

Free to Choose

As we ponder our legacy and consider what we can leave to our kids, grandkids, friends, and charity, most of us need not be too concerned about the impact of estate taxes. This stands in sharp contrast to the situation that existed not long ago. In 2001 estates exceeding \$675,000 were potentially subject to these federal taxes. However, the rules changed dramatically over the last few years and today the vast majority of us need not agonize over the impact of estate taxes. As such, it seems appropriate to take a step back and focus on the fact that that we can pretty much do as we please with the assets we have accumulated over our lifetimes. We are free to provide for our families and, perhaps, to leave a bequest to those charities, like Cato, that are important to us.

This flexibility and freedom is possible because the last decade saw a major overhaul of federal estate tax laws. The estate tax is a tax on the transfer of assets of a deceased person—hence, “death tax” is a frequent moniker. Because these assets have typically been taxed during life—either as income and capital gains—Cato scholars and many others argue that the estate tax should be repealed in its entirety because it amounts to double taxation. Despite the logic and merit of this position, the estate tax remains with us, albeit in a less onerous form. A total repeal would take agreement in the House and Senate, as well as a president willing to sign the legislation.

The mechanism that allows most of us to avoid the estate tax is called an “exemption.” For 2015, \$5,430,000 can be given by an individual without incurring federal estate taxes. This \$5,430,000 is per person, so a couple can give up to \$10,860,000. As a result, only the largest



2 percent of estates have to pay federal estate taxes. The exemption is indexed for inflation so it will keep on growing. And you can use your exemption at death or you can use it to make tax-free gifts during your lifetime. Once you go beyond the exemption limit, estate taxes click in at a pretty hefty rate of 40 percent. Rather than pay this to the Feds, wealthy individuals have a couple of options because the estate tax does not apply—in tax parlance, you get a “deduction”—for assets left to a spouse or charity.

Many states have also cleaned up their act and repealed state death taxes. (Nineteen states still retain some form of estate or inheritance tax, however—so keep that in mind when you do your planning.) Since the states are constantly tinkering with their rules, it’s best to have your tax adviser verify whether or not you live in a state that still imposes some form of death tax. These exemption levels tend to be much lower than the federal level, so states can take a bit out of even a relatively modest estate. Folks have been known to move to another state just to avoid these taxes, just as many people have moved to avoid burdensome state income taxes.

Nevertheless, our reformed, “minimalist” estate tax leaves most of us free to remember family, friends, and charities as we choose. That is as it should be. Ideally, of course, all Americans would be free of estate taxes and Cato will continue to advocate for that policy. ■

IF YOU HAVE QUESTIONS ABOUT ESTATE PLANNING OR WOULD LIKE TO LEARN MORE ABOUT MAKING A BEQUEST TO THE CATO INSTITUTE, PLEASE CONTACT GAYLLIS WARD, ASSOCIATE VICE PRESIDENT OF DEVELOPMENT, AT (202) 218-4631 OR GWARD@CATO.ORG.