How inheritance data secretly explains U.S. inequality

Analysis by Andrew Van Dam, *The Washington Post*, November 10, 2023 (shortened)

We hate to be the bearers of bad news, but you're probably not going to get an inheritance.

A little over 1 in 5 U.S. households had received an inheritance at some point in their lives as of 2022, according to the Federal Reserve's remarkable Survey of Consumer Finances. The inheritance rate jumps to 2 out of 5 if you look only at folks in their 70s, who have had more time for their parents and favorite aunts to meet a regrettable but timely demise. But even those folks are in the lucky minority.

Since 1992, the number of people getting inheritances from parents has nearly doubled even as bequests from grandparents and aunts and uncles have remained flat. Your 50s will be your peak inheriting ages, which makes sense given that an average 65-year-old in the U.S. can expect to live to around age 83 and your parents are, sadly, mortal.

These windfalls include homes and other real estate. They also include related gifts and trusts, but those go to a much smaller share of Americans. They don't include assets left to you by your spouse, unless you were divorced at the time of the gift.

The average American has inherited about $58,000 as of 2022. But that's if you include the majority of us whose total lifetime inheritance sits at $0. If you look only at the lucky few who inherited anything, their average is $266,000. And if you look only at those in their 70s, it climbs to $344,000.

White folks are about three times more likely to inherit than their Black, Hispanic or Asian friends. The gap closes slightly when you account for the fact that the typical White American is older than their peers, but it remains vast enough to help explain why the typical White family has more than six times the net worth of the typical Black American family.

Folks in the bottom 50 percent of earners inherit at half the national rate, while those in the top 1 percent are twice as likely to inherit something.

When we called John Ricco, an associate research scholar at Yale Law School who has worked with this data for years, he confirmed that inheritances make the rich richer. But a rich kid's true inheritance goes far beyond cash value: In a million less-measurable ways, elite parents give you a head start in life. By the time they die and hand you a windfall, you've already used all your advantages to accumulate wealth of your own.

"It's not just the dollar amount that you get when your parents die," Ricco said. "It's the safety net that you had to start a business when you were younger, or the ability to put down a larger share of your savings into a down payment and a house because you know that you can save less for retirement.

"Little things like that are probably the main mechanisms through which intergenerational wealth is transmitted and are not easily captured just by the final value of what you see."

The U.S. tax system does little to temper our uneven inheritance. Consider the stepped-up basis provision, "one of the most egregious (tax loopholes) that we have," according to Marc Goldwein, senior policy director at the nonpartisan Committee for a Responsible Federal Budget, who boasts the tax-loophole knowledge of a man with many times his net worth.

When you sell something at a profit, you typically pay capital gains tax. But you can avoid that tax by holding the asset until you expire. At your death, the cost basis of your assets gets stepped up to their current value—meaning your heirs avoid getting taxed on what might be a very substantial gain.

Now multiply that loophole by the millions of homes, businesses, equities and other assets being handed down each year. Goldwein and his colleagues estimate that closing the loophole could reap as much as $204 billion in revenue over the next decade, depending on how aggressively it was taxed.

The loophole's effect on the economy extends well beyond inheritance and inequality, Goldwein and Ricco told us. It encourages older folks to hoard homes and businesses they can no longer make full use of, assets our housing-starved millennial readers would gladly snap up.

Revenue lost to the loophole was partly offset by a simpler-to-administer levy: the estate tax. But the threshold for paying the estate tax was raised substantially by George W. Bush, extended and indexed for inflation under Barack Obama, and raised once more in Donald Trump's Tax Cuts and Jobs Act, which expires after 2025.

Total revenue from the estate tax, as a result, has plummeted. Just 2,192 estates were subject to the tax in 2019, down from 51,159 at the turn of the millennium, and it raised just $14.6 billion, down from more than $35 billion in 2000, adjusted for inflation. Even among the elite, most estates today go untaxed.

"Between politicians continuing to cut the estate tax and taxpayers becoming increasingly good at avoiding it, very few now pay it," Goldwein said. "That means we now have a big net tax break for most people inheriting large amounts of money."