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BACK FROM THE DEAD: STATE ESTATE TAXES AFTER THE FISCAL CLIFF

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ABSTRACT

Historically, the federal estate tax provided a credit for state estate and inheritance taxes. This credit, which offset dollar-for-dollar up to 16 percent of an estate's value against federal taxes, gave states a strong incentive to impose estate or inheritance taxes: states could raise revenue without increasing the net tax burden on their citizens. As a result, all 50 states and the District of Columbia had such taxes directly linked to the maximum value of the credit. The 2001 tax act phased out the credit and replaced it in 2005 with a less-valuable deduction. States responded in three different ways. Some simply repealed their estate taxes. Others decoupled from the federal law, either establishing a stand-alone tax or explicitly linking their taxes to the 2001 law. But most states did nothing, effectively eliminating their estate taxes but leaving in place the legislation that set their estate tax equal to the federal credit. If the 2001–10 tax cuts expire as scheduled on January 1, 2013, the federal estate tax will revert to its 2001 status, bringing back the credit and, with it, the estate taxes of the latter group of states. As a result, 30 states will resume collecting estate taxes, boosting their revenue by about $3 billion in 2013. Whether the state credit revives, the recent history of the federal estate tax highlights both the interrelationship between the federal and state tax systems and the uncertainty federal temporary actions create for taxpayers and other levels of government.

BACK FROM THE DEAD: STATE ESTATE TAXES AFTER THE FISCAL CLIFF

Absent legislative action, the United States will go over the "fiscal cliff" at the end of 2012, simultaneously cutting federal spending and allowing a host of temporary tax cuts to expire (Williams et al. 2012). The Congressional Budget Office (2012) projects that the expiration of tax cuts, combined with the reduction in spending, will cause the U.S. economy to contract in the first half of 2013. This contraction will reduce state tax revenues that are only just beginning to recover from the recession. While going over the fiscal cliff can affect states in many ways (Pew Fiscal Federalism Initiative 2012), one aspect of the sunset of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the 2010 Act) may help fill state coffers: the transfer of revenue from the federal government caused by the resurrection of the federal credit for state inheritance and estate taxes.[1]

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) phased out the federal estate tax and repealed it entirely in 2010.[2] As noted by Burman, Lim, and Rohaly (2008), few analysts believed the federal government would actually allow the estate tax to be fully repealed, but, right on schedule in 2010, the tax was gone. EGTRRA, however, was set to expire at the end of that year and thus to restore the estate tax, along with many other tax provisions, to the pre-2001 law.

The 2010 Act extended EGTRRA and most other tax law changes passed between 2001 and 2009 until the end of 2012. The 2010 Act did not, however, extend the repeal of the estate tax but instead reinstated the estate tax for 2011 and 2012 with a higher exclusion and a lower tax rate. These provisions are scheduled to sunset on January 1, 2013, raising the top federal tax rate from 35 percent to 55 percent and dropping the exclusion from $5.12 million to $1 million (Williams et al. 2012, 5; see box 1 of this paper for terminology).[3] Reverting to the higher rate and lower exclusion of the 2001 estate tax law would boost federal revenue by an estimated $31 billion in 2013 (Williams et al. 2012, 12).

For many states, however, a more important factor will be the return of the "credit for state death taxes" (CSDT).[4] The CSDT applied to estate and inheritance taxes paid to states, setting the credit on a graduated schedule up to 16 percent of the base value of the estate (appendix A). Estates could claim the credit against federal unified estate and gift taxes

The CSDT gave states a strong incentive to impose their own estate or inheritance taxes. As long as those taxes did not exceed the maximum credit, they could raise revenue without

[1] This report examines only one aspect of how going over the fiscal cliff will affect states. For a broader discussion of the effect of going over the fiscal cliff on states see Pew Fiscal Federalism Initiative (2012).
[2] The estate tax change in EGTRRA was just one component of the Act (TPC 2012, I-11-4).
[3] The 2010 Act indexed the exclusion from the 2011 amount of $5 million in 2012.
[4] This is the official name in the US Code: "26 USC § 2011 - Credit for State death taxes" and was used to recognize the variety in state taxes which included inheritance, succession, legacy, and estate taxes.

Box 1: Glossary

***Estate tax**: A tax levied on a person's estate at the time of his or her death.*

***Inheritance tax**: A tax levied on the value of property inherited by a taxpayer. The tax rate typically depends on the relationship of the taxpayer to the decedent, with higher rates on more distant and non-relatives.*

***Gift tax**: A tax levied on gifts in excess of an exempt amount. That amount is $13,000 in 2012. Spouses can each give this amount to any number of individual beneficiaries. Gifts can be transfer of tangible or intangible property including transfers that are part of a sales transaction. Gifts to resident spouses are not taxed.*

***Exclusion:** The basic exclusion is a filing threshold. Although referred to as an exclusion, on the tax return it is referred to as the unified credit, which is equivalent to the tax on the exclusion threshold. In 2012, the unified credit of $1,772,800 excluded $5.12 million of value from the gross estate. The credit is "unified" because it applies to both estates and gifts and relates to the unified estate and gift tax.*

***2010 Act**: The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, enacted in December 2010, extended most of the 2001–09 tax cuts, and reinstated the estate tax (which had been repealed in 2010) with a larger effective exclusion and a lower tax rate.*

***EGTRRA:** The Economic Growth and Tax Relief Reconciliation Act of 2001 reduced most tax rates, doubled the child tax credit and made it partially refundable, expanded tax-free retirement savings, reduced marriage penalties, increased the child and dependent care tax credit, and phased out the estate tax, among other changes.*

Sources: IRS, Tax Policy Center

increasing the total tax burden on estates and heirs. These taxes will return in 2013 if Congress does not change the law. In part to help pay for tax cuts, EGTRRA phased the CSDT out and replaced it with a less valuable deduction in 2005. That allowed the federal government to capture much of the revenue that states had previously collected (table 1).

When Congress enacted EGTRRA, the Joint Committee on Taxation estimated that the estate tax provisions would reduce federal revenues by $133 billion over 10 years; 40 percent of that cost was from the one-year repeal of the estate tax for 2010 decedents (JCT 2003, 71). That cost was held down by the changed treatment of state estate and inheritance taxes.[5] However, the change also complicated state-level taxes by moving from federal rules that strongly encouraged states to piggyback on the federal policy to rules that could affect states differently.

[5] Duncan (2002) framed the issue well: "The effect of the phase-out was also to transfer revenue from states to the federal government during the period of the phase-out, thus allowing greater federal tax reductions than would otherwise have been possible." At the time, Duncan was referring to the period when the CSDT was being phased out. After the phaseout, the transfer continued when the deduction replaced the CSDT (table 1). The original bill, H.R. 8, which was folded into EGTRRA, only required the credit be scaled down proportionately to the reduction in the top tax rate rather than the complete repeal of the credit and replacing it with a deduction (H.R. 8 of the 107th Congress, "Death Tax Elimination Act of 2001"). Somewhere in the final negotiations of EGTRRA, this benefit to the states was used to reduce the total price tag.

If Congress fails to act and the 2010 Act sunsets in 2013, the federal credit will be restored. The many states whose laws explicitly reference the federal credit will automatically resume collecting their estate and inheritance taxes. That situation poses planning problems for affected states. Should these "dormant" states anticipate the return of the CSDT and the resultant additional revenue? Or will they ignore that source of revenue, assuming that it is gone for good? These issues illustrate how the introduction of temporary federal tax measures, and their subsequent expiration or extension, increase the budgeting uncertainty imposed on states.

With the fiscal cliff a few months away, state revenue analysts are worried about the consequences of continued federal gridlock on their states' revenues. Colorado, New Mexico, Oregon, Washington, and the District of Columbia all recently updated their revenue estimates, and all mentioned the "fiscal cliff" or otherwise cited the federal budget crisis as a risk in the revenue estimate narrative. (Colorado 2012; Walker-Moran, Van Moorsel, and Smith 2012; Oregon 2012; Washington 2012; District of Columbia 2012). New Mexico specifically noted that the return to 2001 federal estate tax law is a positive risk to its revenue estimate. In the face of budget cuts from federal grants and an uncertain economy that will affect the major revenue sources, states that begin putting together the 2014 budget this fall may look at this federal credit as a budget balancer, as California did the last time the credit was supposed to come back in 2010 (California 2010, 79). But the uncertain fate of the CSDT and other federal provisions affecting states makes it more difficult for the states to plan and budget.

HISTORY OF FEDERAL ESTATE TAX AND CSDT

Following several temporary federal estate taxes used to finance wars, the modern federal estate tax was enacted in 1916 and expanded to include a gift tax in 1924 (Jacobson 2012). Gift taxes are taxes on transfers between individuals. The 1924 law mandated that gifts given while the taxpayer was alive would be included in—and taxed as part of—the estate, but it also provided that any taxes paid on those gifts would directly reduce estate tax liability (Jacobson 2012). The law also allowed a state tax credit equal to 25 percent of the federal tax as a political compromise to share the estate tax with the states and make it more consistent across states (Joulfaian 2012). The Internal Revenue Act of 1954 changed the credit from a percentage of the federal tax to the "credit for state death taxes" of up to 16 percent of the estate's value.

Before EGTRRA, every state and the District of Columbia imposed an estate tax equal to the CSDT.[6] Federally, estates could claim a credit for state estate and inheritance taxes according to a progressive schedule with a top rate of 16 percent of the taxable value of the estate (appendix A).[7] In effect, the credit transferred revenues from the federal estate tax to states that

[6] Some states also had inheritance taxes separate from the estate tax.
[7] The credit was allowed only if the estate had paid state estate or inheritance taxes.

had estate or inheritance taxes.[8] This is often referred to as a "pick-up" tax—states capture the amount of the credit rather than the federal government. State death taxes did not increase the tax paid by estates as long as they did not exceed the maximum credit. States thus shared the revenue up to the amount of the CSDT. This provision made the estate tax across the states effectively uniform—at the maximum rate—which simplified the tax faced by estates with property in multiple states.

Most states had virtually identical language setting the amount of state tax liability at the maximum amount of the federal credit. For example, the North Dakota statute explicitly sets the amount of tax as equal to the maximum allowed federal credit (box 2).

Some states also had an inheritance tax, and for these states the estate tax was a "sponge" tax to maximize or soak up any federal credit left after credit claimed for the inheritance tax. For example, Iowa's statute sets the estate tax equal to the federal credit in 451.2(1), offset by a credit for inheritance tax paid (box 2).

Box 2: Sample of State Statutes before EGTRRA

North Dakota: ND Cent. Code 57-37.1-04 (Dormant State)

> 1. The amount of tax imposed upon the transfer of the North Dakota taxable estate must be equal to the maximum tax credit allowable for state death taxes against the federal estate tax imposed with respect to a decedent's estate which has a taxable situs in this state.

Iowa: Title X.3.451.2 Iowa Law 2011 (Dormant State but had inheritance tax)

> 1. An amount equal to the federal estate tax credit for state inheritance and estate taxes as allowed in the Internal Revenue Code is imposed upon every transfer of the net estate of every decedent being a resident of, or owning property in, this state.
>
> …
>
> 3**. The total tax or the Iowa share of the total tax shall be credited with the amount of any inheritance tax due the state of Iowa as provided in chapter 450**.

EGTRRA phased out the federal credit and replaced it with a deduction for state estate or inheritance taxes paid. That change cut off a revenue stream to states, shifting most of that revenue to the federal government. As a result, even with lower tax rates and the increased exclusion, the federal government received about the same net revenue from estate taxes.[9]

EGTRRA and the 2010 tax act sharply reduced both the number of estates subject to tax and the amount of estate tax revenue by 2011 (table 1). In 2000, estates filed 52,000 taxable

[8] This discussion omits other parts of the estate tax law that vary by state including marital exclusions and treatment of farm property.

[9] Federal estate tax revenue fell sharply in 2011 (when estates of people dying in 2010 filed estate tax returns) to just $3 billion, down from $25 billion in 2008. That revenue will rebound to some degree in 2012 and 2013.

returns reporting an aggregate gross estate value of $130.4 billion.[10] Subtracting deductions (primarily charitable and spousal transfers) and adding taxable gifts made after 1977 reduced the aggregate taxable value of estates to just over $100 billion. Applying progressive tax rates that ranged up to 55 percent yielded an aggregate before-credits tax of about $42 billion. That liability was reduced by two credits: the unified credit—$211,300, which effectively exempted $650,000 from tax per estate—and the CSDT.[11] Net of those credits, the federal estate tax collected $24.4 billion in 2000.

Over the next nine years, federal estate tax revenue was relatively constant, fluctuating between $21 billion and $25 billion, despite a more than five-fold increase in the effective exemption, a more than two-thirds drop in taxable estates, and a 10 percentage-point drop in the top tax rate. The tax maintained its value for two primary reasons: the average value of decedent's assets grew substantially, and replacing the CSDT with a deduction shifted between $4 billion and $5 billion a year from states to the federal government.[12] The CSDT was reduced by 25 percent a year in 2002, 2003, and 2004, and it was replaced by a deduction in 2005. Because many states did not decouple, their estate tax collections fell and the federal deduction dropped as well, helping maintain federal revenues.

Fewer than 7,000 estates paid estate taxes totaling $13 billion in 2010, and fewer than 1,500 paid just $3 billion the following year, reflecting the elimination on the estate tax for 2010 decedents. Return of the federal estate tax in 2011 will restore some lost revenue, but collections will not return to their levels of the early 2000s if Congress extends the tax at its 2012 level.

STATE RESPONSES TO EGTRRA

States responded in different ways to EGTRRA's replacement of the CSDT with a deduction. Some explicitly repealed their own estate taxes. Others that had estates taxes explicitly tied to the CSDT effectively did the same thing by doing nothing—with no federal credit, they collected no tax. Revenue fell for both groups of states, which meant that either they would have to cut spending or raise other taxes. Some states took different tacks, either decoupling from the federal law or adopting stand-alone estate taxes. In any case, the changes came at a particularly bad time for states when the 2001 recession was eroding state tax collections (Orszag 2003).

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[10] This discussion examines only taxable returns. Many returns have no federal tax liability but are filed because the estate paid state estate taxes or for other reasons.

[11] The unified credit is $155,800 plus the product of $150,000 (the amount the exclusion exceeds the $500,000 bracket) and 37 percent, or $211,300 in 1999. This is the tax on $650,000.

[12] The repeal of the credit saved the federal government about $6 billion; the deduction offset that by the deduction amount times the tax rate, or about $1.5 billion. The average taxable estate value was $2.5 million in 2000 and $7.5 million in 2008.

The different responses of states to repeal of the CSDT made computation of taxes more difficult for estates with property in more than one state. For 90 years, state estate taxes were based on the CSDT, which was uniform for all states and the District of Columbia. Because states responded differently, an estate with property in multiple states may owe estate taxes in some of or all those states and may face different rules and exemptions.

Table 1: Federal Estate Tax 2000–11, by Year Estate Tax Returns Filed

	2000	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**
Taxable returns	52,000	51,736	45,018	33,302	31,329	20,250	22,798	17,408	17,144	14,713	6,711	1,480
						Billions of dollars						
Gross estate value of taxable returns	130.4	123.9	117.5	112.0	108.5	104.0	116.1	112.1	128.2	102.0	69.2	19.8
Deduction for state estate and inheritance taxes	**-**	**-**	**-**	**-**	**-**	**(0.1)**	**(2.5)**	**(3.1)**	**(3.1)**	**(2.6)**	**(1.6)**	**(0.5)**
Other deductions	(34.9)	(29.8)	(33.0)	(30.6)	(26.7)	(28.7)	(28.7)	(30.3)	(38.9)	(26.3)	(19.8)	(7.2)
Taxable estate	95.5	94.1	84.4	81.5	81.7	72.7	84.9	78.7	86.1	73.1	47.7	12.1
Taxable estate plus previous gifts	100.8	99.0	89.9	87.7	87.7	80.6	90.7	84.5	92.6	79.0	52.1	13.4
Estate tax before credits	42.0	41.2	37.4	36.3	36.1	34.0	37.9	35.3	38.2	32.5	22.7	5.5
Unified credit	11.0	11.3	10.2	10.7	11.2	10.3	12.8	12.7	13.2	11.8	8.3	2.1
Credit for state estate and inheritance taxes	**6.4**	**6.2**	**5.7**	**4.7**	**3.1**	**1.8**	**0.3**	**-**	**-**	**-**	**-**	**-**
Other credits	0.2	0.1	0.2	0.1	0.1	0.2	0.1	0.1	0.2	0.1	-	-
Estate tax revenue	24.4	23.5	21.4	20.8	21.6	21.7	24.7	22.5	24.8	20.6	13.2	3.1
Addendum: Applicable Law - Assumes filing year is year after year of death												
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Maximum tax rate	55%	55%	55%	50%	49%	48%	47%	46%	45%	45%	45%	n.a.
Exclusion (000s)	655	675	675	1,000	1,000	1,500	1,500	2,000	2,000	2,000	3,500	n.a.

Source: IRS Statistics of Income Division
Notes: Estate tax returns must generally be filed within nine months following the decedent’s death. Returns filed in a given year therefore include mostly people who died the previous year but also include some who died during the year tax returns were filed. Because estates are subject to the tax provisions applicable in the year the decedent died, data for a given year reflect estate tax laws for multiple years. Detail may not sum to totals because of rounding.

When the CSDT was repealed, each state with language that explicitly linked to the credit by definition (like North Dakota, box 2) had to choose whether to change its statutes to retain the state-level tax—which would have increased the combined federal and state taxes on estates—or do nothing and lose revenue starting in 2002. States followed four different paths (box 3):

1. Dormant states without inheritance taxes retained pick-up taxes directly linked to the federal credit and therefore lost that source of revenue.

2. Dormant states with inheritance taxes kept those taxes in place but lost revenue from sponge estate taxes that previously collected up any excess of the maximum CSDT over the inheritance tax.
3. Decouple/stand-alone states maintained freestanding estate taxes, either as independent taxes or with explicit links to the pre-EGTRRA federal credit.
4. Repeal states repealed all references to estate taxes in their laws.

Box 3: Estate Tax Status by State

Dormant without inheritance tax: *25 states have laws similar to North Dakota's that explicitly reference the federal credit. Since the federal credit is gone, these states no longer have estate taxes.*

Alabama	Alaska	Arkansas	California	Colorado
Florida	Georgia	Idaho	Louisiana	Michigan
Mississippi	Missouri	Montana	Nevada	New Hampshire
New Mexico	North Dakota	South Carolina	South Dakota	Texas
Utah	Virginia	West Virginia	Wisconsin	Wyoming

Dormant with inheritance tax: *Five states have estate taxes similar to Iowa that equal to the maximum federal credit less any inheritance tax. These states collect inheritance taxes but no longer have estate taxes since the federal credit is gone.*

Indiana	Iowa	**Kentucky**	Pennsylvania	Tennessee

Decouple/stand alone: *15 states and the District of Columbia either have decoupled from current federal law by referring to pre-EGTRRA law (box 2) or have established stand-alone estate taxes independent of federal law. Maryland and New Jersey also have inheritance taxes.*

Connecticut	Delaware	Hawaii	Illinois	Maine
Maryland*	Massachusetts	Minnesota	New Jersey*	New York
North Carolina	Oregon	Rhode Island	Vermont	Washington
District of Columbia				

Repeal state: *five states have repealed all references to the estate tax. (Repeal dates in parentheses)*

Arizona (2006)	Kansas (2010)	Nebraska (2007)	Ohio (2010)	Oklahoma (2010)

Source: Tax Policy Center review of state statutes. See appendix C for more detail.

Repeal of the CSDT made it more attractive for states to vary other aspects of their inheritance or estate taxes. For example, 13 of the 15 states that decoupled have exclusions below $5 million; only Hawaii and North Carolina use the current federal exclusion—$5.12 million in 2012 (appendix C).

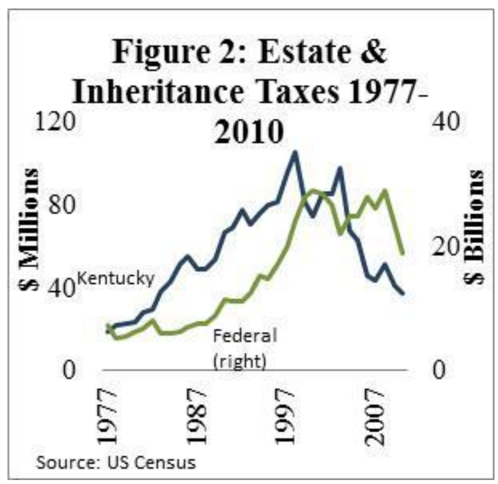
Detailed case studies of a sample state from each category illustrate how the different approaches work in practice.

Dormant state: New Mexico

New Mexico did not amend its estate law following the repeal of the CSDT. The state collected about $28 million in 2003—about 1 percent of total tax collections—on estates of people who died in 2001 and 2002. That revenue had all but disappeared by 2010 (figure 1).

The state levies "a tax in an amount equal to the federal credit… on the transfer of the net estate of every resident."[13] The federal credit is defined as "the maximum amount of the credit for estate death taxes allowed by Section 2011[Internal Revenue Code] for the decedent's net estate."[14]

Dormant state with inheritance tax: Kentucky



Kentucky has an estate tax similar to New Mexico's but also has an inheritance tax. As a result, repeal of the CSDT reduced Kentucky's revenue by the sponge amount in excess of the inheritance tax (figure 2).

Like New Mexico, the Kentucky estate tax is tied directly to the federal credit.[15] The state's tax laws tie its estate tax to the federal credit and provide that the tax goes away if the credit is repealed, but they also insure that the state tax would resume if the credit comes back in any section of federal code. The state collects inheritance tax at graduated rates up to 16 percent depending on the relationship of the beneficiary.[16]

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[13] 7-7-3(a) NMSA 1978

[14] 7-7-1(d) NMSA 1978; "Section 2011" means Section 2011 of the United States Internal Revenue Code of 1986, as amended or renumbered (7-7-1(l) NMSA 1978).

[15] Kentucky Revised Statutes 140.130

[16] Spouses, parents, children, grandchildren, and siblings are exempt.

Decoupled state: Maryland

Maryland decoupled from the federal law regarding the CSDT in 2002 following passage of EGTRRA. In 2004, Maryland also decoupled from the federal law regarding the unified credit and froze the credit equivalent to $1 million, the federal level in 2003. The Maryland estate tax is the "amount, if any, by which the federal credit exceeds the total of death taxes other than the Maryland estate tax."[17]

Figure 3: Estate & Inheritance taxes 1977-2010

Maryland also has an inheritance tax. The inheritance tax, however, has a much narrower base and collects only about a quarter as much revenue as the estate tax. Property passing to a child or other lineal descendant, spouse of a child or other lineal descendant, spouse, parent, grandparent, stepchild or stepparent, siblings, or a corporation having only certain of these persons as stockholders is exempt from taxation. Property passing to other individuals is taxed at a 10 percent rate.[18]

Maryland has a section in its code called "Effect of change in federal estate tax law," which defines the federal credit "allowable by § 2011 of the Internal Revenue Code as in effect before the reduction or repeal of the federal credit pursuant to the Act of Congress."[19]

Repeal State: Arizona

Arizona was one of five states that repealed its estate tax altogether after repeal of the CSDT. Before 2006, Arizona's estate tax equaled the maximum CSDT. In 2006, the state repealed all references to the estate tax; thus, the tax will not be revived if Congress restores the CSDT. Before repeal of the CSDT, Arizona collected almost $100 million from the estate tax, about one percent of total tax revenue.[20] Since 2006, the state has collected no estate tax revenue.

Figure 4: Estate taxes 1977-2010

A comparison of the tax liability of a $10 million estate in 2001 (the last year of the full CSDT), 2005 (the first year of the deduction), and 2012 shows how the different approaches taken by states affected estate tax liability (table 3). Over the 12-year period, the effective federal estate tax

[17] MD Ac Code 1957 *§ 7-304*
[18] http://individuals.marylandtaxes.com/estatetax/inherit.asp
[19] MD Ac Code 1957 *§ 7-309*
[20] http://www.azdor.gov/Portals/0/AnnualReports/annual2003.pdf .

exclusion increased from $675,000 to $5.12 million, and the top tax rate dropped from 55 to 35 percent. The combination of those changes and repeal of the federal credit affected states differently, depending on the choices they made. The costs and calculations are even more complicated for estates that own property or have residency in multiple states, a fairly common situation for wealthy decedents.

- The combined federal and state estate tax on a $10 million estate was $3,985,250 in 2001, roughly three-quarters of which went to the federal government in every state (table 2), unless the state inheritance tax was greater than the CSDT, as in Kentucky.[21]

- The amount of tax in 2005 and who received it varied, depending on how states reacted to repeal of the CSDT (table 2).
  - In the dormant states without inheritance taxes like New Mexico and those that repealed their estate tax law like Arizona, a $10 million estate would have paid about $1 million less total tax in 2005 than in 2001, but all the revenue would have gone to the federal government—the state portion was eliminated.
  - In states that had decoupled like Maryland or that had inheritance taxes in addition to dormant estate taxes like Kentucky, the amount of estate tax would have fallen much less (or not at all) because the estate and inheritance taxes were not fully defined by the federal tax. Kentucky, for example, would have collected the same in 2005 as in 2001 because it had an inheritance tax. A $10 million estate in Maryland would have paid the same state tax in 2005 as in 2001 because the state decoupled.
- In 2012, a $10 million estate would have owed less combined federal and state estate and inheritance tax in all states because the federal tax dropped sharply (table 3).
  - In the dormant states without inheritance taxes like New Mexico and those that repealed their estate tax law like Arizona, such an estate would have paid $1,155,000 in federal tax and nothing to the state.
  - In states that had decoupled or that had inheritance taxes in addition to dormant estate taxes, combined federal and state estate taxes would have dropped less but would still have been less than half as much as in 2001.

AFTER THE FISCAL CLIFF: WHAT HAPPENS NEXT?

The fiscal cliff is fast approaching, and its abrupt effects on the economy, the federal budget, and tax law could all have adverse impacts on states. Expiration of the 2010 Act is just one of many effects, and the uncertainty over the CSDT is just a small part of that.

[21] States with inheritance taxes received revenue from both those taxes and separate state estate taxes that collected any excess of the federal CSDT over an estate's inheritance tax. Kentucky's inheritance tax can be larger than the CSDT for non-exempt beneficiaries (e.g., a nephew or nonrelative).

Nonetheless, the uncertainty affects states' ability to administer taxes and to budget responsibly. Several dormant states may lack the necessary architecture—that is, the forms, computer programming, and customer service personnel—to resume collecting the estate tax. Yet, the levy may return in 2013, whether or not states act. Uncertainty also imposes a planning burden on states, which often have multiyear budgets that they must balance. The added revenue may surprise some states—and their residents. Several states where the tax would return say on their web sites that they have no estate tax. For example, the Virginia Department of Taxation web site says:

> Legislation enacted by the 2006 General Assembly, House Bill [5019], repeals the Virginia estate tax for the estates of decedents whose date of death occurs on or after July 1, 2007.[22]

But the Virginia legislation did not repeal the estate tax: it only removed a section that defined the federal credit as it existed pre-EGTRRA. Removing this section "recoupled" or relinked the Virginia estate tax to current federal law and made Virginia a dormant state. The restoration of the federal credit would revive Virginia's estate tax, and the state would resume collecting it.[23]

Some states, however, would not benefit from the return to pre-2001 federal estate tax law in 2013. The five states that repealed the tax would get no additional revenue and would probably restore the link to the federal credit: doing that would increase revenue with no additional burden on resident estates.

The future of the federal credit will be decided in the broader context of the many tax provisions scheduled to expire at year's end. The 2010 legislation that extended the provisions of EGTRRA for two years did not extend the repeal of the estate tax but instead modified the estate tax with a lower rate (35 percent) and a higher threshold ($5 million, indexed). The extension did not restore the CSDT but instead retained the deduction for state estate taxes. Congress could extend those provisions either temporarily or permanently. That outcome would not affect states, at least in terms of the CSDT.

Alternatively, the 2010 Act could sunset at the end of 2012 as scheduled, restoring 2001 law. That would increase federal revenue significantly because the top rate would go up to 55 percent and the exclusion would drop to $1 million, imposing estate taxes on many more estates. Restoration of the CSDT in 2013 would reduce federal revenues in 2013 by about $5 billion (assuming no behavioral changes and no additional estate planning) and increase revenue in 30 states that have dormant estate taxes by about $3 billion, half of which would go to California

[22] http://www.tax.virginia.gov/site.cfm?alias=Estate; as of October 22, 2012, the web site refers to H.B. 5018, a law that related to payments out of the treasury, rather than H.B. 5019, the estate tax change.

[23] It's worth restating that from 2005 to 2007, Virginia levied an additional tax on estates that was deductible on federal estate tax returns. In 2013, when the 2010 Act sunsets, Virginia estates will begin paying state estate tax again, but the full amount will be credited against the federal liability.

and Florida.[24] The revenue loss is relative to the significantly higher federal revenue that would come from raising the top rate back to 55 percent and slashing the exclusion to $1 million—on net, the 2013 law would increase federal revenues.

A third alternative would extend 2012 law but restore the CSDT in place of the deduction. That policy would affect far fewer estates than the current law because it would maintain a high threshold—an estimated $5.24 million in 2013, is five times the threshold under pre-2001 law.[25] The IRS reports fewer than 3,000 estates with a value greater than $5 million in 2011. The Tax Policy Center estimates that this policy would reduce federal estate taxes by about $1 billion (for estates of people dying in 2013) but increase state revenues by about $600 million. Estates would save the $400 million difference because they benefit more from a credit against the federal estate tax than from the current deduction.

CONCLUSION

Since 1926, states shared estate tax revenue with the federal government via the CSDT. Until 2001, it was only once significantly modified to change the calculation from a percent of the federal tax to a percent of the estate value. The CSDT mechanism let states share in the most progressive feature of the federal tax code (Burman 2008), potentially offsetting more regressive sales and excise taxes and leading to a uniform estate tax across all fifty states and the District of Columbia. However, in order to reduce the total cost of EGTRRA, Congress repealed the credit in the reconciliation between the House and Senate. From the beginning of the negotiations in 2001, there was momentum to repeal the federal estate tax. States with pickup taxes knew the revenue would probably disappear, but were expecting it to happen in a gradual manner. In the final legislation, the federal estate tax was phased out over ten years, with the bulk of the lost revenue at the end of the period, while the CSDT was phased out much more quickly, reducing state revenue almost immediately. The decision to repeal the credit may have been popular with federal lawmakers because it increased federal revenue without increasing federal rates, but it made estate tax law more complex for both state governments and taxpayers.

The repeal of the CSDT began to affect estates in 2002, when it was reduced by 25 percent, and the revenue for dormant states disappeared by 2006. The timing was especially unfortunate since it coincided with the 2001 recession and exacerbated existing budget shortfalls caused by other declining revenues and increased spending needs in 2002 (National Association of State Budget Officers (NASBO) 2003).[26] States responded in different ways, while a majority left the credit

[24] Appendix B presents estimates for each state. The CBO estimated that switching from the credit to the deduction increased federal revenue by $3.4 billion in 2006 (Greene 2009, 3) .

[25] Pre-EGTRRA, the exclusion was $675,000 in 2001 but was increasing annually. In 2006, the threshold would have been $1 million per law in effect in 2000.

[26] NASBO (2002) reported that 40 states had to make mid-year budget cuts to balance fiscal year 2003 budgets, the highest number in the organization’s records.

language dormant but intact, other states decoupled from federal law—leaving a patchwork of estate laws across the country (Maguire 2012).

Table 4: Three Scenarios for the Federal Credit for Estate and Inheritance Taxes (CSDT)

Dollars are in millions and are for estates of 2013 decedents. Impact may span several years based on filing time.

Current Policy: 2012 Policy Extended		**Federal**	**State**	**Net Impact on Estates**
All states	No change in policy, CSDT stays dormant	No change	No change	-
Current Law: CSDT Restored		**Federal**	**State**	**Net Impact on Estates**
Dormant states	The state estate tax returns with the resumption of the credit.	(3,092)	3,092	-
Dormant states with inheritance	The state estate tax returns with the resumption of the credit and so states will begin receiving the difference between the federal credit and the existing inheritance tax.	(531)	91	(440)
Decouple/stand-alone states	The resumption of the credit reduces federal revenue by the difference between the cost of the deduction and the amount of the credit.	(1,728)	-	(1,728)
Repeal states	No impact	-	-	-
Total		**(5,350)**	**3,183**	**(2,167)**
Alternative to Current Policy: 2012 Estate Tax Law is Extended but CSDT is Restored.		**Federal**	**State**	**Net Impact on Estates**
Dormant states	Estate tax returns with credit but the high $5 million exclusion limits the number of estates that file.	(609)	609	-
Dormant states with inheritance	Estate tax returns with credit but the high $5 million exclusion limits the number of estates that file.	(101)	18	(83)
Decouple/stand-alone states	Loss to federal revenues because deduction converted to credit mitigated by the high $5 million exclusion.	(328)	-	(328)
Repeal states	No impact.	-	-	-
Total		**(1,037)**	**627**	**(410)**

Source: Tax Policy Center; for state-by-state data and methodology, see appendix B.
Note: Calculations here are only for the scenarios restoring the CSDT and not for any other changes to the estate tax that might impact states.

An important aspect of the EGTRRA estate tax legislation was that it was temporary. While federal estate taxes were completely repealed in 2010, the law was scheduled to revert to pre-2001 in 2011. This schedule was delayed two years by the 2010 Act, but now federal lawmakers need to decide again what federal estate tax law will be and how much it costs in foregone revenue by limiting the tax. While the CSDT has not come up in public policy discussions, the uncertainty of federal tax policy leads to uncertainty in state policy.[27] This is a policy that should be on the table based on sound tax policy principles.[28] Simplicity is often cited as a goal of any tax reform proposal and the restoration of the CSDT would likely lead to states adopting a consistent set of laws. The elimination of the federal credit has only increased the complexity for estates in the sixteen states that have opted to retain a state level tax.

However, unlikely it is that the CSDT will be revived. At this date, states don't know for certain what to plan. The state fiscal crisis due to the most recent recession has been even worse than the 2002-03 crisis, requiring states to cut budgets drastically or raise revenues (and in most cases, both). The uncertainty in federal funding and tax law due to the fiscal cliff has made states' ability to effectively and efficiently manage their budgets more difficult. A consistent and permanent federal policy accounting for how changes affect other levels of government supports the formation of sound and efficient tax policy across the states. This brief highlights only one aspect of the temporary federal tax legislation enacted over the last decade and shows how a cost saving measure by the federal government has led to a shift in revenue from the states to the federal government, an inconsistent application of estate tax law depending on geography, and uncertainty and confusion for other levels of government.

[27] Williams, 11.
[28] Maguire (2012) assesses the CSDT on four principles: simplicity, equity, economic efficiency, and revenue efficiency.

APPENDIX A: COMPUTATION OF MAXIMUM CREDIT FOR STATE DEATH TAXES

From 1954 to 2001, the federal credit offset estate tax by up to 16 percent of the value of the estate if the state of residence had estate or inheritance taxes. The maximum credit was determined by the taxable value after specific deductions related to the administration of the estate. For example, the maximum allowable credit for an estate with a taxable value of $600,000 (net of a $60,000 adjustment) would be $16,400—$10,000 base tax on the first $440,000, plus 4 percent of $160,000 over that amount (see table). The credit only applied if the estate had a state tax liability. Up until 2001, every state and the District of Columbia had an estate tax equal to the maximum value of the credit.

Taxable Value of Estate After $60,000 deduction		
(1)	*(2)*	*(3)*
More than	*but less than*	*Base Tax*
-	40,000	No tax
40,000	90,000	$0 plus 0.8% above $40,000
90,000	140,000	$400 plus 1.6% above $90,000
140,000	240,000	$1,200 plus 2.4% above $140,000
240,000	440,000	$3,600 plus 3.2% above $240,000
440,000	640,000	$10,000 plus 4.0% above $440,000
640,000	840,000	$18,000 plus 4.8% above $640,000
840,000	1,040,000	$27,600 plus 5.6% above $840,000
1,040,000	1,540,000	$38,800 plus 6.4% above $1,040,000
1,540,000	2,040,000	$70,800 plus 7.2% above $1,50,000
2,040,000	2,540,000	$106,800 plus 8.0% above $2,040,000
2,540,000	3,040,000	$146,800 plus 8.8% above $2,540,000
3,040,000	3,540,000	$190,800 plus 9.6% above $3,040,000
3,540,000	4,040,000	$238,800 plus 10.4% above $3,540,000
4,040,000	5,040,000	$290,800 plus 11.2% above $4,040,000
5,040,000	6,040,000	$402,800 plus 12.0% above $5,040,000
6,040,000	7,040,000	$522,800 plus 12.8% above $6,040,000
7,040,000	8,040,000	$650,800 plus 13.6% above $7,040,000
8,040,000	9,040,000	$786,800 plus 14.4% above $8,040,000
9,040,000	10,040,000	$930,800 plus 15.2% above $9,040,000
10,040,000		$1,082,800 plus 16% above $10,040,000

Source: IRS Instructions for Form 706 (2001)

APPENDIX B: ESTATE TAX STATUS BY STATE, COLLECTIONS IN 2001 AND 2010, AND PROJECTION OF GAIN/LOSS DUE TO RESTORATION OF CREDIT FOR 2013 ESTATES WITH FEDERAL LIABILITY (DOLLARS IN MILLIONS)

State	Amount collected by state in 2001 (1)	Amount collected by state in 2010 (1)	Current Law Scenario (2)		Alternative Scenario (3)	
			Federal	State	Federal	State
Dormant without inheritance						
Alabama	47	*	(63)	63	(12)	12
Alaska	3	*	(6)	6	(1)	1
Arkansas	26	*	(44)	44	(9)	9
California (4)	935	-	(962)	962	(189)	189
Colorado	83	*	(81)	81	(16)	16
Florida	708	3	(573)	573	(113)	113
Georgia	126	-	(111)	111	(22)	22
Idaho	43	*	(18)	18	(3)	3
Louisiana	83	2	(56)	56	(11)	11
Michigan	155	-	(173)	173	(34)	34
Mississippi	28	*	(35)	35	(7)	7
Missouri	154	*	(126)	126	(25)	25
Montana	20	*	(24)	24	(5)	5
Nevada	40	-	(30)	30	(6)	6
New Hampshire	59	*	(27)	27	(5)	5
New Mexico	23	*	(28)	28	(6)	6
North Dakota	5	*	(18)	18	(4)	4
South Carolina	49	*	(75)	75	(15)	15
South Dakota	35	*	(17)	17	(3)	3
Texas	322	*	(317)	317	(62)	62
Utah	30	*	(25)	25	(5)	5
Virginia	127	6	(152)	152	(30)	30
West Virginia	18	*	(25)	25	(5)	5
Wisconsin	77	1	(95)	95	(19)	19
Wyoming	8	*	(12)	12	(2)	2
TOTAL	**3,204**	**13**	**(3,092)**	**3,092**	**(609)**	**609**
Dormant with inheritance						
Indiana	164	133	(101)	26	(19)	5
Iowa	88	68	(87)	29	(17)	6
Kentucky	85	37	(49)	27	(9)	5
Pennsylvania	777	729	(217)	10	(41)	2
Tennessee	84	81	(76)	-	(14)	-
TOTAL	**1,198**	**1,049**	**(531)**	**91**	**(101)**	**18**

State	Amount collected by state in 2001 (1)	Amount collected by state in 2010 (1)	Current Law Scenario (2)		Alternative Scenario (3)	
			Federal	State	Federal	State
Decouple/Stand-alone states						
Connecticut	258	168	(98)	-	(19)	-
Delaware	41	*	(18)	-	(3)	-
D.C.	51	39	(18)	-	(3)	-
Hawaii	18	-	(25)	-	(5)	-
Illinois	361	243	(284)	-	(54)	-
Maine	31	31	(22)	-	(4)	-
Maryland	169	173	(103)	-	(19)	-
Massachusetts	203	221	(148)	-	(28)	-
Minnesota	53	148	(79)	-	(15)	-
New Jersey	478	582	(205)	-	(39)	-
New York	759	866	(404)	-	(77)	-
North Carolina	143	84	(123)	-	(23)	-
Oregon	42	98	(61)	-	(11)	-
Rhode Island	27	30	(20)	-	(4)	-
Vermont	13	14	(14)	-	(3)	-
Washington	106	82	(108)	-	(20)	-
TOTAL	**2,753**	**2,781**	**(1,728)**	**-**	**(328)**	**-**
Repeal States						
Arizona	77	*	-	-	-	-
Kansas	41	8	-	-	-	-
Nebraska	27	*	-	-	-	-
Ohio (5)	166	55	-	-	-	-
Oklahoma (5)	85	23	-	-	-	-
TOTAL	**396**	**87**	**-**	**-**	**-**	**-**
GRAND TOTAL	**7,551**	**3,930**	**(5,350)**	**3,183**	**(1,037)**	**627**

(1) Actual collections of inheritance, estate and gift taxes as reported to the U.S. Census. Includes revenues from prior year estates.
(2) Current law assumes federal top rate of 55 percent and exclusion of $1 million.
(3) Alternative scenario assumes federal top rate of 35 percent and exclusion of $5.24 million.
(4) The California revenue analysts estimated the full year impact of reviving the CSDT would increase revenue by $1.8 billion, used to balance its 2010 budget (California 2010, 79).
(5) Ohio and Oklahoma recently repealed their estate taxes and were still collecting revenue in 2010.
* Less than $1 million.

Source: U.S. Census Survey of Government Finances for revenue collected; Tax Policy Center for scenario estimates.

Methodology:

The first two columns of data show actual revenue collections as reported by the Census Survey of State and Local Government Finance. These data (which include inheritance, gift, and estate tax revenue) are reported when states receive the revenue and may include estates more than one year old.

TPC modeled the impact of restoring the credit using estate tax data from the IRS Statistics of Income. The table shows two scenarios: current law under which the 2010 Act sunsets and 2001 law is restored, and an alternative in which 2012 law is extended but the CSDT is restored. The table omits the current policy scenario because extending current policy would not affect state estate taxes.

The analysis required several assumptions because of data limitations. Determining the level of estate tax in 2013 under the 2001 law is complicated by the fact that there are far fewer estates filing returns in 2011 (the latest available data from IRS) due to the $5 million exclusion. Also, there is significant volatility at the state level, so using any single year may not be representative. It is a major assumption that 2001 estate values are similar to 2013 values for the current law scenario and 2011 are similar to 2013 for the alternative scenario.

- The dormant states are those that currently do not have an estate or inheritance tax. The calculation of the impact is
  *Impact = number of estates * average value of estate * effective rate*
  Where
    - The number of estates is the average state share of the national number of estates over the period 1995-2001, multiplied by the number of estates in 2001 for the current law scenario, and by the number of estates greater than $5 million for the alternate scenario.
    - The average value of estate is the national average in 2001 for the current law and 2011 for the alternative.
    - Effective rate is the ratio of the 2001 aggregate state death tax credit and the gross estate value reported by the IRS, divided. The effective rate is used and not the schedule for the credit because information about the deductions and the unified credit by state are not reported.
- Two additional steps had to be performed for the dormant states with inheritance taxes because of the deduction for the inheritance tax to calculate the federal cost.
    - The repeal of the deduction will offset the cost of restoring the CSDT, but not fully. Using the pre-2001 law, the ratio of the marginal cost of converting the deduction to a credit was 0.16.
    - However, the deduction for dormant states with inheritance taxes is for inheritance taxes paid to the state, while the dormant estate tax would capture the amount of the credit for all estates paying federal tax. The current inheritance tax in these states has exemptions for beneficiaries that would not apply to the federal

estate tax, which is levied on the value of the estate. The ratio of the average number of estates claiming the CSDT before repeal and the average number of estates claiming the deduction is 5.1.

- A similar methodology was used for decouple/stand-alone states, and because of the volatility of estate tax revenue, averages were also used based on historic IRS data. The impact is the conversion of the deduction to a credit and only impacts the amount at the federal level.
- There is no change for repeal states.

APPENDIX C: STATE LEGISLATIVE DETAIL

DORMANT STATES WITHOUT INHERITANCE TAX

Colorado, Georgia, Idaho, Mississippi, Missouri, Nevada, New Hampshire, New Mexico, North Dakota, South Carolina, Texas, Utah, Virginia, West Virginia, and Wisconsin link explicitly to the IRC CSDT.

Alabama, Alaska, California, Florida, Louisiana, Michigan, Montana, South Dakota, and Wyoming do not specifically cite the IRC as most of the other dormant states but say the estate tax is equal to any credit against federal taxes offered by the federal government.

Arkansas links to the 2002 IRC in one place but in another section says that the chapter (referring to the section of law) is not in effect after January 1, 2005. We have interpreted this to mean that the state is dormant, but Arkansas may find it does not have a tax if the CSDT is revived and could plausibly be considered a repeal state (Arkansas Code 26-59-103).

DORMANT STATES WITH INHERITANCE TAXES

Indiana has an inheritance tax that has different rates and exemptions based on the type of beneficiary. For transfers to lineal descendants or ascendants (e.g. son, mother, grandchild), the amount above $250,000 is taxed according to a graduated schedule with a top rate of 10 percent above $1.5 million. For transfer to siblings and their descendants, the exemption is $500 and the top rate is 15 percent on transfers above $1 million. For all others, the exemption is $100 and the top rate is 20 percent on transfers above $1 million. Beginning in 2013, the inheritance tax will begin phasing out and be repealed in 2022.

The estate tax in Indiana is explicitly linked to the CSDT and so there has been no estate tax since 2004. The estate tax is the difference between the maximum federal credit and the inheritance tax liability (i.e. a sponge tax). If the CSDT is restored, the estate tax will be revived and slowly replace the inheritance tax as that tax is phased out (Indiana Code 6-4.1-1-4).

Iowa has an inheritance tax and a dormant estate tax. The lineal descendants and ascendants are exempt as are in-state charitable institutions. There is a blanket exemption on the first $25,000. There is a graduated schedule for siblings and their descendants, with a top rate of 10 percent on transfers over $150,000. For firms and organizations that don’t qualify as nonprofits, the entire transfer is taxed at 15 percent. For out of state charitable organizations, the rate is 10 percent.

The estate tax is equal to the maximum CSDT with a credit for any inheritance taxes paid (Iowa Code 450 and 451).

Kentucky has both an inheritance tax and an estate tax. The inheritance tax is based on the relationship to the decedent. Transfers to direct descendants and ascendants and spouses are exempt while transfers to the children of siblings and skipped generation beneficiaries (e.g. grandchild) are taxed at a maximum rate of 16 percent above $200,000 with a $1,000 exemption. Charities are taxed at a top rate of 16 percent on value above $60,000 after a $500 exemption.

The estate tax is equal to the maximum CSDT with a credit for any inheritance taxes paid (Kentucky Code 140.010 for inheritance and 140.130 for estate).

Pennsylvania has both an inheritance tax and an estate tax. The decedent's spouse and children under age 21 are exempt. Other beneficiaries are taxed on the whole amount. Lineal descendants and ascendants are taxed at 4.5 percent. Siblings are taxed at 12 percent and all others are taxed at 15 percent. Charitable organizations are exempt.

The estate tax is equal to the difference between the CSDT and the inheritance tax.

Tennessee has begun to phase out its inheritance tax by increasing the exclusion to $5 million in 2015 and then repealing it in 2016. The inheritance tax is on value after a $1 million exemption (in 2012). The rate is graduated with a top rate of 9.5 percent on taxable value above $440,000. The estate tax is equal to the difference between the CSDT and the inheritance tax, so if the CSDT is restored, the estate tax will replace the inheritance tax as it is phased out. (Tennessee also had a gift tax that was repealed in 2012.)

DECOUPLE/STAND-ALONE STATES:

Connecticut has a stand-alone tax structure with a top rate of 12 percent on taxable values over $10,100,000 and the first $3,500,000 is not taxed. There is a credit for gift taxes paid, which Connecticut levies. If the 2010 Act expires, the Connecticut estate tax may not be high enough to match the CSDT and Connecticut may not maximize the revenue from a return of the CSDT.

Delaware has varied its estate tax over the last decade. Originally, the state had a dormant tax, tied to the CSDT, but in 2009, they changed the law to refer back to the 2001 Internal Revenue Code (IRC), thereby restoring the estate tax. But the change was only effective until July 1, 2013 at which point the reference reverts to the current law IRC. If the 2010 Act expires, there's no change for Delaware. The 2001 IRC will be restored, but if the estate tax is instead retained as it is in 2012, Delaware will lose estate tax revenue late in FY 2014. (The revenue estimators in Delaware only show the impact of tax returns related to estates prior to 7/1/2013 in their June forecast.)[29]

[29] FY 2014 revenue estimate from Delaware Economic and Financial Advisory Council (DEFAC) forecast on June 18, 2012. Accessed September 12, 2012, http://finance.delaware.gov/defac/june2012/revenues.pdf.

Hawaii had been a dormant state but restored the estate tax as of May 2010 using the $3.5 million threshold set by the IRC in 2009 plus $100,000. The threshold will be tied to the federal threshold in 2012 and beyond. In 2013, the expiration of the 2010 Act means that the threshold will decline to $1 million, exposing many more estates to the state estate tax.

Illinois kept references to the Credit from 2003 to 2005 but allowed the exclusion amount to increase per EGTRRA. For tax years after 2005, Illinois maintained the reference to 2001 IRC but set the exclusion amount to $2 million through 2011, $3.5 million for 2012, and $4 million for later years. If the 2010 Act expires, this language will create a tax gap for 2013 where an estate between $1 million and $4 million will file a federal return, but not an Illinois return.

D.C., Maryland, Maine, Massachusetts, Minnesota: These states decoupled by referring to the IRC, pre-EGTRRA. This has maintained the level of the state estate tax and means that the expiration of the 2010 Act will have no revenue impact on these states.

New Jersey also refers to pre-EGTRRA IRC but allows $675,000 exclusion as opposed to $1 million. This creates a tax gap where estates valued between $675,000 and $1 million would have to file a New Jersey return but not a federal one.

New York refers to the IRC in place in 1998 with an exclusion of $1 million. For the purposes of this discussion, the 1998 IRC is functionally equivalent to the 2001 IRC.

North Carolina refers to the 2001 Credit but bases all other aspects of its estate tax to current law so that if the estate tax is repealed completely (as it was in 2010) North Carolina's estate tax is also repealed. Thus it currently has a $5.24 million exclusion.

Oregon uses the IRC in effect December 31, 2010, to determine the taxable estate value but has its own rate schedule that excludes the first $1 million and has a top rate of 16 percent on value above $9.5 million (similar but not exact to the Credit schedule).

Rhode Island also refers to pre-EGTRRA IRC but allows $892,865 (adjusted for inflation from the 2010 level of $850,000) exclusion as opposed to $1 million. This creates a tax gap where estates valued between the Rhode Island threshold and $1 million would have to file a Rhode Island return, but not a federal one.

Vermont has a stand-alone tax schedule identical to the 2001 Credit. The Vermont exclusion is $2.75 million so there is a tax gap where, in the case of 2012, an estate would not be required to file a federal return but is required to file a Vermont return, and in the case of the 2010 Act expiring, an estate would file a federal return, but not a Vermont return.

Washington's code makes it unequivocal that there shall be a state tax regardless of what the federal government does:

> The tax imposed under this section is a stand-alone estate tax that incorporates only those provisions of the internal revenue code as amended or renumbered as of January 1, 2005, that do not conflict with the provisions of this chapter. The tax imposed under this chapter is independent of any federal estate tax obligation and is not affected by termination of the federal estate tax.[30]

Washington has its own tax schedule that excludes the first $2 million and has a top rate of 19 percent on taxable value above $9 million.

REPEAL STATES

Arizona, up until 2006, was a dormant state and had an estate tax equal to the maximum CSDT. In 2006, the state repealed all references to the estate tax and the tax will not be revived if the CSDT is restored. Before the CSDT was phased out, Arizona collected almost $100 million from the estate tax, about one percent of total tax revenue.[31]

Kansas, until 2010, referred to the federal estate tax law as it existed in 1997. In 2010, Kansas's legislators repealed all taxes related to estates. The Kansas Department of Revenue sums up what can be expected for estates of decedents dying in 2010 and later:

> *The Kansas Legislature has not enacted any estate tax provisions which apply to the estates of decedents dying after December 31, 2009. As a result, no tax is or will be due from these estates. Because no Kansas estate tax law applies to these estates the Department of Revenue will not process estate tax returns filed for them. (Kansas, 2010)*

Nebraska repealed the provision relating to the CSDT in 2007, but still has an inheritance tax. The inheritance tax will still be converted to a credit but because the state estate tax, based on the maximum CSDT less inheritance tax, explicitly excludes decedents after January 1, 2007, the state won't collect the additional tax (Nebraska Revised Statute 77-2101.01).

Ohio repealed its inheritance tax and estate tax in 2010. The compilation of the estate sponge tax sets the tax equal to the IRC as it is in 2010, so even if the CSDT is revised, Ohio's code refers to a year when there was no CSDT (Ohio, 2011 p.34).

Oklahoma repealed its estate tax in 2010. It had a stand-alone tax independent of the federal estate tax. There still exists in the statute a section that imposes additional tax up to the maximum CSDT but also references a section that has been repealed. It is unclear if this is sufficient language to constitute a dormant estate tax or if additional legislation is necessary (Oklahoma Statute 68.804).

[30] 83.100.040(3) Revised Code of Washington
[31] http://www.azdor.gov/Portals/0/AnnualReports/annual2003.pdf

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