APAC Agricultural Policy Analysis Center
The University of Tennessee

PolicyPennings by Dr. Daryll E. Ray

Do "death taxes" cause the death of family farms?

Judging by the amount of effort that some farm organizations have put into their support of eliminating the estate tax (also dubbed the death tax), one would think that most farm heirs are like the maiden in the typical silent film melodrama. As the piano player builds to a musical climax, the villain (played by the federal government's estate tax) tells the helpless maiden (read farm heirs) that if she doesn't give him the deed to the ranch he is going to tie her to the railroad tracks.

In an era of federal budget deficits it seems to us that it makes sense to determine how likely such a scenario is. Is the federal estate tax breaking up family farms and driving the next generation off the farm? The Congressional Budget Office examined that question in a report they completed in July 2005. The report is titled, "Effects of the Federal Estate Tax on Farms and Small Businesses," and is available online at www.cbo.gov/ftpdocs/65xx/doc6512/07-06-EstateTax.pdf.

The report shows that in 2000, the number of farm estates that had to file an estate tax return was 4,641 and of those a little over one-third (1,659) owed any estate tax at all. Of the 1,659 who owed estate taxes only 138 did not have sufficient liquid assets to immediately pay the taxes due. It should be noted that for farmers, the estate tax payments can be paid over as many as 14 years. The 2000 filings included the estates of persons dying in 1998, 1999, and 2000 and the exemption level varied from $625,000 to $675,000, according to the year of death.

If the exemption level were raised to $1.5 million, the number of farm estates required to file an estate tax return would shrink to 1,005 with just 300 of those having to pay any estate tax. Of that 300, only 27 would lack sufficient liquid assets to immediately pay the tax. At a $3.5 million exemption the numbers would be 187 tax returns, 65 owing any tax, and 13 with insufficient liquid assets to pay the estate tax liability. The CBO notes that its analysis "probably overestimate[s] the number of estates with taxes in excess of liquid assets because they do not reflect money held in trusts."

If we accept that the number of commercial farms in the US is around 500,000, then with a $3.5 million exemption, only 3-one thousandths of one percent of farms would be in jeopardy of having to sell some land to pay the taxes. These numbers also assume that at least one of the heirs wants to stay on the farm and continue the operation. In some cases the farm is broken up after death not because of taxes but because some of the non-farm siblings want to sell the land and invest the money in other ways.

It is often the lack of interest by family members to remain in farming that causes the break-up of family farms, not estate taxes.

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