

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. Before 2005, there was virtually no cross-state variation in effective EI tax rates on billionaire's estates due to a federal credit. This credit was eliminated in 2005, resulting in substantial variation between states with and without EI taxes. This change allows for identification of the tax sensitivity of the ultra-wealthy's locational choices. Using a difference-in-difference estimator, we find the number of Forbes 400 individuals in EI states fell significantly after 2004 compared to non-EI states. EI states lost an average of 2.8 Forbes 400 billionaires, with an implied semi-elasticity equal to $-.35$. Using a triple-difference estimator based on the notion that a billionaire's sensitivity to the EI tax should increase with age, we find that the number of Forbes 400 individuals in EI states is uncorrelated with age up to 2004, but falls sharply with age after 2004. We conclude that billionaires' locational choices within the U.S. are highly sensitive to state EI taxes.

States therefore 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. Using our estimates of the 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 16%, despite the high elasticity. The cost-benefit ratio, however, varies substantially across states, with the cost of an EI tax exceeding its benefit in states with high income tax rates.

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