Taxing Billionaires: Estate Taxes and the Geographical Location of the Forbes 400

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Abstract

We study the effect of state-level estate and inheritance (EI) taxes on the geographical location of the Forbes 400 richest Americans and its implication for tax policy. First, we use a change in federal tax law to identify the tax sensitivity of the ultra-wealthy’s locational choices. Before 2004, there was no cross-state variation in effective EI tax rates on billionaire’s estates due to a federal credit. This credit was eliminated in 2004, resulting in substantial variation between states with and without EI taxes. We find the number of Forbes 400 individuals in EI states fell by 35% after 2004 compared to non-EI states. Billionaire’s sensitivity to the EI tax increases significantly with age. The number of Forbes 400 individuals in EI states is uncorrelated with age up to 2004, but falls sharply with age after 2004.

Second, we use our estimated elasticity to quantify aggregate revenue losses caused by mobility to non-EI states. We find that $123 billion of 2004 Forbes 400 wealth escaped EI taxation in the subsequent years due to billionaires moving away from EI states. This amounts to 48.8% loss in aggregate state EI tax earnings. Finally, we estimate the cost and benefits of adopting EI on each state’s tax revenues. States face a trade-off. Adoption of an EI tax implies a one-time tax revenue gain for the state when a resident billionaire dies, but it also reduces its billionaire population and thus their flow of income tax revenue over remaining lifetimes. Despite the high elasticity of geographical location with respect to the EI tax, we find that for the average state the benefit of additional revenue from the EI tax exceeds the cost of foregone income tax revenue by 30%. While the cost-benefit ratio varies substantially across states, most states that currently do not have EI taxes would have higher revenues if they adopted it.

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