Estate taxes are applied to inherited wealth at the time it passes from the deceased to her or his inheritors. Prior to 2001, every state in the nation levied a state-level estate tax. Changes to federal estate tax laws that began to take effect in 2001, however, meant that states which did not "decouple" from these federal changes eventually lost a valuable state revenue stream. Today, twenty-one states and DC continue to levy estate taxes, generating over $4.5 billion annually.

By reforming current state-level estate tax laws, states have the potential to raise many millions of dollars to fund essential public programs. Given that only the very wealthiest families are subject to estate taxes, the new revenues can be collected exclusively from those households best able to contribute a bit more.

WAYS TO DO IT

**DECOUPLE FROM THE FEDERAL ESTATE TAX LAW**

"Decoupling" a state's estate tax law from federal law would allow states to avoid being impacted by changes to the federal law. For example, before 2001, the federal "pickup credit" gave tax filers a dollar-for-dollar credit against their federal estate taxes when paying their state's estate tax. Many states had tied their estate tax laws directly to this credit as defined in federal tax law. When the federal credit was phased out starting in 2001 and fully eliminated in 2005, 29 states no longer had an operating state-level estate tax. If those states decoupled from the federal changes and began collecting estate taxes again, as they did prior to 2001, together they would generate around $4 billion annually.

**LOWER THE AUTOMATIC EXCLUSION VALUE**

A common feature of state and federal estate tax law is to provide an “automatic exclusion”, which removes a portion of an estate from taxation. The size of this automatic exclusion greatly affects the amount of revenue collected through an estate tax. The pre-2001 federal rules set the automatic exclusion amount at $675,000 ($1.35 million for married couples), but have since raised that amount to $5.43 million ($10.86 million for married couples). The current, very high federal exclusion amounts mean that many large estates of wealthy families go entirely untaxed. States that decouple from federal estate tax laws can return to the pre-2001 federal exclusion amount or establish their own exclusion amounts, thus collecting significant revenue from these large estates.

**INCREASE TAX RATES ON ESTATES OF HIGHER VALUE**

Under a “graduated” estate tax structure, estates of lesser value are taxed at lower rates than are estates of greater value. States that decouple from the federal estate tax law and re-design their own system have the option of establishing a more progressive rate structure by adjusting the number and range of brackets and the tax rates applied to each.

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TALKING POINTS: STATE REVENUE STRATEGIES

Taxes are the way we pay for the many important things we do together through our governments. The common goal of the tax reform proposals presented on the Investing in the Future website is to generate revenue sufficient to pay for schools and universities, roads and bridges, subways and buses, police and fire departments, libraries and parks, and so much more.

Any proposal to generate new tax revenue, however, necessarily raises a number of important questions: How will these tax changes affect the state’s economy? How will the changes affect family budgets? How can proponents facilitate a thoughtful and constructive public discussion of the proposals at hand? Below is an overview of responses to each of these questions – greater detail can be found on the Background Basics page of the Investing in the Future website.

TAXES & THE ECONOMY

The evidence strongly indicates that when appropriate investments are paid for with well-structured tax increases they result in significant positive net impacts to a state’s economy, particularly over the long term.

- Raising taxes on high-income households = substantial net tax revenue gains
- Raising taxes on high-income households does not lead to substantial migration out-of-state
- States with higher tax levels do NOT have weaker economies than low-tax states
- Better educated workforce = higher wage economy

FAIRNESS

In every state in the U.S., low and middle-income households pay more of their income in combined state-and-local taxes than high-income households do. It is reasonable, therefore, that efforts to raise more revenue for education and other public investments would seek to collect that new revenue from high-income households. This would bring the tax levels of high-income households closer to the levels paid by other households.

The goal of tax reform is to generate adequate revenue to pay for essential government functions, and to raise that revenue in a fair way.

TALKING ABOUT TAXES AND GOVERNMENT

Thirty years of determined anti-tax/anti-government messaging has undermined the general public’s belief in the essential, positive role that government plays in our daily lives. The fact is, we do many great things – large and small - for our communities, working together through our federal, state and local governments. Telling this positive story is essential, just as it is essential to offer a positive, aspirational vision of the future:

- Help people imagine how their communities can benefit from increased investment in schools, roads, libraries, public safety and more.
- Remind people of the direct connection between these public goods and the taxes we all pay.
- Focus discussion on overall public benefit and revenue gains of a particular tax proposal rather than an extensive debate on the minor details of a given plan.
- Remember to stay positive and inclusive and to focus on the big picture: Tax reform is a tool that will help people realize the aspirational visions they have for their communities.

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