

# Summary

In this report, we summarize the last decade's research on the consequences of and attitudes toward inheritance taxation. Since the abolishment of the inheritance tax in Sweden in 2004, more than 30 Swedish research papers and reports have been written on different aspects of inheritances and the inheritance tax. We summarize these studies as well as the lessons learned from over a hundred international studies. The objective is to summarize the current knowledge about the pros and cons of inheritance taxation. Based on this knowledge we discuss how an inheritance tax might be designed for the Swedish context and what such a tax would be able to accomplish. Our conclusion is, however, that the possibilities of achieving intended policy goals, such as reducing economic inequality, by an inheritance tax, are limited.

## *History*

In the second chapter, we provide a historical description of the Swedish inheritance tax. Inheritances in Sweden were taxed for more than a hundred years before the tax eventually was abolished through two reforms in 2004. From the beginning of the 20th century until the late 1980s, the Government raised the tax rates successively, while from the 1990s rates were successively lowered. Although the highest tax rate exceeded 70 percent in the 1980s, the tax revenue remained modest. Over the years the tax revenue peaked at 0.3 percent of GDP but in the years before the abolishment the tax only generated revenues of around 0.1 percent of GDP. The many exceptions and special rules led to loopholes which facilitated tax planning and rendered the tax essentially toothless. One of the reasonings behind the abolishment was, according to the Government, that it was too difficult to design an appropriate tax.

*2003 – a snapshot*

In the third chapter, we describe the construction of the tax, just prior to its abolishment in 2004. The tax was associated with relatively low exemptions and was progressive with a top tax rate of 30 percent. Using data from the Belinda databases, we provide descriptive statistics of the magnitudes, composition and distribution of estates, inheritances and tax revenues. The analysis shows that estates and inheritances generally were small and that, consequently, only about a third of the inheritances were taxed and that average tax payments were small. A common feature of both the inheritances and gifts was that they were primarily received by close family members (children and spouses) and that these individuals made up the majority of the tax base.

*Inheritance taxation in other countries*

In the fourth chapter, we provide an international outlook over the use of inheritance taxes. In the last decades, several countries, including Norway and Austria, have abolished their inheritance taxes. Yet, most of the OECD countries still levy inheritance taxes, and in some countries the revenues as a share of GDP have even increased. Despite a substantial variation in the design of inheritance taxes across countries, the tax revenues are generally very small. Belgium raises the largest inheritance tax revenue, which amounts to 0.7 percent of GDP.

*Theory*

In the fifth chapter, we focus on the theory of inheritance taxation. The design of an optimal inheritance tax is associated with a trade-off between distributional concerns on the one hand, and efficiency losses on the other. How inheritance taxes affect the behavior of bequeathers and heirs, depends largely on the motives that govern savings and capital accumulation. If leaving inheritances is the by-product of people saving enough capital for unexpected expenditures during retirement, inheritance taxation should not affect capital accumulation. In that case, the tax may appear to be an

effective option in relation to other taxes. But if people save with the motive to bequeath wealth to others, the consequences of inheritance taxation could be substantial. As of today, there is no consensus on which motive that best explains why people leave bequests, which makes it difficult to design an optimal tax.

### *Behavioral effects*

In chapter six, we describe and discuss empirical studies on behavioral responses to inheritance taxes among those who give and those who receive inheritances. Because most responses to inheritance taxes depends on how the tax affects the size of the inheritance, we discuss the research on behavioral responses to both inheritances and inheritance taxes. The general finding seems to be that inheritance taxes lead to less savings among those who leave bequests, but that those who receive inheritances save more and increase their earnings as a consequence of the tax. We also review the literature on how inheritance taxation affects entrepreneurial activity and generational transfers of family firms, as well as gift giving and charitable bequests.

### *Tax avoidance and evasion*

In chapter seven, we discuss the literature on inheritance tax planning. Inheritance taxes are often easy to avoid through either legal or illegal planning. The empirical studies carried out in Sweden indicates that heirs to a large extent underreported the value of the decedent's assets in the estate report in order to avoid the tax. Legal planning among heirs, in the form of for example, tax favored inter vivo gifts, also seem to have been extensive. However, tax planning by bequeathers is less evident. Many easily available planning strategies, such as gift giving during life, appears to have been underused.

### *Inequality*

In chapter eight, we focus on the distributional consequences of inheritance taxation. While it at first may seem obvious that inheritance taxation should reduce economic inequality, research from several countries provide evidence that the tax, in fact, renders the distribution of wealth more unequal, at least in the short run. However, how the tax revenue is used is also critical for whether the tax lead to an increase or decrease in inequality. In Sweden, the inheritance tax appears to have contributed to increased wealth inequality, although it seems to have been of minor importance for economic inequality in general.

### *Attitudes towards inheritance taxation*

Inheritance taxes usually evoke strong emotions and opinions. In chapter nine, we discuss the research on peoples' attitudes towards inheritance taxation. Survey evidence shows that the Swedish tax was highly unpopular. Support for the tax is similarly low in many other countries, even in those where only very substantial inheritances are taxed. Why people are against a tax that is paid only by a few and benefit the many, is a puzzle to researchers in the field. While the aversion could be explained in part by ignorance, it appears as if the extensive possibilities for tax planning, especially for the rich, make people perceive the tax as unfair.

### *Conclusion*

In the final chapter, we discuss what the objective of an expedient inheritance tax may be and the most prominent trade-offs that policymakers must deal with. For example, it appears difficult to simplify generational transfers of family firms and at the same time avoid creating new possibilities to circumvent the tax. We also present a sketch of how an inheritance tax in Sweden could be constructed. We suggest a structure based on a flat tax rate of 20 percent, a basic exemption of one million SEK together with an additional income-based exemption, as well as a new means to simplify tax payment, without having to sell inherited business or

real estate. The sketch also includes incentives for charitable gifts. The design of the exemptions implies that the tax payable not only depends on the inherited amount, but also on the economic situation of the heirs. This feature makes the tax progressive in a way which is likely to enhance the redistributive possibilities of the tax. The suggested tax would, however, render very modest revenue according to our calculations.