Insight

Growth Consequences of Estate Tax Reform: Impacts on Small and Family Businesses

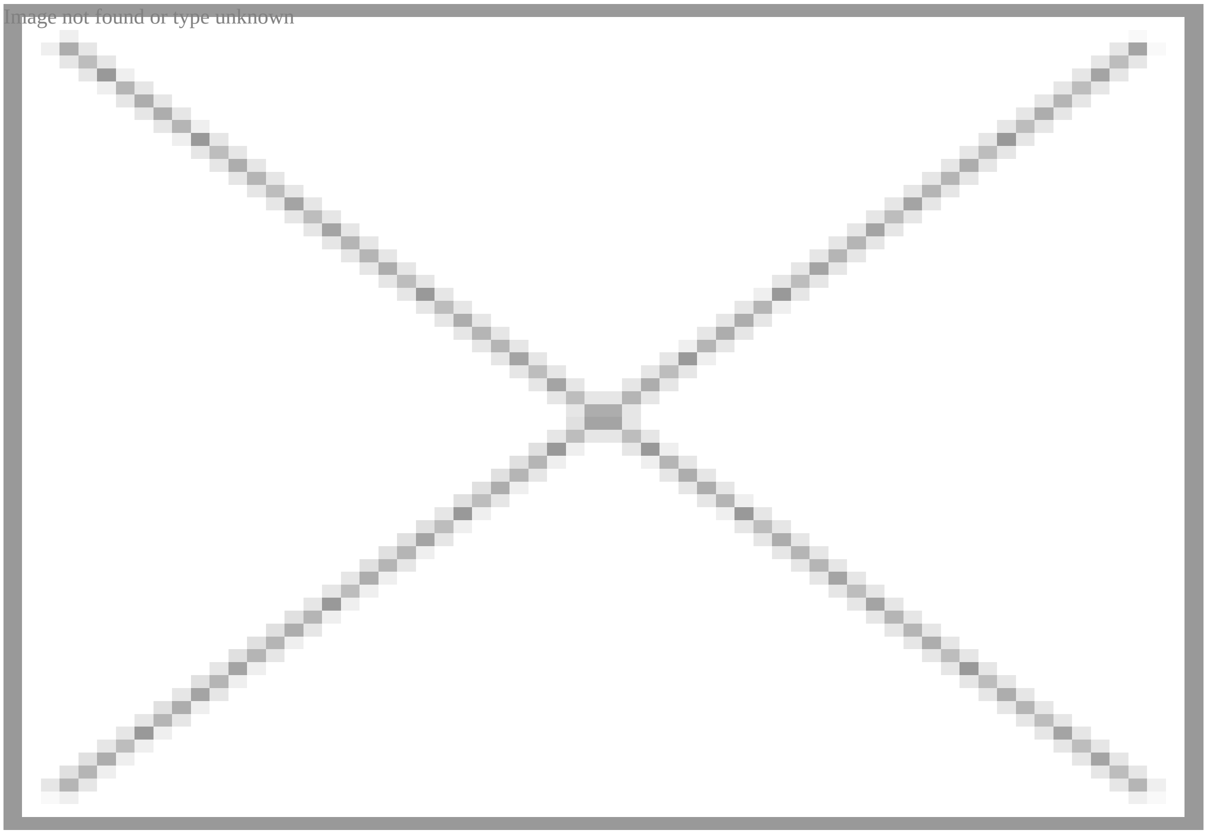
DOUGLAS HOLTZ-EAKIN | OCTOBER 5, 2010

The United States' economy has endured a severe recession and is currently growing too slowly. Accordingly, it is imperative that policy be focused on generating the maximum possible pace of economic growth. The estate tax is an important element of pro-growth tax policy. Recent research indicates that the estate tax has significant impacts on asset accumulation (and, thus, balance sheet repair), as well as the payroll and investment decisions of small and family businesses.

However, the future of the estate tax is up in the air. At present, the tax has been temporarily repealed, but in the absence of new legislation in 2011 the top effective tax rate will jump to 60 percent. A variety of proposals include top rates ranging from 35, to 45, to 65 percent.

This paper examines the impacts of a higher estate tax rate on asset accumulation, small and family businesses' cost of capital, investment outlays, desire to hire, size of payrolls and jobs. In each instance, raising the estate tax has significant negative impacts. In particular, letting the tax rate rise to 60 percent will cost as much as 1.5 million jobs, and even a more modest rate of 15 percent could diminish hiring by over 350,000 jobs (see Table). Other impacts on small and family businesses of increasing the tax rate from zero to 60 percent include:

- Raising the "hurdle rate" of return required for investment by 34 basis points,
- Reducing capital outlays by 7.8 percent,
- Decreasing the probability of new hiring by 8.3 percent, and
- Cutting the size of payrolls by 2.5 percent.



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