Testimony of Frank Clemente, Executive Director, Americans for Tax Fairness
Public Hearing on Internal Revenue Service Rule on Estate, Gift, and Generation-skipping Transfer Taxes: Restrictions on Liquidation of an Interest
(REG-163113-02)

December 1, 2016

Americans for Tax Fairness is a diverse coalition of 425 national and state endorsing organizations with a combined membership in the tens of millions.

I'm here in part to deliver a letter in favor of the valuation discount rule signed by 45 national organizations, which is an addendum to this testimony. The list of signers is diverse, ranging from think tanks to unions to religious groups to public interest organizations.

Americans for Tax Fairness also secured support for this rule from 18,930 of our members and supporters who sent comments to the Treasury Department urging that the rule be finalized. The letter of transmission used to place those comments into the regulatory record is also attached.

We are concerned that the wealthy and many large corporations avoid paying their fair share of federal taxes by taking advantage of sophisticated interpretations of the law and regulatory guidance. That is why we strongly support Treasury moving to address these instances of tax avoidance wherever possible and appropriate. The present Treasury action is just such a situation and represents a highly appropriate action on Treasury's part to protect the tax base and enforce the intent of the tax law in this area.

Strengthening the estate tax

The estate tax was implemented 100 years ago, to impose a check on the growing intergenerational concentration of wealth and to generate much needed revenue. Loopholes in the estate tax enable the wealthy to dodge paying their fair share of taxes. While the nominal tax rate on estates is 40%, the effective tax rate is currently only about 17% for all estates that are taxed and under 19% for estates above $20 million.

Over its century-long existence, the estate tax has been significantly more robust, with higher rates and lower wealth exemptions, than the last two decades. The efficacy of the tax as a brake on concentrated wealth has been undermined, both by legislation and loopholes.

The estate and gift taxes have become riddled with loopholes that the wealthy exploit eroding the intended scope and revenue-raising potential of these progressive taxes. Instituting the rule to close one of these loopholes—valuation discounts—is an important step toward restoring the estate and gift taxes to their intended scopes.

Much misinformation has been spread about the estate tax, some of it in testimony earlier today:

- Opponents claim it impacts low and middle income families. In fact, the federal estate tax is levied on an individual's estate worth more than $5.45 million (or $10.9 million for a married couple's estate). Estates worth less than those amounts pay nothing.
- Opponents claim it hurts small businesses and breaks up family farms. In fact, only about 20 small business and small farm estates in the entire country owed any federal estate tax in 2013, according to the Tax Policy Center.
- Opponents claim it disproportionately impacts racial minorities. It doesn't. The estate tax is paid by just the wealthiest 0.2% of estates in the country, fewer than 2 out of 1,000 estates. That's roughly 4,700 estates in any given year, according to the Joint Committee on Taxation.
- Opponents allege it is a form of double taxation. In fact, the bulk of assets in the biggest estates that are subject to the estate tax are unrealized capital gains that have never been taxed. No one who relies on a paycheck to make a living is impacted by the estate tax.

The valuation discount rule seeks to close a loophole that the ultra-wealthy exploit to dodge paying their taxes. Other explanations you may have heard today are intended to obscure this very basic fact.

Why address valuation discounts?

The valuation discount loophole enables estate planners to place assets in specially created companies and other entities for the sole purpose of reducing the asset's value for tax purposes. This technique can discount the value of assets by as much as 40%, artificially reducing the value of an estate below the taxable threshold.

Like many aspects of our tax code, the technical details are complicated but the concept is fairly simple. If I own an asset worth $100 million and I'm looking to dodge the estate tax using the valuation discount loophole that we are discussing today, here is how I'd do it.

I could create a limited partnership and place $100 million in assets in it. My wife and children also contribute assets. Because control of the partnership is disbursed among a group of people, our estate lawyers would argue the partnership interests would be harder to sell, and therefore each person's individual share should be assessed at a lower value. After I'm gone and my estate is taxed, my partnership interest could be discounted up to 40% using the valuation discount loophole. So, a $100 million asset becomes a partnership interest worth $60 million. With an estate tax of 40%, that's an estate tax break of up to $16 million.

For the ultra-wealthy households who take advantage of this loophole, there's no problem here. But for the overwhelming majority of families, this loophole means less revenue for vital public programs they depend on. The estate tax is the only time that this wealth is going to be subject to tax since the heirs will receive all bequests tax-free.

What is the impact of this tax cut giveaway to the wealthy? Consider that closing this loophole could generate up to an estimated $18 billion over 10 years. In essence, by giving an $18 billion tax break to the wealthiest households in the country, we are collectively choosing not to address serious and significant social problems.

For example, for less than $15 billion we could help end family homelessness by helping 550,000 homeless families with children pay for housing over the next 10 years at a cost of $11 billion. In addition, we could also help a million young people get their first job through partnerships with businesses and communities ($3.5 billion).

It is unconscionable that tax loopholes exclusively benefiting the very rich should be allowed to continue. We're hopeful that closing the valuation discount loophole is just the first of consistent efforts to preserve fairness and balance in the tax system, including by protecting the integrity of the estate and gift taxes.

Comments to the U.S. Treasury Department Supporting the Proposed Rule on the Estate & Gift Taxes Valuation Discount

TO: Internal Revenue Service, Department of the Treasury
RE: Comments on REG-163113-02, the Estate, Gift, and Generation-skipping Transfer Taxes; Restrictions on Liquidation of an Interest
DT: November 2, 2016

The 45 organizations that have signed these comments, which represent tens of millions of members, strongly support finalizing the proposed rule that would put an end to the "valuation discount loophole."

We are concerned that the wealthy and many large corporations avoid paying their fair share of federal taxes by taking advantage of sophisticated interpretations of the law and regulatory guidance. We strongly support Treasury moving to address these instances of tax avoidance wherever possible and appropriate. The present Treasury action is just such a situation and represents a highly appropriate action on Treasury's part to protect the tax base and enforce the intent of the tax law in this area.

The estate and gift taxes have become riddled with loopholes the wealthy exploit eroding the intended scope and revenue-raising potential of these progressive taxes. Instituting new rules to close one of these loopholes—valuation discounts—is an important step toward restoring the estate and gift taxes to their intended scopes. Treasury's proposed administrative action is important and hopefully the beginning, not the end, of such steps.

The estate tax was implemented 100 years ago to impose a check on the concentration of wealth held over long periods until the death of the family patriarch and to generate much needed revenue. Loopholes in the estate tax enable the wealthy to dodge paying their fair share of taxes. While the nominal tax rate on estates is 40%, the effective tax rate is currently only about 17% for all estates that are taxed and under 19% for estates above $20 million.

The valuation discount loophole enables estate planners to place assets in specially created companies and other entities for the sole purpose of reducing the assets value for tax purposes. This technique can discount the value of assets by as much as 40%, artificially reducing the value of an estate below the taxable threshold. The estate tax is the only time that this wealth is going to be subject to tax since the heirs will receive all bequests tax free. Closing this loophole could generate about $18 billion over 10 years.

By comparison, for less than $15 billion we could help end family homelessness by helping 550,000 homeless families with children pay for housing over the next 10 years ($11 billion), and help a million young people get their first job through partnerships with businesses and communities ($3.5 billion).

While closing this loophole is important, it should be followed by further action to close loopholes like the Grantor Retained Annuity Trust (GRAT), which can be done at least partially through executive action. The GRAT, a complex trust that enables the ultra-wealthy to dodge estate, gift and generation skipping taxes, may have cost an estimated $100 billion in lost revenue since 2000. It will also likely allow the heirs of at least one billionaire to dodge nearly $3 billion in taxes.

It is unconscionable that tax loopholes exclusively benefiting the very rich should be allowed to continue. We're hopeful that closing the valuation discount loophole is just the first of consistent efforts to preserve fairness and balance in the tax system, including by protecting the integrity of the estate and gift tax.

Sincerely,

AFL-CIO
Alliance for Retired Americans
American Association of University Women (AAUW)
American Federation of Government Employees
American Federation of State, County & Municipal Employees
American Federation of Teachers
Americans for Democratic Action
Americans for Tax Fairness, a coalition of 425 endorsing organizations
Bend the Arc Jewish Action
Campaign for America's Future
Center for Biological Diversity
Children's Defense Fund
Citizens for Tax Justice
Coalition on Human Needs
CREDO
Demand Progress
Economic Policy Institute
Friends of the Earth
Institute for Policy Studies, Program on Inequality
International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW)
National Association of Social Workers
National Education Association
National Latino Farmers & Ranchers Trade Association
National Low Income Housing Coalition

National Organization for Women
National Priorities Project
NETWORK Lobby for Catholic Social Justice
9to5, National Association of Working Women
National Women's Law Center
Other 98
Patriotic Millionaires
People's Action
Progressive Congress Action Fund
Public Citizen
Responsible Wealth
RESULTS
Service Employees International Union
Social Security Works
The Arc
Unitarian Universalists for Social Justice (UUSJ)
United for a Fair Economy
United Steelworkers
Voices for Progress
Working America
Working Families Party

AMERICANS FOR TaxFairness

Comments to the Internal Revenue Service on the "Valuation Discount Loophole"

November 2, 2016

Mr. John Koskinen, Commissioner
Internal Revenue Service
1111 Constitution Ave NW
Washington, D.C. 20224

Re: Comments on REG-163113-02, the Estate, Gift, and Generation-skipping Transfer Taxes; Restrictions on Liquidation of an Interest

Dear Mr. Koskinen:

Attached, please find comments submitted by 18,930 Americans for Tax Fairness members and supporters urging the Internal Revenue Service to put an end to the "valuation discount loophole."

We are concerned that the wealthy and many large corporations avoid paying their fair share of federal taxes by taking advantage of sophisticated interpretations of the law and regulatory guidance. We strongly support Treasury moving to address these instances of tax avoidance wherever possible and appropriate. The present Treasury action is just such a situation and represents a highly appropriate action on Treasury's part to protect the tax base and enforce the intent of the tax law in this area.

The comment to the IRS that our supporters signed reads as follows:

> The Estate Tax was meant to curb dynastic wealth, but over the years it has been riddled with loopholes, reducing its effectiveness. That is why I strongly support the U.S. Treasury Department's proposed rule that would close the "valuation discount loophole." This rule will strengthen the Estate Tax, generating up to $18 billion over 10 years. It will also require the wealthiest estates to pay a fairer share in taxes. I am hopeful that closing the valuation discount loophole is a sign of more actions by the Treasury Department to ensure that we have a fairer and more balanced tax system in the future.

Thanks for giving these comments every consideration during the review process.

Sincerely,

Frank Clemente
Executive Director
Americans for Tax Fairness