

THE FEDERAL ESTATE TAX AND NONINDUSTRIAL PRIVATE LANDOWNERS

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ABSTRACT. Timber and land values have increased significantly in many areas of the U.S. in recent years, and in some circumstances heirs liquidate timber, or sell or develop portions of inherited timber and agricultural lands to pay federal estate taxes. To better understand how the estate tax is affecting timberland owners, a survey was conducted of members of the National Woodland Owners Association, the American Tree Farm System, and a random sample of landowners throughout the United States in 1999. Survey questions involved estate values, and estate tax liabilities that were incurred between 1987 and 1997. Respondents were asked if it was necessary to harvest timber, or to sell land to pay federal estate taxes. Responses were obtained from 1,905 people (a 33.5% response rate), and results indicate that the federal estate tax was a contributor to the conversion of forest and agricultural lands to other uses during this period. Two hundred and two of the 1,905 respondents were involved in an estate between 1987 and 1997. Forty-three percent of the estates exceeded the \$600,000 exemption that was allowed in those years; eight percent of the estates exceeded \$3 million and were taxed at the highest marginal rate. Almost twenty-seven percent of the estates paid federal estate taxes. Approximately twenty-eight percent responded that timber was harvested or land was sold to pay federal estate taxes.

KEY WORDS. Estate, Taxes, Nonindustrial Landowners

INTRODUCTION

There has been a lot of discussion about whether the federal estate tax has an impact on nonindustrial private landowners. Many case studies have been conducted showing the potential impact of the estate tax on a hypothetical landowner. Mississippi State University and the USDA Forest Service collaborated on a study to determine the current and potential impacts of the federal estate tax on nonindustrial private forest and agricultural lands. This study focused on whether the estate tax contributes to land-use conversion in the United States.

From 1987 to 1997 an estate could pass \$600,000 tax-free through the use of the unified credit. During this time, there was no indexing for inflation. There are two different viewpoints on whether estate taxes are a problem. Advocates of the estate tax cite figures from the Internal Revenue Service that show less than 2% of adult deaths result in a taxable estate. Opponents of the estate tax point to the number of small businesses that fold each year because of the estate tax. This study was designed to evaluate the effects of the federal estate tax on forest and agricultural lands from 1987 to 1997.

METHODS

The survey instrument was developed in the spring of 1998 with input from the USDA Forest Service, the Mississippi State University Social Science Research Center and faculty at Mississippi State University. A pilot test of the members of the Mississippi Forestry Association was conducted. Following the pilot test, changes were made to the survey instrument to clarify questions. The total design method (Dillman 1978) was used in all phases of survey design and implementation. The instrument contained seventeen questions focusing on the amount of the taxable estate and the methods used to pay the federal estate tax.

Surveys were mailed to 5,682 members of the National Woodland Owners Association, the American Tree Farm System and a random sample of landowners throughout the United States who were classed as "individuals". A cover letter stated that the survey was confidential. Follow-up surveys were mailed 1-2 weeks after the initial deadline passed. All surveys were individually coded to maintain confidentiality. Each landowner's name was cross-referenced to a code corresponding to the organization and the landowner.

Responses were entered into a spreadsheet by the number coded on the questionnaire. Responses were grouped by the answer to question number five: "*What was the value of the taxable estate?*" Descriptive statistics were calculated on the responses.

To determine if non-respondents differed from respondents, a survey of non-respondents is being conducted. A sample of members who did not respond will be contacted by phone, and asked a sample of the questions from the questionnaire.

RESULTS AND DISCUSSION

A response rate of 33.5% resulted from the 5,682 questionnaires that were mailed. Of the people who responded, almost 11% had been involved in the estate of a nonindustrial private landowner during the period of 1987-1997. Respondents that had not been involved in an estate were instructed to return the survey but not to fill out the remainder of the questionnaire. The respondent's relationship to the decedent ranged from spouse or child to the decedent's accountant, lawyer or forester.

Value of the taxable estate. Respondents who had been involved in an estate were asked to indicate the value of the taxable estate by choosing from ranges that corresponded to the tax brackets for the federal estate tax. Fifty-seven percent of the responses (110 responses) indicated a taxable estate value less than \$600,000. Because the estate had a value of less than \$600,000, no federal estate tax was due. Eight percent (16) of the respondents reported a taxable estate in excess of \$3,000,000. This was the highest tax bracket (55%) for the federal estate tax during this period. Figure 1 shows the number of estates in each tax bracket.

Amount of tax paid. Respondents were asked to indicate the amount of tax paid on the estate by choosing from ranges that corresponded to the tax brackets for the federal estate tax. Of 185 responses to this question, almost 27% (49 respondents) paid tax. The amount of tax paid ranged from one dollar to over \$1,098,000. Figure 2 shows the number of respondents paying tax in each tax bracket. A total of 136 estates reported paying no tax. Eighteen of those estates had a taxable value of over \$600,000. Of the 8% that indicated a taxable estate in excess of \$3,000,000, only half paid taxes in that bracket. No explanation was provided as to how the estate reduced or avoided taxation.

Method of payment. Respondents who indicated that an estate tax was paid were next asked how taxes were paid. The questionnaire described five situations and the respondent was to indicate the appropriate statement(s). Of the 49 estates that paid taxes, 66% used assets other than land or timber to pay the tax. Ten percent responded that timber was harvested to pay the tax. Another 18% sold land to pay the estate tax. There were cases where the estate had used other assets and harvested timber.

Number of acres sold or harvested. Respondents who indicated that timber was harvested or land was sold to pay the tax were asked to report the number of acres that were affected. Of the five respondents who indicated that timber was harvested, three reported that timber was clearcut. The total acreage of clearcuts for the three respondents was 905 acres. Another three respondents replied that 1.120 acres were thinned. Seven respondents indicated the amount of land that was sold to pay the tax. The total amount sold was 2,220 acres.

Use of professional estate planning services. The final questions asked whether the decedent had used professional estate planning services. Of the 194 responses to this question, 31% had not used professional estate planning services. One percent (3) did not know if planning had been done. Many respondents commented that some providers of the estate planning services had either given bad advice or over-charged the client.

CONCLUSION

Estate taxation is an area of concern for landowners and foresters throughout the United States. Forty-three percent of those surveyed with involvement in an estate reported estate values over the \$600,000 exemption in effect from 1987 to 1997. Twenty-eight percent of the respondents that paid tax sold land or harvested timber. The majority of the estates in our survey had conducted some form of professional estate planning. Landowners should be encouraged to have their property appraised on a periodic basis. Those landowners who are approaching the exemption amount should be encouraged to seek professional planning assistance.

LITERATURE CITED

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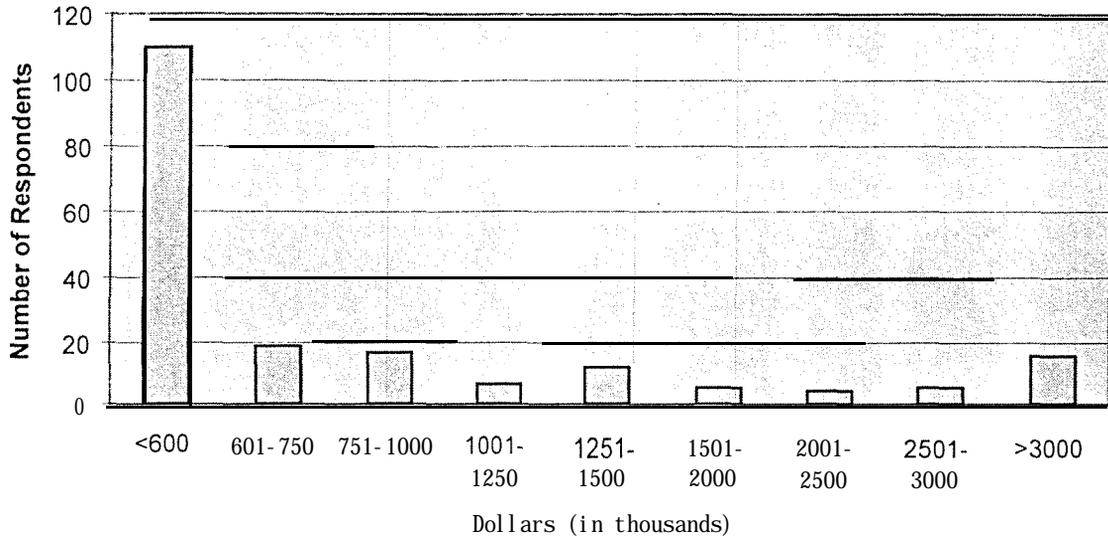


Figure I. Number of estates in each tax bracket.

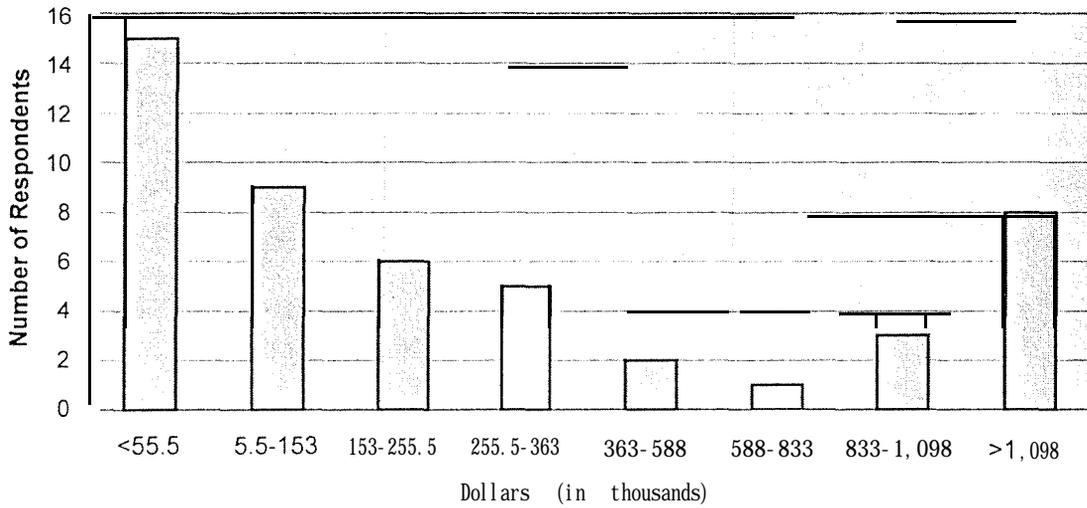


Figure 2. Amount of estate tax paid.