Taxation of Transfers and Wealth by Wojciech Kopczuk

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What Makes Wealth Transfer Taxes Different?

1. They occur only at very infrequent intervals
   - This makes empirical work difficult, since
     - Only observe in a small fraction of the population at any given time
     - Expectations of tax rates far into the future should play a key role in determining behavior
   - A possibly large incentive for tax avoidance
     - If avoidance technology involves some fixed costs, very large payoff to investment

What Makes Wealth Transfer Taxes Different?

2. They apply only to the very top of the wealth distribution
   - Typically 1-2% in the US since 1980
   - Very skewed even among taxpayers
   - Have a potentially large impact on the dynamics of wealth distribution, given how concentrated wealth is
   - Reinforces potential for avoidance, if increasing returns to avoidance expenditures

What Makes Wealth Transfer Taxes Different?

3. They inherently involve direct effects on two parties, the individual leaving the estate and heirs or charities who receive it
   - Makes nature of social welfare evaluation central to determining optimal policy
   - Can push optimal policy toward subsidization:

     “Progressive *subsidies* are not the first thing that comes to mind when thinking about treatment of estate taxation for redistributive purposes.”

What Makes Wealth Transfer Taxes Different?

3. They inherently involve direct effects on two parties, the individual leaving the estate and heirs or charities who receive it
   - Requires an understanding of motivation (need to extend standard models of utility maximization):
     - Accidental bequests
     - Warm glow
     - Well-being of recipients
     - Exchange
     - Benefits of wealth accumulation *per se*

What Makes Wealth Transfer Taxes Different?

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   – We would also like to know more about intergenerational correlations of ability, and the extent to which these relate to bequests

What Makes Wealth Transfer Taxes Different?

4. They are integrally related to death
   - Makes tax avoidance through timing less of an issue
   - May interfere with or shape tax planning
     - Example: holding on to assets too long, given the tax advantages of *inter vivos* gifts
   - Limits the form that the tax may take
     - Can’t rely on taxpayer for information about gains, time pattern of wealth accumulation, etc.

What Makes Wealth Transfer Taxes Different?

4. They are integrally related to death
   - Likely to involve important decisions at an advanced age
     - Evidence from other contexts (e.g., financial planning, Medicare Part D plan choice) suggests that such decisions may be challenging

What Makes Wealth Transfer Taxes Different?

5. They may induce sales of illiquid assets
   - Big issue (politically, anyway) is induced sales of family businesses
     - This might be good or bad
     - Empirical evidence is scant, but some suggestion that the effect is present

What Makes Wealth Transfer Taxes Different?

6. They are politically very unpopular
   – Proposals to increase taxes on the *incomes* of “millionaires and billionaires” rather than on their estates, without much regard to the relative equity-efficiency trade-offs

Other Issues

- Interactions with other taxes important
  - Integration of estate and gift taxes; changes can lead to complicated incentives
    - Example: 2010 repeal of estate tax, but not gift tax
  - A backstop for capital gains taxation?
    - 2010: replaced with COB
  - Are wealth transfer taxes better or worse than annual wealth taxes?
  - What would the role of the estate tax be under a comprehensive consumption/expenditure tax?

Other Issues

- Economic environment important
  - How well annuities market functions
  - Importance of old-age uninsured health shocks

Other Issues

- Tangible versus human capital
  - Only tangible transfers are taxed
  - Transfers of human capital (including tangible costs of education) are not taxed
- How important are taxed versus untaxed transfers?
  - Likely to vary substantially across the wealth distribution
  - Same is true of motivations for leaving bequests
    - Accidental bequests can’t be important at the top

Agenda

What role should wealth transfer taxes play in a well-designed tax system?

- Form (e.g., estate, inheritance, gift, etc.)
- Level
- Progressivity
- Coverage and exemptions