

February 13, 2001

## Estate Tax Repeal Would Compound State Budget Crisis

Last summer Congress approved legislation to repeal the estate tax over a period of 10 years. Vetoed by President Clinton, the 107<sup>th</sup> Congress has opened with several proposals to repeal the tax, either through President Bush's comprehensive tax reduction package or dedicated legislation.

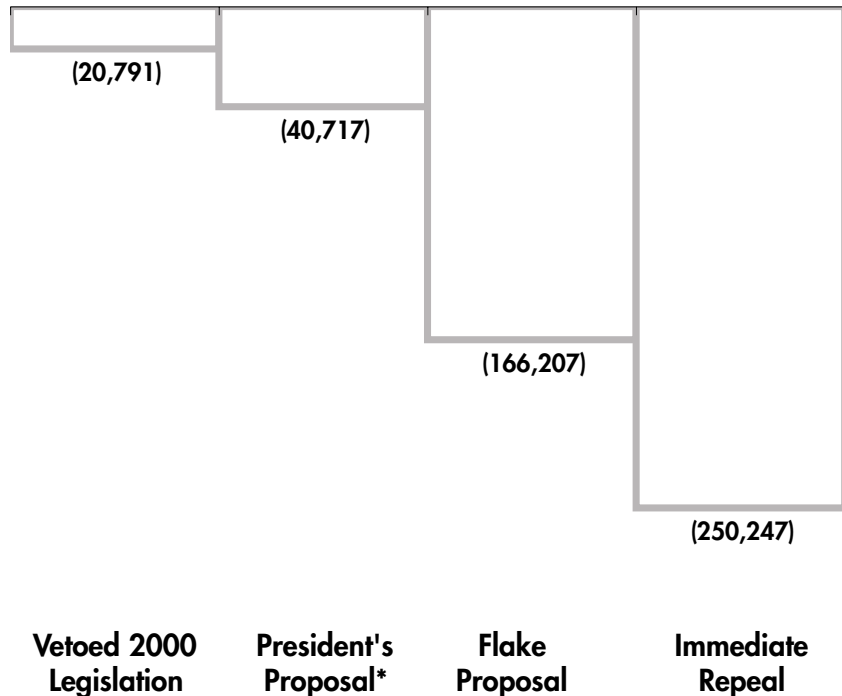
As the federal legislative process unfolds, specific details are hazy. The most prominent repeal bill, introduced by Congresswoman Jennifer Dunn, has been announced, but the text of the bill remains unpublished.

Momentum for a larger and immediate or even retroactive comprehensive tax cut have also affected estate tax proposals. Bush's still evolving plan calls for phased repeal over six years; plans like Congressman Jeff Flake's accelerate repeal even further.

### ESTATE TAXES IN WASHINGTON

One of the first state taxes established in Washington was the inheritance tax, adopted in 1901. Initiative 402, approved in 1981,

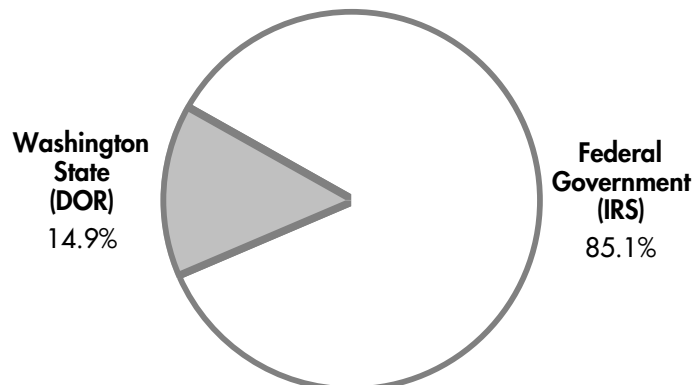
**State Revenue Reduction, FY 2001-2003**  
General Fund - State, Thousands of Current Dollars



\* Assumes no retroactive 2001 reduction.

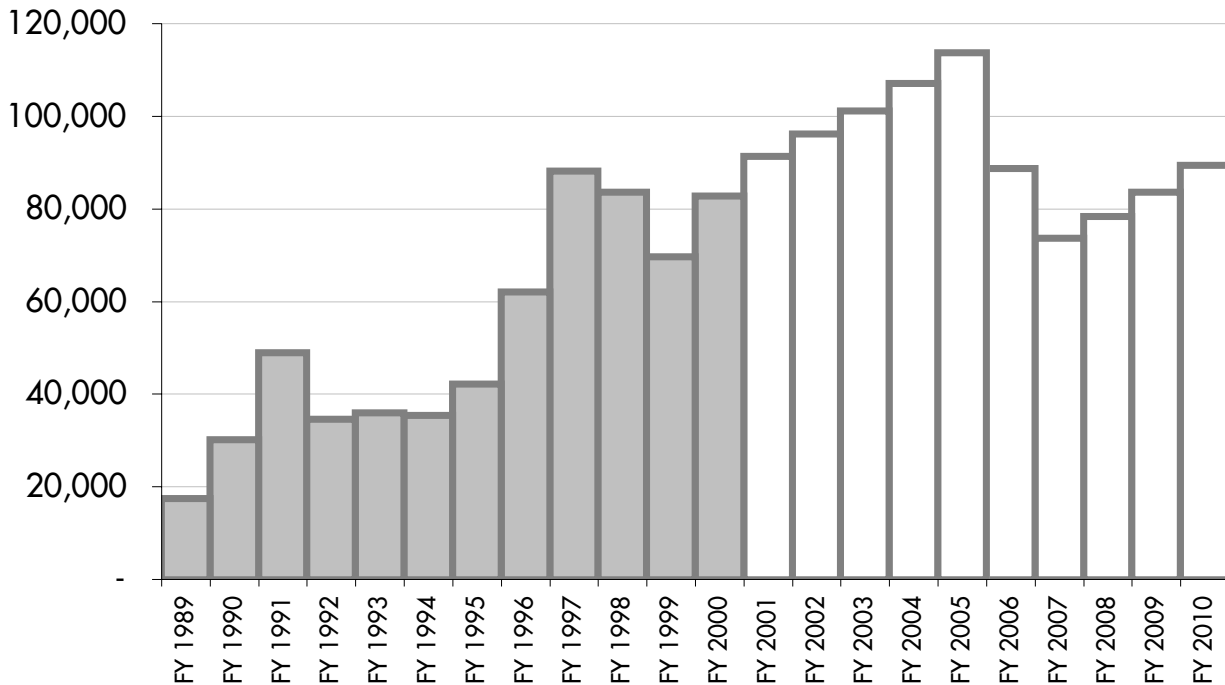
### Relative Estate Tax Revenue Shares

Taxes on Washington Residents, Calendar Year 1998



## Past and Projected Washington State Estate Tax Revenues

State Fiscal Years, Thousands of Current Dollars



eliminated the inheritance tax, instead imposing an estate tax equal to the state tax credit allowed on the federal estate tax. With a dollar-for-dollar credit under federal law, the state effectively keeps a portion of federal estate tax revenues. Repeal of the federal tax and its resulting credit would thus end collection of the state tax.

At present the tax is imposed only on estates valued above \$650,000, with the exemption rising to \$1,000,000 in 2006. With transfers to spouses also exempt, the tax effects only about 2,100 Washington families each year (including related gift and generation-skipping transfer taxes).

Individuals subject to the estate tax tend to have high incomes: a recent Treasury Department study found that 91 percent of all estate taxes are paid by individuals whose

annual incomes exceeded \$190,000 at the time of their death. Less than one percent of estate taxes are paid by those with annual incomes below \$100,000.

### BUDGET IMPLICATIONS

State legislators are currently at work on a new two-year budget for the 2001-2003 biennium which starts July 1<sup>st</sup>. Depending on the details, particularly the treatment of the state credit, estate tax proposals would have a significant effect on state revenues.

At most, repeal retroactive to January 1, 2001 would reduce Washington general fund revenues by \$53 million for the 1999-2001 biennium, and \$197.2 over the 2001-2003 biennium. Lost revenue for the 2003-2005 biennium would be approximately \$220.6 million based on state demographics assuming a constant distribution of wealth.

Although the Initiative 601 spending limit is adjusted for lost federal revenue and cost shifts, the state portion of the estate tax, collected directly by the Department of Revenue, would trigger no adjustments since it is treated as a purely state revenue source.



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