 129572 | 0.0074 | no | 36 |
| Minnesota | 48662 | 0.0044 | yes | 49 |
| Mississippi | 18357 | 0.0045 | no | 48 |
| Missouri | 91462 | 0.012 | no | 20 |
| Montana | 15237 | 0.0118 | no | 21 |
| Nebraska[d] | 14828 | 0.0058 | yes | 43 |
| Nevada | 33859 | 0.0108 | no | 23 |
| New Hampshire | 41661 | 0.0362 | no | 1 |
| New Mexico | 15168 | 0.0046 | yes | 46 |
| New York | 849286 | 0.0234 | no | 6 |

| State | State Revenue from Estate and Gift Tax 1992 to 2002 Average (in $000s) | Estate and Gift Taxes as Percentage of Total Tax Revenue 1992 to 2002 Average | State Estate Tax in 2005 | Reliance on Estate and Gift Taxes Rank |
|---|---|---|---|---|
| New Jersey | 358949 | 0.0229 | yes | 7 |
| North Dakota | 4755 | 0.0046 | no | 47 |
| North Carolina | 136586 | 0.0108 | no | 26 |
| Ohio | 109702 | 0.0066 | yes | 39 |
| Oklahoma | 73134 | 0.0145 | yes | 12 |
| Oregon | 40779 | 0.0087 | yes | 32 |
| Pennsylvania | 656508 | 0.0334 | yes | 2 |
| Rhode Island | 20076 | 0.0113 | yes | 22 |
| South Carolina | 36673 | 0.0068 | no | 38 |
| South Dakota | 24538 | 0.0318 | no | 3 |
| Tennessee | 72434 | 0.0108 | yes | 25 |
| Texas | 226492 | 0.0095 | no | 29 |
| Utah | 18272 | 0.0055 | no | 44 |
| Vermont | 12613 | 0.0124 | yes | 19 |
| Virginia | 100538 | 0.0097 | yes | 28 |
| Washington | 68375 | 0.006 | yes | 42 |
| West Virginia | 15697 | 0.0054 | no | 45 |
| Wisconsin | 71983 | 0.0069 | yes | 37 |
| Wyoming | 11772 | 0.0138 | no | 13 |

**Sources:** U.S. Bureau of Census, State Government Tax Collections: 1992-2002; and author's calculations.

The following table notes are from Federation of Tax Administrators Bulletin, *Repeal of Federal Estate Tax Would Have Effect on States*, Feb. 22, 2001, Washington, D.C.

[a]Connecticut is phasing out its inheritance tax; under current law, the state will move to a pick-up only tax in 2005.
[b]The District of Columbia tax data are from its FY2004 proposed budget and may not be directly comparable to the Census data used for the states.
[c]Louisiana is phasing out its inheritance tax; under current law, the state will move to a pick-up tax in 2004.
[d]Nebraska counties impose and collect a separate inheritance tax.

In addition to providing information about the existence of the state estate tax in 2005, Table 1 also provides data on the relative importance of estate and gift taxes to each state using the average tax revenue generated by state estate taxes from FY1992 to FY2002. The average annual revenue over 11 years is provided because state estate tax revenue fluctuates significantly from year to year. The fluctuation is greatest in less populated states where the death of one very wealthy resident would significantly affect revenue collected. The final column in Table 1 reports the relative rank of states based upon their reliance on state estate and gift taxes.

In addition to year-to-year fluctuations within states, there is considerable variation among the states in proportion of the total state tax revenue accounted for by the estate tax. In Alaska, the pick-up estate tax amounts to only 0.16% of tax revenues. In New Hampshire, on the other hand, the state's independent inheritance tax contributes 3.62% of the state's total tax revenues.

The anticipated revenue loss generated by repeal of the federal estate tax could be approximated by revenue collected in the states that will not have any type of state estate tax in 2005. In contrast, the estate and gift tax revenue collected in states with an independent estate tax would not accurately predict the potential revenue loss from repeal or reform of the federal estate tax.[8]

[8] For more on the federal estate tax and the effect of its repeal would have on specific states, see the following: Federation of Tax Administrators Bulletin, *State Responses to Changes Enacted as Part of EGTRRA*, Oct. 24, 2002, Washington, D.C. The report is available on the following Web site: [http://www.taxadmin.org/fta/rate/Estatetax.html].