American Business Defense Foundation

The Federal Estate Tax, Family Businesses and Jobs 2018 and Beyond

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Executive Summary

In the Tax Cuts and Jobs Act of 2017, it was the intent of the White House and the House of Representatives to achieve permanent repeal of the Federal Estate Tax. Those plans were altered by the Senate. The final outcome was to double the exemption of the Estate Tax from $5.58 million to $11.16 million from 2018 until 2026.

What does this mean for families, family businesses, farms and ranches? What does it mean for jobs and employment numbers? How many jobs would be added to the American economy if the Federal Estate Tax were repealed altogether?

Jobs from Family Businesses, Farms & Ranches. The 2.3 million family-owned business, farms, and ranches represent 29% of all firms with employees in the U.S. They provide a total 49 million jobs.

Family Businesses and the Estate Tax. Analysis shows that under the 2018 tax law as many as 36,000 family business providing up to 32.1 million jobs qualify to pay Federal Estate Taxes when the family business owner dies.

Jobs Lost. This analysis reveals that in the coming generational cycle, up to 11.6 million jobs will be lost when family businesses are liquidated to pay the Federal Estate Tax.

More Jobs by Repealing the Federal Estate Tax. If the Federal Estate Tax were repealed, it would increase employment levels of up to 380,000 new jobs each year in the United States.

Conclusion. While up to 1.5% of family businesses are eligible to pay the Federal Estate Tax, they provide two-thirds of all family business jobs. While this onerous tax is paid by thousands of grieving family members, it affects millions of working American families through job destruction and lower wages.

The Tax Cuts and Jobs Act of 2017 dramatically changed the Federal Estate Tax. While many studies have been written and published on the effects of the Federal Estate Tax over the years, changes in tax law, changes in the rates of business ownership, and changes in wealth all contribute to the need for updated estimates of the effects of the estate tax on jobs and businesses. If we are to seriously deal with the legislative issues surrounding the Federal Estate Tax, we need to revisit questions: How many family businesses, farms and ranches are eligible to pay the new Federal Estate Tax? How many jobs do they provide? What is the jobs effect of the new tax law? Perhaps most importantly, how many new jobs each year would be added to the U.S. economy if the Federal Estate Tax were completely repealed? Each of these questions are addressed in this paper.

The Survey of Business Owners and Self-Employed Persons (SBO) is a periodic census of non-farm U.S. Businesses conducted by the U.S. Census Bureau.[1] The data include numbers of employees, sales, and annual payrolls, arranged by industry category, gender, ethnicity, race, and veteran status of the business owner, and whether the business is family-owned. SBO classifies a business as "family-owned" if two or more members of one family own a majority of the business, where "business" includes entities reporting any business activity on IRS forms 1040 Schedule C (proprietorships), 1065 (partnerships), any of the 1120 corporate tax forms, or 941 or 944 employer tax returns.[2] The SBO counts firms, not establishments. A firm is a business organization consisting of one or more domestic establishments under common ownership or control.

[1] https://www.census.gov/programs-surveys/sbo/technical-documentation/methodology.2012.html
[2] The survey asks, "…did two or more members of the same family own the majority of this business? *(Family refers to spouses, parents/guardians, children, siblings, or close relatives.)*" (https://www.census.gov/programs-surveys/sbo/technical-documentation/methodology.2012.html)

According to the Small Business Administration (SBA), the number of firms with employees in the U.S. was 5.83 million in 2014.[3] That number has been growing at a median annual rate of 0.7 percent since 1997. Applying that median growth, we can estimate that there are approximately 6 million firms in the U.S. as of 2018.

As of 2012 and according to the latest SBO data, family-owned businesses represented 29 percent of all U.S. firms with paid employees.[4] That number is down from 36 percent in 2007.[5] Applying the 29 percent to the 6 million firms with employees, we can estimate that there are 1.8 million family-owned non-farm firms with paid employees in the U.S. as of 2018.

While the SBO excludes farms and ranches (hereafter, "farms") from its survey data, the U.S. Census compiles the Census of Agriculture (COA), a periodic census of farms conducted by the USDA.[6] According to the latest COA census, there were 1.9 million family-owned farms in the U.S. as of 2012.[7,8] Of these, 490,000 had paid employees. Combining the SBO and COA data yields an estimate of 2.3 million family-owned businesses with paid employees.

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[3] https://www.sba.gov/advocacy/firm-size-data
[4] https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=SBO_2012_00CSCB04 &prodType=table
[5] https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=SBO_2007_00CSCB04 &prodType=table
[6] https://www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1,_Chapter_1_US/
[7] https://www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1,_Chapter_1_US/st99_1_067_067.pdf
[8] The USDA combines family-owned and individual-owned farms into a single category.

How many jobs do family businesses provide?

SBO surveys firms to produce an estimate of the number of firms that satisfy various demographic criteria. Combining SBO survey results with data from the Federal Reserve Economic Data (FRED) database at the Federal Reserve Bank of St. Louis yields census estimates.

For example, according to the most recent SBO survey, family businesses account for 38 percent of U.S. private sector jobs.[9] The FRED database shows 126.3 million non-farm private sector employees in the US economy as of May 2018.[10] Assuming that the fraction of workers employed by family-owned businesses has not changed, the number of workers employed by non-farm family-owned businesses as of May 2018 is approximately 48 million.[11]

According to the latest COA census, the 490,000 family-owned farms with employees employ a total of 2.0 million workers. Approximately 67 percent of these workers worked less than 150 days out of the year. The census reports the remainder not as full-time, but as working "150 days or more." If we count the 33 percent that worked 150 days or more as working year-round, and the 67 percent that worked less than 150 days as working one-quarter of the year, the full-time-equivalent number of workers among all family-owned farms is approximately 1.0 million.

Total private payroll in 2014 was $5.9 trillion.[12] Nominal GDP has grown at approximately 3.6% annually from 2014 to 2018. Applying this same annual growth, total private payroll in 2018

[9] This fraction is based on firms that either identified as "family-owned" or "not family-owned."
[10] https://fred.stlouisfed.org/series/NPPTTL
[11] According to SBO data, the fraction of private-sector workers employed by family-owned businesses was 42% in 2007.
[12] https://www.sba.gov/sites/default/files/advocacy/static_us_14.xls

will be approximately $6.8 trillion. As family-owned businesses account for 36 percent of private sector payrolls, total payroll in 2018 paid by family-owned businesses is approximately $2.4 trillion.

	Family-Owned Farms	Family-Owned Non-Farms	Total
Firms with paid employees	0.5 million	1.8 million	2.3 million
Total employees	1.0 million	48 million	49 million

How are family-owned business demographics different?

The SBO survey asks for the business owner's gender, which allows for a comparison of female-owned family businesses to female-owned non-family businesses. The SBO data indicate that female-owned family businesses are (relative to male-owned businesses) more numerous, produce more, employ more, and pay more than do female-owned non-family businesses. Female owners of firms with paid employees are more common among family businesses (27.8% female, 72.2% male) than among non-family businesses (22.6% female, 77.4% male). This contrasts with the approximately 6 percent of Fortune 500 companies that are headed by women.[13] Female business owners employ a significantly larger proportion of workers among family businesses (21.4% employed by female-owned, 78.6% employed by male-owned) than among non-family businesses (15.5% employed by female-owned, 84.5% employed by male-owned).

Female-Owned Firms as a Fraction of Female- and Male-Owned Firms				
	Number of Firms with Paid Employees	Output with Paid Employees	Number of Paid Employees	Annual Payroll
Family Business	27.8%	16.0%	21.4%	19.1%
Non-Family Business	22.6%	9.8%	15.5%	11.6%

[13] https://www.washingtonpost.com/news/on-leadership/wp/2017/06/07/the-number-of-women-ceos-in-the-fortune-500-is-at-an-all-time-high-of-32

How many jobs do family business that qualify for the estate tax now provide?

In 2016, there were 12,411 estates tax filings. Of these, 5,219 owed estate tax. The table below shows the number of filings that included business assets that are associated with family businesses.[14]

All Estate Tax Returns	Closely held stock	Real estate partnerships	Limited partnerships	Other non-corporate business assets	Farm assets
Filed	3,442	2,498	3,608	3,034	1,731
Owed estate tax	1,263	960	1,556	1,097	682

To account for the current $11 million exemption, we can exclude from the 2016 filings estates that were smaller than $10 million in gross value. In 2016 and among estate tax filings listing gross estates of at least $10 million, there were 4,142 filings, of which 2,204 owed estate tax. The table below shows the number of filings for these larger estates only.

Estate Tax Returns Over $10 Million	Closely held stock	Real estate partnerships	Limited partnerships	Other non-corporate business assets	Farm assets
Filed	1,562	1,146	1,656	1,458	590
Owed estate tax	748	562	876	674	305

Let us call a family business that is part of an estate worth at least $10 million, a "high-value family business." Given data limitations, it is not possible to know the value of the business itself, only the value of the estate to which it belongs. Consequently, it is possible, though less likely, that a given "high-value family business" is actually worth a small amount if that business comprised a small fraction of an estate's value.

[14] https://www.irs.gov/statistics/soi-tax-stats-estate-tax-statistics-filing-year-table-1

Where there is a family business, one would expect to find assets among the categories listed in the table. However, the presence of assets in these categories does not imply that an estate contains a portion of a family business. For example, real estate partnership assets may or may not be part of a family-owned business. The SBO data show that 29 percent of firms with paid employees are family-owned businesses. Applying that same fraction to the estate tax data in the table above, and assuming that all high-value family businesses involved in estate tax filings have paid employees, yields an estate of the number of estate tax returns that involved high-value family-owned businesses.

Estate Tax Returns Over $10 Million Involving Family-Owned Businesses (estimated)	**Closely held stock**	**Real estate partnerships**	**Limited partnerships**	**Other non-corporate business assets**	**Farm assets**
Filed	453	332	480	423	171
Owed estate tax	217	163	254	195	88

An estimate of the number of high-value family businesses listed on returns that owed the estate tax is the number of estates that owed the estate tax, and that owned assets in at least one of the five categories above. This estimate will slightly over count high-value family businesses to the extent that more than one owner of a single jointly owned family business dies in the same year. This could trigger two estate tax filings, though only one family business would have been affected. The probability of this is small enough to be ignored.

Because a single filing may show assets in more than one asset category, it is not possible to determine how many estates owned assets in at least one of the five categories. What we do know is that the number is, at the least, the largest of the numbers appearing in the five categories and, at the most, the sum of the numbers appearing in the five categories. Therefore, we can estimate

that in 2016, between 480 and 1,859 estate tax filings involved high-value family businesses, and between 254 and 917 of those owed estate taxes. As of 2018, there are approximately 2.3 million family-owned businesses with paid employees in the U.S.[15] Based on the above estimates, high-value family businesses with paid employees represent between 0.02 percent and 0.08 percent of all family businesses with paid employees. Those that also contributed to an estate owing estate taxes represent between 0.01 percent and 0.04 percent of all family businesses with paid employees.

Family Businesses with Paid Employees (estimated)	Lower Limit	Upper Limit
Filed estate taxes in 2016	480	1,859
Owed estate taxes in 2016	254	917

But these estate tax figures capture only those businesses whose owners died in the previous year. What is relevant is not the number of family businesses that triggered an estate tax filing, but the number that *would have* triggered a filing if their owners had died. Let us call the businesses that would have triggered an estate tax filing if their owners had died, businesses that *qualify* for the estate tax.

This number is important because the estate tax has several effects, only one of which is manifest upon the business owner's death. The first, and most obvious effect, is paying the estate tax upon the owner's death. Paying the estate tax can cripple businesses because the tax owed is based on the value of the business, regardless of liquidity. A business whose value is concentrated in buildings, land, and machinery may find itself having to sell these productive assets so as to raise money needed to pay the tax. A second, less noticed effect is that anticipation of the estate tax

[15] https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=SBO_2007_00CSCB04 &prodType=table

gives the owner an incentive, while still living, to reduce the amount he might otherwise have invested in the business. Any tax reduces the production of the thing being taxed. So too here, anticipation of owing the estate tax reduces the owner's incentive to invest in the business. A business owner who anticipates triggering the estate tax will divert resources that otherwise would have gone into expanding the business so as to better prepare heirs to be able to pay the estate tax when the owner dies. A third, perhaps more insidious, effect is that the estate tax creates an incentive for business owners to avoid growing their businesses to a size that would qualify them for the estate tax in the first place. This effect does not show up in the data precisely because these business owners deliberately prevent their businesses from becoming large enough to qualify for the estate tax.

In a study of 1,003 family businesses, more than 60 percent of business owners reported that paying estate taxes will limit their business' growth.[16] Sixty-four percent said that paying estate taxes will threaten their business' survival. Sixty percent reported that they would immediately hire more workers if the estate tax were eliminated. When this survey was conducted, the estate tax exemption was lower ($600,000 versus $11 million today), and the estate tax rate was higher (55 percent versus 40 percent today).[17] However, these differences affect the number of family businesses that anticipate having to pay the estate tax, not necessarily the fact that the businesses anticipate it. This comports with economists' belief that the estate tax is really a tax on capital

[16] Astrachan, Joseph H., and Roger Tutterow. "The Effect of Estate Taxes on Family Business: Survey Results." Family Business Review 9.3 (1996): 303-14.
[17] https://taxfoundation.org/federal-estate-and-gift-tax-rates-exemptions-and-exclusions-1916-2014/

because of the effect on businesses.[18] A 2009 study estimated that fully repealing the estate tax would create 1.5 million jobs.[19]

In 2010, 2 million people age 55 or older died in the U.S., out of a population of 77.5 million people age 55 or older. Thus, the number of people age 55 or older who did not die in 2010 is 38 times the number who did die. Assuming mortality rates among business owners are the same as among non-business owners, that mortality rates among business owners who qualify for the estate tax are the same as among business owners who do not, and that no business owner under age 55 would qualify for the estate tax, at least 38 times the number of businesses qualified for the estate tax in 2016 as triggered an estate tax filing in 2016.[20]

These calculations pick up the generational effect of the estate tax. The distortionary effect of the estate tax begins before the owner dies, as the owner diverts some of the business' productive resources so as to mitigate the tax. When the owner dies, not only must the heirs divert further productive resources to pay the tax, but the businesses they inherit are commensurately weaker because of the earlier attempts to mitigate the tax. These effects compound as the business is passed down through multiple generations. Importantly, these effects do not exist for widely held corporations. Heirs of shareholders who owe estate taxes might sell shares to raise money to pay the tax, but doing so has no effect on the corporation. With each passing generation, the estate

[18] Robert Carroll et al., "Personal Income Taxes and the Growth of Small Firms," National Bureau of Economic Research, October 2000.
[19] Douglas Holtz-Eakin and Cameron T. Smith, "Changing Views of the Estate Tax: Implications for Legislative Options," American Family Business Institute, February 2009.
[20] The actual number is slightly less than 66 due to the chance that more than one owner of a single jointly owned family business may die in the same year. This would be an opportunity for two estate tax filings but only one family owned business would be affected. The probability of this is small enough to be ignored.

tax eats away at the productive resources of family businesses but not at the resources of large corporations.[21]

Applying the 38x magnification factor to our earlier numbers, the number of high-value family businesses with paid employees that qualify for the estate tax is between 19,000 and 72,000 (between 0.8% and 3.1% of all family businesses). The number that qualify to owe estate taxes is between 10,000 and 36,000 (between 0.4% and 1.5% of all family businesses).

High-Value Family Businesses with Paid Employees (estimated)	**Lower Limit**	**Upper Limit**
Qualify to file estate taxes	19,000	72,000
Qualify to owe estate taxes	10,000	36,000

The important question now is how many jobs the family businesses that qualified for estate taxes represent. Estimates of the number of employees at firms affected by the estate tax is complicated by the fact that firms that are more likely to qualify for the estate tax will have a greater market value, and so will be more likely to employ larger numbers of workers. The distribution of firms according to the numbers of workers the firms employ is given in the table below. The data are for 2014, the latest year available.

Census Category	**Number of Firms**	**Average Employees per Firm**	**Fraction of Firms**
0-4 employees	3,598,185	2	61.8%
5-9 employees	998,953	7	17.1%
10-19 employees	608,502	13	10.4%
20-99 employees	513,179	39	8.8%
100-499 employees	87,563	195	1.5%
500+ employees	19,076	3,312	0.3%

[21] Yakovlev, P. and A. Davies, 2014. How Does the Estate Tax Affect the Number of Firms? Journal of Entrepreneurship and Public Policy, 3(1): 96-117.

This table shows that the top 0.3% of firms, according to numbers of employees, employ an average of 3,312 workers per firm. The next 1.5% of firms employ an average of 195 workers per firm. If we assume that the distribution of job numbers among family businesses with paid employees matches the distribution of job numbers among all firms, then we can use the distribution among all firms to estimate the number of workers employed by the most valuable family businesses. From the table, we can calculate the average number of employees per firm for firms in any percentage bracket.

We have estimated that the top 0.8% to 3.1% of all family businesses qualify to file estate taxes, and that the top 0.4% to 1.5% qualify to owe estate taxes. Applying these numbers to the above table, we can estimate that the number of employees at family-owned businesses that qualify to file estate taxes is between 27.6 million and 32.8 million, and the number of employees at family businesses that qualify to owe estate taxes is between 25.8 million and 32.1 million.

	Top % Firms by Employees	Average Employees per Firm	Firms	Employees
Firms that qualify to file estate taxes (estimated)				
Lower Estimate	0.8%	1,457	19,000	27.6 million
Upper Estimate	3.1%	456	72,000	32.8 million
Firms that qualify to owe estate taxes (estimated)				
Lower Estimate	0.4%	2,580	10,000	25.8 million
Upper Estimate	1.5%	892	36,000	32.1 million

This analysis assumes that the number of workers the firm employs is an adequate proxy for the value of the firm. The employee numbers in the table above represent the total number of employees employed by firms that qualify for the estate tax. Only a fraction of those would be in danger of losing their jobs if the business that employed them were passed on to heirs.

In a 1995 survey, 36 percent of owners of family-businesses claimed that paying the estate tax would require liquidating all or part of their businesses.[22] In 1995, the estate tax exemption was, adjusting for inflation, lower than in 2016. However, the estate tax rate was higher. The number of estate tax filings as a fraction of employer firms in 1995 was 6.6 times what it was in 2016.[23] However, the average estate tax owed per filing in 2016, after adjusting for inflation, was 5.6 times what it was in 1995.[24] In total, federal estate and gift taxes collected in 1995 were, adjusted for inflation, approximately the same as those collected in 2016.[25] Though we can expect the number of family businesses that owe the estate tax today to be less than it was in the past, we can also expect the tax per business that owes estate taxes to be greater. As larger firms will, on average, employ more workers, it is unclear whether the 36 percent survey result is too high, too low, or about right for today's family businesses.

Absent other data, we can use the 36 percent survey estimate as a starting point. Applying this figure to the above estimates of the number of employees working at firms qualifying to owe estate taxes yields, on the low end, 9.3 million and, on the high end, 11.6 million jobs that will be lost when these qualifying business' owners die.

	Lower Limit	**Upper Limit**
Jobs That Will Be Lost When Existing Family Businesses Are Liquidated to Pay the Estate Tax (estimated)	9.3 million	11.6 million

[22] Astrachan, Joseph H., and Roger Tutterow. "The Effect of Estate Taxes on Family Business: Survey Results." Family Business Review 9.3 (1996): 303-14.
[23] In 1995, 31,563 estates owed taxes versus 5,219 in 2016.
[24] In 2016, the average net estate tax owed was $3.5 million per estate that owed taxes. Adjusted for inflation, the figure for 1995 was $627,000.
[25] https://www.whitehouse.gov/omb/historical-tables/

How many family business jobs could be saved by eliminating the estate tax?

A panel data study of the effect of growths in the estate, inheritance, and gift taxes on the number of firms estimated that a ten-percentage point increase in the tax per decedent is associated with a 0.02 percentage point slowing in the growth rate of the number of firms.[26] Based on these results, a 40 percentage point reduction in the estate tax (for example) can be expected to be followed by a 0.8 percentage point increase in the growth in the number of family businesses. At 48 million employees, and an average of 21 employees per firm, that is the equivalent of an additional 380,000 jobs annually.

This figure is commensurate with the figures in the previous table. The previous table shows the estimated number of jobs that will be lost when existing family businesses are inherited and, in whole or in part, liquidated to raise money to pay the estate tax. Thus, the job losses shown in the table are estimated to occur over the course of a generation. Counting a generation as 25 years, the job losses in the previous table are the equivalent of between 370,000 and 460,000 annually.

[26] Yakovlev, P. and A. Davies, 2014. How does the estate tax affect the number of firms. Journal of Entrepreneurship and Public Policy, 3(1): 96-117.