New Life For Death Taxes?

They say the only certainties in life are death and taxes, whilst marrying the two is truly the last nail in the coffin felt by a nation's wealthy. Such a view of death, estate or inheritance taxation was certainly held in Queensland when it kick started a race to the bottom through a complete abolishment of its inheritance tax in 1976. The other States and Territories fearing mass migration to the sunshine State quickly followed suit and the nation was devoid of any inheritance taxation by 1979. Since 1979 Australia has had no federal or state run inheritance taxation scheme whilst inequality as measured by the Gini coefficient and P90/P10 ratios have been trending upwards[1]. The diminishing marginal utility of wealth ensures such inequality is inefficient for a utilitarian society, whilst a Rawlsian analysis also calls for redistribution albeit for the purpose of raising the absolute living standards of the least advantaged members of society. Further problems of intergenerational economic inequality arise when the divergent momentum of inequality[2] is coupled with a political system sympathetic to private donations. In any case it is commonly agreed that ceteris parabis a fairer more equitable distribution of societies resources and opportunities is desirable. Unfortunately with taxation, all other things are never constant and like any tax, an inheritance tax must fight off criticisms pertaining to its distortionary nature.

One of the main criticisms of taxing the bequeathment of one individual to another is that it distorts the incentives of the individual leaving the inheritance behind. If we were to imagine taxing inheritances at 100% the effect becomes clear. People would be incentivised to frivolously spend their money before death, perhaps only keeping enough to ensure a comfortable survival. The decision to migrate investments and savings to more frivolous consumption could have dire impacts on the economy. Capital stocks and future projects funded by savings would decrease, with real GDP following closely behind. Such an analysis brings light to the inherent economic trade off between GDP and equality, although ignores the inherent distortionary nature of giving someone a large inheritance. A large endowment received through inheritance may have an income effect of societies statistically most productive. This may occur when privileged inheritance recipients high in human capital, buy more leisure (and thus work less) shrinking the economy. In this case inheritances are uniquely distortionary with or without tax. A progressive inheritance tax as seen in most OCED countries[4] would allow someone to save, invest and bequeath monetary gifts to loved ones whilst taking a portion to create a more equitable and fairer society. It is for this reason among others that Australia should breath new life into the death tax debate.