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Estate Taxes

New Jersey Estate Tax Debate Thickens: Higher Threshold or Five-Year Phaseout?

Estate planners say New Jersey is one of the worst places in the country to die.

The Garden State is one of just two states—the other is Maryland—with both an estate tax and an inheritance tax. Unlike with federal estate tax rules, a surviving spouse in New Jersey can't inherit the deceased spouse's unused estate tax exemption. And New Jersey's \$675,000 estate tax threshold is the lowest in the nation, falling well below the current \$5.45 million federal exemption and lagging behind six-figure thresholds in other states.

"We're probably one of the worst states as far as the imposition of death taxes," Wendy Wolff Herbert, a partner at Fox Rothschild LLP in Princeton, N.J., told Bloomberg BNA April 19. "Many people are subject to the tax who don't consider themselves particularly wealthy."

Critics of the estate tax say it is one of many tax burdens in New Jersey that drive people out of the state. In his February budget address, Gov. Chris Christie (R) pressured lawmakers to repeal the estate tax, blaming it for an outflux of 2 million people in the past 10 years. Calls to revamp the estate tax got louder in April after news broke that billionaire hedge-fund manager David Tepper had moved from New Jersey to tax-friendly Florida, taking potentially millions of annual income tax revenue with him (2016 Weekly State Tax Report 27, 2/19/16) (2016 Weekly State Tax Report 41, 4/8/16).

Since January, New Jersey lawmakers have introduced no less than 10 different proposals to phase out or otherwise change the estate tax. While many lawmakers agree that the estate tax is a problem, they haven't yet agreed on how to fix it. Debate intensified April 18 after Assembly Speaker Vincent Prieto (D) spoke out against the only bill to come up for a committee vote, a bipartisan proposal that would increase the estate tax exclusion and then phase it out over five years. The same day, Sen. Jennifer Beck (R) suggested that raising the threshold to \$2.5 million would be a better long-term solution.

Costly Change. Those who want to keep the estate tax say the state simply can't afford to eliminate it. New Jersey's inheritance and estate taxes combined are expected to generate \$828.5 million in fiscal 2016, making it the fourth-largest source of state tax revenue, accord-

ing to the most recent tax and revenue analysis from the Office of Legislative Services (OLS).

Progressive policy organizations such as New Jersey Policy Perspective say elimination of the estate tax would take \$300 million per year away from colleges, health care and other social services.

In a January report, the group argued against the idea that tax impacts middle-class households, noting that only 4 percent of estates in New Jersey ever owe any estate tax, and most who pay the tax are wealthy.

During an April 18 news conference, Prieto said that while he would be open to increasing the threshold on the estate tax, he didn't want to eliminate it.

"That's not something we can repeal right off the bat because that would leave a \$400 million hole in our budget," he said.

S. 1728. Yet the only estate tax proposal that has moved beyond committee seeks to repeal the tax entirely.

S. 1728 (A. 3562), sponsored by Sen. Steven Oroho (R) and Sen. Paul Sarlo (D), was approved by the Senate budget committee Feb. 29 by a vote of 9-0, with four abstentions.

The bill seeks to eliminate the estate tax after a five-year phaseout, first by increasing the \$675,000 threshold to \$1 million in January 2017, then increasing the exclusion to \$2.5 million in 2018, \$3.5 million in 2019 and \$5 million in 2020. In 2021, the tax would be eliminated.

Sarlo suggested during budget hearings April 19 that the bill could be part of a larger package to help resuscitate New Jersey's languishing Transportation Trust Fund, which is going to run out of money on June 30. The package would combine the phase out of the estate tax and other tax breaks with a gas tax increase to raise transportation funding. Legislators have suggested in the past that a gas tax hike could be more appealing if it were combined with corresponding cuts in estate taxes.

In a fiscal note accompanying S. 1728, the OLS estimated the bill would reduce annual estate tax revenue by \$120 million in fiscal year 2018, \$245 million in FY 2019, \$300 million in FY 2020, \$365 million in FY 2021 and \$550 million in FY 2022, at which point the estate tax would be fully repealed.

\$2.5M Exclusion. On April 18, Beck suggested that simply increasing New Jersey's threshold to \$2.5 million would eliminate most of the problems.

Of the 15 other states in the country that have an estate tax, the filing exemptions range from \$1 million in the District of Columbia, Oregon and Massachusetts to \$5.45 million in Delaware, Hawaii and Maine, she noted.

“We can make New Jersey more competitive by increasing our exemption to \$2.5 million, about the average of other states’ exemptions,” Beck said in a statement. About 87 percent of estate tax returns would fall below the \$2.5 million mark, resulting in no tax liability, she said. “Increasing our exemption to \$2.5 million would have the same effect as eliminating the estate tax completely for most people,” she said.

A spokeswoman with Beck’s office told Bloomberg BNA April 19 that Beck hadn’t yet introduced formal legislation associated with her idea.

Other estate tax bills introduced since January that remain in committee include:

- A. 611/S. 1666, which would increase filing threshold to \$1.5 million;
- A. 1059/S. 477, which would phase out the estate tax over five years;
- A. 1112/S. 57, which would end the estate tax and raise the gross income tax rate;
- A. 1223, which would repeal the estate tax;
- A. 1236/S. 1206, which would increase the filing threshold to \$5 million over five years;
- A. 1242/S. 1101, which would increase the filing threshold to \$5 million over five years;
- A. 1385, which would increase the filing threshold to \$1 million;
- A. 2154/S. 1358, which would increase the filing threshold; and
- A. 2919/S. 303, which would increase exclusion amounts to the federal level.

Moving to Florida. Estate planners told Bloomberg BNA that New Jersey is out of step with other states.

Clients do consider estate taxes when choosing whether to make a move to a more tax-friendly state, Gary A. Phillips, a member in the Tax, Trusts and Estates Department of Cole Schotz P.C., told Bloomberg BNA.

“It’s a factor, for sure,” said Phillips, who helped write “On the Road to Florida,” a Cole Schotz guide on moving to Florida from New Jersey or New York. A husband and wife can exclude more than \$10 million under federal rules, Phillips said. “If you live in New Jersey and possess \$10 million, your estate would pay over \$1 million in New Jersey estate tax, which is roughly a 10 percent estate tax.”

Phillips said it would make sense for New Jersey to bring its estate tax threshold more in line with the federal exclusion. He noted that New York recently passed legislation that will bring the state up to the federal level over time, making New Jersey appear even more out of step with neighboring states.

Rothschild’s Herbert said New Jersey’s estate taxes alone probably don’t prompt people to move, but if clients already have homes in other states and are trying to make a decision about where to retire, New Jersey’s taxes soon become part of the equation.

“I don’t think I’ve had any clients who’ve come in and said, ‘I want to move because taxes are too high,’ but if they already have ties to a lower-tax state, then we start to have the conversation,” she said.

The decision is usually made on a number of factors—not just estate taxes, but also income taxes, taxation of retirement income and other factors, she said. “People do make decisions about where they’re going to retire based on the tax burden.”

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□ S. 1728 is at <http://src.bna.com/ee5>.

The fiscal note for S. 1728 is at <http://src.bna.com/efa>.

Information on the other estate tax bills is at <http://www.njleg.state.nj.us/bills/billsbynumber.asp>.

For additional discussion of New Jersey’s estate tax, see *Estates, Gifts, & Trusts Navigator*, at New jersey I.