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Individuals and Inheritance Taxes: A Praxeological Examination of Pennsylvania's Inheritance Tax

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I. INTRODUCTION

Much has been written regarding the economic effects of the federal estate tax, but relatively little has been published about state inheritance taxes and their economic consequences.[1] Additionally, what has been

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1. One reason for this imbalance is the federal estate tax's role as a major policy debate. *See, e.g.,* Kathryn L. Moore, *Business Law Forum: The Aging of the Baby*

written has not been addressed primarily to a legal audience.[2] The legal literature discussing the Pennsylvania inheritance tax, one of the eleven effective state inheritance or estate taxes found across the country,[3] is no exception to this observation; beyond practice guides, few legal resources have discussed the tax, and virtually none have substantively and systematically examined its economic effects.[4] Furthermore, Pennsylvania's inheritance tax, like those of other states that have such taxes, has never been specifically analyzed in a legal context from the unique perspective of praxeology,[5] an economic framework rooted in the

Boomers and America's Changing Retirement System, 11 LEWIS & CLARK L. REV. 267, n.130 (2007) (discussing and citing sources that evidence the debate).

2. Only four articles addressed to a legal audience have been written that generally mention the economics of state estate or inheritance taxes: Anne L. Alstott, *Equal Opportunity and Inheritance Taxation*, 121 HARV. L. REV. 469, 496-501 (2007); Jeffrey A. Cooper, *Interstate Competition and State Death Taxes: A Modern Crisis in Historical Perspective*, 33 PEPP. L. REV. 835 (2006); Jeffrey A. Cooper, John R. Ivimey & Donna D. Vincenti, *State Estate Taxes After EGTRRA: A Long Day's Journey into Night*, 17 QUINNIPIAC PROB. L.J. 317 (2004); Susan K. Hill, Comment, *Leaping Before We Look?: Repeal of the State Estate Tax Credit and the Consequences for States, Americans, and the Federal Government*, 32 PEPP. L. REV. 151, 172-79 (2004).

This lack of literature addressed primarily to a legal audience does not reflect the value of such analysis to the legal community. The economic analysis of state inheritance taxes is useful to lawyers for at least two reasons. First, lawyers and, in particular, law professors have traditionally held positions that enable them to significantly influence legislation and governmental policy, as evidenced by the preponderance of persons with law degrees that a) sit in legislatures and in state agencies and b) participate in policy organizations and state bar associations. If economic effects are to be considered in the context of legislative purposes, economic analysis of a state's inheritance tax is likely to be valuable. Second, economic analysis based on praxeology focuses on the actions of individual persons, who are also lawyers' clients. Thus, beyond being only an abstract exercise in "the dismal science," an economic examination of state inheritance taxes also reveals some of the concerns, needs, and even the available options of the legal profession's clients.

3. JULIEANNE E. STEINBACHER & ADRIANNE J. STAHL, PENNSYLVANIA TRUST GUIDE: A HANDBOOK FOR TRUSTEES AND THEIR ADVISORS 525 (2008) (listing states with effective inheritance or estate taxes as being Connecticut, Indiana, Iowa, Kansas, Kentucky, Maryland, Nebraska, New Jersey, Oregon, Pennsylvania, and Tennessee). *See also* Jeffrey A. Cooper, *Interstate Competition and State Death Taxes: A Modern Crisis in Historical Perspective*, 33 PEPP. L. REV. 835, 877-79 (2006) (listing many of the states with effective inheritance taxes and discussing how the list of states with effective inheritance or estate taxes is in flux).

4. State governments have produced some materials regarding their inheritance taxes. *See, e.g.*, PENNSYLVANIA DEPARTMENT OF REVENUE, INSTRUCTIONS FOR FORM REV-1500 (2008), http://www.revenue.state.pa.us/revenue/lib/revenue/rev-1501.pdf. These legislative or governmental resources, however, differ in both content and purpose from legal resources written to inform members of the legal audience about state inheritance tax issues.

5. The limited legal literature mentioning the praxeological concept of the primacy of individual action includes: John M. Czarnetzky, *Time, Uncertainty, and the Law of Corporate Reorganizations*, 67 FORDHAM L. REV. 2939 (1999); Gary Lawson, *Efficiency and Individualism*, 42 DUKE L.J. 53, 58-60 (1992); Timothy Mulligan, Note, *In the*

study of individual human action.[6] This praxeological approach, with its recognition of "the market" as the aggregation of the actions and exchanges of individual persons,[7] provides several significant and relevant insights into the nature of Pennsylvania's inheritance tax, which has taken and will likely continue to take various forms.

Thus, after providing a brief introduction of both the history of Pennsylvania's inheritance tax and praxeology in Parts II and III, this Comment examines the Pennsylvania inheritance tax 1) in its current statutory form, 2) as it would have been affected by a recent bill in the General Assembly, and 3) in the extreme forms possibly permitted by the case law of both Pennsylvania and the United States Supreme Court. In Part IV, this Comment outlines the economic effects of each of these three expressions of Pennsylvania's inheritance tax in four praxeologically-significant categories: ante-mortem capital accumulation, ante-mortem capital flight, post-mortem capital consumption, and state revenue.[8] Consistent with praxeology's goal of serving an exclusively descriptive and educational function that avoids

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Context of Homeowner's and Commercial General Liability Insurance Policies, Should the Issue of Whether an Incident Was an Accident Be Determined from the Insured's or the Injured Party's Perspective, 73 U. DET. MERCY L. REV. 753, n.154 (1996); John K. Palchak & Stanley T. Leung, *No State Required? A Critical Review of the Polycentric Legal Order*, 38 GONZ. L. REV. 289, 302-05 (2002-2003); George Steven Swan, *The Law and Economics of Affirmative Action in Housing: The Diversity Impulse*, 15 U. MIAMI BUS. L. REV. 133, 195 (2006); Joseph Becker, Comment, *Procrustean Jurisprudence: An Austrian School Economic Critique of the Separation and Regulation of Liberties in the Twentieth Century United States*, 15 N. ILL. U. L. REV. 671, 691-93 (1995); David Baer, Comment, *Establishing a Moral Duty to Obey the Law Through a Jurisprudence of Law and Economics*, 34 FLA. ST. U. L. REV. 491, 507-39 (2007). None of these sources analyze state inheritance taxes from a praxeological perspective.

6. Praxeology is the general theory of human action; it is an economic system deduced from the central premise that individual persons act. MURRAY N. ROTHBARD, MAN, ECONOMY, AND STATE: A TREATISE ON ECONOMIC PRINCIPLES, 63 (The Ludwig von Mises Inst. 2001). *See infra* Part III (describing praxeology and the economic method for which it provides the basis).

7. ROTHBARD, *supra* note 6, at 71-80; LUDWIG VON MISES, HUMAN ACTION: A TREATISE ON ECONOMICS 257-58 (3d rev. ed. Henry Regnery Co. 1966). Mises defines the market as

> a process, actuated by the interplay of the actions of the various individuals cooperating under the division of labor. The forces determining the—continually changing—state of the market are the value judgments of these individuals and their actions as directed by these value judgments. . . . There is nothing inhuman or mystical with regard to the market. The market process is entirely resultant of human actions. Every market phenomenon can be traced back to definite choices of the members of the market society.

MISES, *supra*, at 257-58.

8. These four categories are praxeologically significant because they are not independent of human action. Individuals affect or are affected by all four of these categories of economic consequences.

rendering normative policy conclusions,[9] this Comment advocates neither for nor against the Pennsylvania inheritance tax on the level of public policy. Rather, in Part V, this Comment discusses the implications on the inheritance tax debate of the conclusions reached in Part IV.

II. ALTERNATIVE FORMULATIONS OF THE PENNSYLVANIA INHERITANCE TAX

Pennsylvania's inheritance tax has a long, nearly two-hundred year history.[10] Over the course of that history, at least three alternative formulations of Pennsylvania's inheritance tax are discernible, whether in actuality or potentiality: 1) in the extensive forms permitted by case law, 2) as the tax currently stands in statute, and 3) as it was intended to be phased out by recently proposed legislation before the General Assembly.[11]

A. The Inheritance Tax in Case Law

The history of Pennsylvania's inheritance tax has not been without conflict, and on numerous occasions the tax has been the subject of battles in court.[12] Despite unfortunate results for at least one party in each case, these legal clashes have enabled courts to clearly establish the nature of the Commonwealth's inheritance tax and define its outer boundaries in more concrete terms.[13] From the case law, two important principles stand out with regard to the nature of Pennsylvania's inheritance tax: 1) the tax differs from the federal estate tax in that it is a levy against one's statutorily-created privilege to inherit property from a decedent, and 2) there are no clear or obvious limitations to the extent of inheritance tax rates.[14]

9. MISES, *supra* note 7, at 10.

10. Pennsylvania was the first state to enact an inheritance tax, having done so in 1826 with "an act relating to collateral inheritances." 1825-26 Pa. Laws 227-30. Pennsylvania's first inheritance tax was levied on property inherited from estates valued at over $250 by persons other than a decedent's "father, mother, husband, wife, children, and lineal descendants born in lawful wedlock" at a rate of two and one-half percent. *Id.* at 227.

11. *See infra* Part II.A-C.

12. *See infra* notes 15 to 31 and accompanying text.

13. *See, e.g.*, Carpenter v. Pa., 58 U.S. 456 (1854); *In re* Estate of Lander, 207 A.2d 753 (Pa. 1965); *In re* Estate of Pickering, 190 A.2d 132 (Pa. 1963); *In re* Estate of Wright, 138 A.2d 102 (Pa. 1958); *In re* Tack's Estate, 191 A. 155 (Pa. 1937); Shugars v. Chamberlain Amusement Enters., Inc., 130 A. 426 (Pa. 1925); *In re* Kirkpatrick's Estate, 119 A. 269 (Pa. 1922); Strode v. Commonwealth, 1866 WL 6214 (Pa. 1866).

14. The former principle is clearly enunciated in *Estate of Lander*, 207 A.2d at 755-56. The latter principle is best illustrated in *Tack's Estate*, 191 A. at 156.

The case law outlining the nature of Pennsylvania's inheritance tax begins in 1854 with *Carpenter v. Pennsylvania*.[15] In *Carpenter*, the executor of an unsettled estate challenged the retroactive application of an amendment to Pennsylvania's first inheritance tax law on constitutional grounds.[16] Siding with the Commonwealth's argument for applying the amendment, the Supreme Court of the United States concluded that a state has primary control of an inheritance up until the time of distribution to the inheritors.[17] The Court also found that taxing inheritances constituted a constitutional exercise of such control.[18]

Nearly seventy-five years later, the Supreme Court of Pennsylvania clarified the nature of Pennsylvania's inheritance tax in *Shugars v. Chamberlain Amusement Enterprises, Inc.*[19] In that case, which dealt with the taxation of inherited life estates and remainders for which the remaindermen could not immediately be identified, the court established that under Pennsylvania's direct inheritance tax,

> the thing taxed was the right[20] of succession or the privilege of receiving at death the property possessed by the decedent, either by will or under the intestate laws. The fundamental thought was to levy a toll against the passing of property of citizens going by reason of death to others in whatever light the taking may be viewed.[21]

This description of the Pennsylvania inheritance tax was adopted and further employed in later cases, including *Estate of Lander*.[22] In that matter, Pennsylvania's Supreme Court echoed language from *Shugars* and noted that the inheritance tax "is usually denominated a legacy or succession tax on the privilege of receiving the property owned by a decedent."[23] Additionally, the court distinguished Pennsylvania's inheritance tax from the federal estate tax on the basis that the latter was

15. *Carpenter*, 58 U.S. 456.
16. *Id*. at 459-61.
17. *Id.* at 463. In articulating this conclusion, the Court stated that "[t]he rights of the donee are subordinate to the conditions, formalities, and administrative control, prescribed by the State in the interests of its public order, and are only irrevocably established upon [the State's] abdication of this control, at the period of distribution." *Id.*
18. *Id.* "If the State, during this period of administration and control by its tribunals and their appointees, thinks fit to impose a tax upon the property, there is no obstacle in the constitution and laws of the United States to prevent it." *Id.*
19. *Shugars*, 130 A. at 426.
20. It is not insignificant that the word "right" was used here. The notion that one has a right to the succession of property has implications on the inheritance tax rate and a State's ability to escheat devised property. *See infra* note 25.
21. *Shugars*, 130 A. at 427. *See also In re* Estate of Pickering, 190 A.2d 132, 136 (Pa. 1963) (using the same language to describe the Pennsylvania inheritance tax).
22. *In re* Estate of Lander, 207 A.2d 753 (Pa. 1965).
23. *Id.* at 754, 756.

a tax on a decedent's privilege of transmission rather than the inheritor's privilege of succession.[24]

On its face, the case law also suggests that the privilege of succession, which was created by the state, is not absolute and can be withdrawn by the state, perhaps through the use of a high inheritance tax rate.[25] The Pennsylvania Supreme Court, in *Kirkpatrick's Estate*, employed the rule that the right or privilege of succession "is purely a creature of statutory law. It did not exist at common law, and individuals possess no natural right to such succession; the sovereign authority that gives it may demand payment for the gift."[26] Building on this principle fifteen years later in *Tack's Estate*, the court cast the inheritance tax as the state's distributive share of an estate, which was based on its allowing the privilege of inheritance, and could amount up to the entire value of such estate.[27] In drawing this conclusion, the court baldly stated that

> Students of law agree that the state has the right to declare an escheat of all the property of a decedent and therefore, as the price of

24. *Id.* at 755-56. The court noted that

> "it is well settled that the Federal Estate tax is not a legacy tax or a succession tax on the privilege of receiving the property possessed by a decedent; instead it is a tax on the privilege of transmission of decedent's property (*i.e.*, the statutory net estate of the decedent) which is payable out of the estate as a whole."

Id. at 756 (quoting *In re* Estate of Pickering, 190 A.2d at 136-37).

25. While the case law is relatively unambiguous in claiming as the state's prerogative the power to eliminate the privilege of succession, any state attempt to that effect would be met with substantial legal challenges. For example, a "dispossessed" heir would likely argue that an inheritance tax rate that eliminates an inheritance effectively serves as an unconstitutional government taking, citing as support the United States Supreme Court's decision in *Hodel v. Irving*, 481 U.S. 704 (1987). Conversely, the state would likely argue that the Court's decision in *Hodel* narrowly protects the right of transmission, and thus a state inheritance tax that abolishes the privilege of succession does not violate the United States Constitution. In response, the heir would likely assert that such a formalistic distinction ignores the fact that a confiscatory tax on either the right of transmission or the right of succession leads to the same result, being two sides of the same coin.

26. *In re* Kirkpatrick's Estate, 119 A. 269, 269 (Pa. 1922) (citing Magoun v. Illinois Trust & Savings Bank, 170 U.S. 283, 290 (1898)). *See also* Strode v. Commonwealth, 1866 WL 6214 (Pa. 1866), in which the Pennsylvania Supreme Court quoted from lower court:

> [A]s the right to take by succession and testament is derived from the state, it must necessarily be enjoyed subject to such conditions as the state may impose. And if a condition be that the kindred or legatees shall pay a bonus, this is not a tax or burthen imposed on *their property*, or on the property of anybody else. It is simply the price of the privilege which the state has conferred upon them. If they do not choose to avail themselves of the privilege they need not pay the price, and are no worse off than before.

Strode, 1866 WL 6214, at *3.

27. *In re* Tack's Estate, 191 A. 155, 156 (Pa. 1937).

> allowing a legatee, devisee, or heir to inherit, it may appropriate to itself any portion of the property which it chooses to exact.[28]

The United States Supreme Court echoed this conclusion in *Irving Trust Company v. Day*, when it held that "[n]othing in the Federal Constitution forbids the legislature of a state to limit, condition, or even abolish the power of testamentary disposition over property within its jurisdiction."[29]

In his dissenting opinion in *Estate of Wright*, Justice John C. Bell summed up what case law has indicated is the extent of Pennsylvania's power to tax inheritances:

> The law is well settled that beneficiaries of a decedent's estate (whether by will or descent) have *no natural or vested* right to receive such property; on the contrary, whatever rights such beneficiaries possess are derived from and governed by statute and consequently the beneficiaries take under and subject to the applicable statutes. Unfortunately, it is established law that a State may validly escheat *all* of a decedent's net estate and such action would violate neither the United States nor the Pennsylvania Constitutions.[30]

On its face, the case law provides no clear and obvious limitations on Pennsylvania's ability to levy an inheritance tax with a rate of up to one hundred percent of inherited property.[31]

B. *The Inheritance Tax as Currently in Statute*

Pennsylvania's inheritance tax, in its current statutory form, is presented in a logical sequence that introduces the tax, defines what inherited property will be taxed, establishes the rate of the tax, and provides the procedures for administering the tax.[32] The statute includes detailed instructions on valuing assets, collecting the tax, receiving tax payments, distributing refunds, and resolving disputes.[33] At the heart of the inheritance tax statutes are those sections dealing with the types of transferred property that will be taxed and the rates at which such

28. *Id. But see supra* note 25. The court's blanket claim that the state can escheat all of a decedent's property may no longer be true in light of the United States Supreme Court's decision in *Hodel*, 481 U.S. 704. The legitimacy of such a "tax" would likely need to rest on a) the distinction between a tax on the right of transmission and one on the privilege of succession and b) the Court's explicit recognition of prior cases validating state inheritance taxing powers.
29. Irving Trust Co. v. Day, 314 U.S. 556, 562 (1942).
30. *In re* Estate of Wright, 138 A.2d 102, 115 (Pa. 1958) (Bell, J. dissenting).
31. *See supra* notes 12-30 and accompanying text.
32. 72 PA. STAT. ANN. §§ 9101-9196 (West 2008).
33. *Id.* §§ 9121-9122, 9136-9154, 9166-9188.

property will be taxed.[34] Pennsylvania's inheritance tax adopts a broad, all-encompassing approach in taxing all property[35] transferred by will, intestate statute, and court order,[36] as well as all specified property transfers made during either a resident or nonresident's lifetime for which valuable and adequate consideration was not received at the time of transfer.[37] The inheritance tax is also applied to "[a]ll succeeding interests which follow the interest of a surviving spouse in a trust or similar arrangement" to the extent that the decedent-spouse's personal representative has not elected to have such interests treated as if transferred by the surviving spouse.[38] In addition, property passing to a non-spouse by virtue of a joint tenancy interest is also taxed as inherited property.[39] To determine the amount attributable to an inherited portion, the value of the whole property is divided by the number of joint tenants living or in existence immediately preceding the death of the decedent.[40]

The value of estate assets is calculated as of the date of death, with special formulas employed for valuing interests such as life estates, future interests, etc.[41] The statute includes a limitation on the valuation of farmland by allowing inherited land "devoted to agricultural use, agricultural reserve or forest reserve," as specifically defined by statute, to be valued only in light of that particular use.[42]

34. *Id.* §§ 9106-9116. Section 9106 formally establishes Pennsylvania's inheritance tax in broadly stating that "[a]n inheritance tax for the use of the Commonwealth is imposed upon every transfer subject to tax under this article at the rates specified in section [9116]." *Id.* § 9106 (West 2008). These inheritance tax provisions are particularly relevant to praxeological analysis because of their direct effect on an individual's finances; the determination of what inherited property is taxed and at what rate fundamentally affects individuals who prospectively consider the disposition of their estates, which subsequently influences their economic decisions.

35. *Id.* § 9107(a).

36. *Id.* § 9107(b).

37. *Id.* § 9107(c). Among the property interests taxed under this subsection are property with a value greater than $3,000 transferred within a year before the decedent's death; property in which the transferor held a reversionary interest; property in which the transferor maintained a right to designate who may possess or enjoy such property; property for which the transferor was to receive interest or support for the remainder of his life (*i.e.* annuities); and property over which the decedent had, within one year of death, the power to alter, amend, or revoke the interest of a beneficiary (*i.e.* retirement funds and trusts). *Id.* § 9107(c).

38. *Id.* §§ 9107(d), 9113.

39. *Id.* § 9108(a).

40. *Id.* This approach differs from the federal estate tax approach. 26 U.S.C.A. § 2040 (West 2008) (providing the federal rules regarding the estate taxation of joint tenancy property).

41. 72 PA. STAT. ANN. § 9121 (West 2008).

42. *Id.* § 9122. If, however, the property is used for different purposes within seven years after the decedent's death, the owner of the land will become liable for the difference between the value of the land as it was valued for a particular use and the value of the land using general valuation methods. *Id.* § 9122(c).

Despite its broad reach, the Pennsylvania inheritance tax specifically excludes from taxation certain types of inherited property and allows a decedent's estate to take statutorily-identified deductions.[43] For example, transfers to governmental bodies, charities, fraternal societies, and veterans' organizations are excluded from taxation.[44] Likewise, among other excluded property are insurance proceeds, intangible property of nonresidents, escheated property, and spousal property obtained by right of survivorship.[45] Lump-sum burial or death payments from the Social Security Administration, Veterans' Administration, or United States Railroad Retirement Board are also not included in a decedent's estate.[46] Also excluded are payments under pension, stock bonus, profit-sharing, and other retirement plans where the decedent, before his death, "did not otherwise have the right to possess (including proprietary rights at termination of employment), enjoy, assign or anticipate the payment made."[47] From the total value of an estate, an executor may also deduct reasonable administration costs, bequests to attorneys or fiduciaries in lieu of fees, the family exemption, funeral and burial expenses, the cost of tombstones or gravemarkers, contributions to burial trusts, payments made for burial contracts, bequests for religious services.[48] Property taxes, non-federal death taxes paid to other states or nations,[49] and several forms of debt owed to others by the decedent's estate may also be deducted.[50]

The inheritance tax applies four different tax rates, each to property transferred to persons standing in certain relationships with the decedent.[51] Currently, property that is transferred to a spouse is taxed at a rate of zero percent.[52] Property inherited from a decedent's estate by a grandparent, parent, lineal descendant, or spouse of a child is taxed at a rate of four and one-half percent.[53] A tax rate of twelve percent is

43. *Id.* §§ 9111-9113, 9126-9130.

44. *Id.* § 9111(b)-(c). These exclusions are allowed, based on the assumption that the inherited property will be used for governmental, charitable, educational, or organizational purposes, with further restrictions being based on the organizational status of the intended beneficiary. *Id.*

45. *Id.* § 9111(d),(h),(k)-(m).

46. *Id.* § 9111(p)-(q).

47. 72 PA. STAT. ANN. § 9111(r) (West 2008).

48. *Id.* § 9127.

49. *Id.* § 9128.

50. *Id.* § 9129.

51. 72 PA. STAT. ANN. § 9116(a) (West 2008).

52. *Id.* § 9116(a)(1.1)(ii). The inherited property taxed at this rate also includes property transferred as a result of a spouse's exercise of elective share rights under 20 PA. STAT. ANN. §§ 2201-2211 (West 2008).

53. *Id.* § 9116(a)(1). Under § 9116(a)(1.2), a special exclusion is applied to property inherited by parents from decedent-children under the age of twenty-one, which is taxed at a zero percent rate. *Id.* § 9116(a)(1.2).

applied to property transferred to siblings.[54] The highest rate, fifteen percent, is reserved for property inherited by persons or entities in all other relationships, known as collaterals.[55]

C. Proposed Legislation to Gradually Repeal the Inheritance Tax

A recent attempt[56] to alter Pennsylvania's inheritance tax came in November 2007, with an amendment to House Bill 377[57] submitted by Representative Scott Perry (R) of the 92nd Legislative District.[58] Intended to phase out Pennsylvania's inheritance tax completely by 2012, the amendment would have steadily decreased inheritance tax rates to zero percent for property inherited from decedents who die in particular years.[59] In addition, the amendment sought to add an additional provision that would have immediately applied a tax rate of zero percent to property transferred to a decedent's parent, adoptive parent, or stepparent.[60] The amendment did not attempt to redefine taxable property or provide additional exclusions, deductions, or

54. *Id.* § 9116(a)(1.3).

55. *Id.* § 9116(a)(2).

56. Other recent attempts are H.R. 635, 191st Gen. Assem., Reg. Sess. (Pa. 2009); H.R. 423, 191st Gen. Assem., Reg. Sess. (Pa. 2009); H.R. 374, 191st Gen. Assem., Reg. Sess. (Pa. 2009); S. 80, 191st Gen. Assem., Reg. Sess. (Pa. 2009); H.R. 1444, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 808, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 836, 190th Gen. Assem., Reg. Sess. (Pa. 2007); S. 417, 190th Gen. Assem., Reg. Sess. (Pa. 2007); and H.R. 409, 190th Gen. Assem., Reg. Sess. (Pa. 2007).

57. House Bill 377 originally sought only to amend Pennsylvania's tax code by adding an "alternative special tax provision for poverty." The General Assembly of Pennsylvania, House Bill No. 377, Printer's No. 441 (Feb. 13, 2007), http://www.legis.state.pa.us/CFDOCS/Legis/PN/Public/btCheck.cfm?txtType=PDF&sessYr=2007&sessInd=0&billBody=H&billTyp=B&billNbr=0377&pn=0441 (amended by House Bill No. 377, Printer's No. 2809).

58. Pennsylvania Legislative Reference Bureau, Amendments of House Bill No. 377, Amendment 04399, (November 21, 2007), http://www.legis.state.pa.us/cfdocs/billinfo/split.cfm?syear=2007&sind=0&body=H&type=B&bn=0377&pn=2849&ayear=2007&an=04399.

59. *Id.* The amendment would have kept the tax rate for spousal transfers at its current, zero percent rate. *Id.* For grandparents, parents, lineal descendants, and the spouses of children, the amendment would have kept the tax rate at four and one-half percent for inheritances received from a decedent's estate who died before 2010, but would have decreased this rate to two percent for inheritances received from decedents' estates who died in 2010 and further reduced it to zero percent for inheritances received from decedents' estates who died after 2010. *Id.* Tax rates on inheritances to siblings would be reduced from twelve percent in 2007 to nine percent in 2008, to six percent in 2009, to four and one-half percent in 2010, to two percent in 2011, and finally to zero percent in 2012 and every year thereafter. *Id.* For all other transfers, the amendment would have reduced the tax rate from fifteen percent in 2007 to ten percent in 2008, and then to seven percent in 2009, after which the tax rate would parallel the rate for transfers to siblings. *Id.*

60. *Id.*

credits.[61] After some debate[62] and with the support of an overwhelming majority of both Democrats and Republicans, the amendment was adopted by a vote of 173-23 in January 2008.[63] On the following day, the bill was passed by a vote of 191-0 and submitted to the Senate for concurrence.[64]

Once in the Senate, House Bill 377 was referred to the Committee on Finance at the end of January 2008.[65] In committee, the sections intended to repeal the Pennsylvania inheritance tax, along with most other provisions, were stripped from the bill as a result of an amendment submitted by Senator Patrick M. Browne (R) of the 16th Senatorial District.[66] After additional referrals to the Senate committees on Finance and Appropriations, House Bill 377 was unanimously passed by the Senate and approved by Governor Edward Rendell in July 2008.[67]

Although the provisions that would have gradually repealed the inheritance tax were deleted before the passage of House Bill 377,[68] those provisions are significant for several reasons, all of which warrant an analysis of the proposed legislation. First, that Representative Perry submitted his amendment, which received widespread support in the House,[69] is indicative of the perennial nature of discussions regarding the

61. *Id.*

62. The General Assembly of Pennsylvania, Legislative Journal-House 82-84 (January 16, 2008), http://www.legis. state.pa.us/WU01/LI/HJ/2008/0/20080116.pdf.

63. *Id.*

64. The General Assembly of Pennsylvania, Legislative Journal-House 120 (January 17, 2008), http://www.legis.state.pa.us/WU01/LI/HJ/2008/0/20080117.pdf; The General Assembly of Pennsylvania, House Bill No. 377, Printer's No. 3094 (Jan. 16, 2008), http://www.legis.state.pa.us/CFDOCS/Legis/PN/Public/btCheck.cfm?txtType=PDF&sessYr=2007&sessInd=0&billBody=H&billTyp=B&billNbr=0377&pn=3094 (amended by House Bill No. 377, Printer's No. 4086).

65. The General Assembly of Pennsylvania, Legislative Journal-Senate 1533 (January 28, 2008), http://www.legis.state.pa.us/WU01/LI/SJ/2008/0/Sj20080128.pdf.

66. Pennsylvania Legislative Reference Bureau, Amendments of House Bill No. 377, Amendment 08080, (June 26, 2008) (on file with committee chairman); The General Assembly of Pennsylvania, House Bill No. 377, Printer's No. 4086 (Jun. 26, 2008), http://www.legis.state.pa.us/CFDOCS/Legis/PN/Public/btCheck.cfm?txtType=PDF&sessYr=2007&sessInd=0&billBody=H&billTyp=B&billNbr=0377&pn=4086 (amended by House Bill No. 377, Printer's No. 4195).

67. The General Assembly of Pennsylvania, Legislative Journal-Senate 2412 (Jul. 4, 2008), http://www.legis.state.pa.us/WU01/LI/SJ/2008/0/Sj20080704.pdf. House Bill 377, on final passage by the Senate and approval by the governor, allowed for the study of a special credit for poverty, the inclusion of a voluntary contribution checkbox on the Pennsylvania income tax return, and the creation of a tax credit to encourage the recruitment and retention of volunteer emergency responders. H.R. 377, 192nd Gen. Assem., Reg. Sess. (Pa. 2008).

68. *See supra* notes 65-67 and accompanying text.

69. The General Assembly of Pennsylvania, Legislative Journal-House 84 (January 16, 2008), http://www.legis.state.pa.us/WU01/LI/HJ/2008/0/20080116.pdf.

inheritance tax.[70] Second, the removal of the inheritance tax provisions by the Senate Committee on Finance[71] reflects the ongoing, controversial nature of any plan to repeal Pennsylvania's inheritance tax.[72] Thus, a praxeological examination of the inheritance tax is useful in evaluating the assumptions or oftentimes convoluted economic analysis surrounding the tax, which will likely, in turn, shed light on the rhetoric employed by all sides in the ongoing debate.[73] Third, proposed legislation seeking to eliminate the inheritance tax,[74] like Representative Perry's amendment to House Bill 377,[75] serves as a useful and realistic construct with which to compare alternative formulations of Pennsylvania's inheritance tax, with the objective being to ascertain the economic effects of each.

III. PRAXEOLOGY AS ECONOMIC THEORY

An entire system of economic thought has been derived from praxeology, which is the general study of human action.[76] Praxeology provides a universal theory of human action by defining the relationship between ends and means in individual decision-making,[77] thus distinguishing itself from other disciplines.[78] Praxeology begins with the

70. Evidence of ongoing discontent with the inheritance tax is revealed in the other, numerous attempts to repeal the inheritance tax. *See e.g.*, H.R. 1444, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 808, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 836, 190th Gen. Assem., Reg. Sess. (Pa. 2007); S. 417, 190th Gen. Assem., Reg. Sess. (Pa. 2007); and H.R. 409, 190th Gen. Assem., Reg. Sess. (Pa. 2007).

71. Pennsylvania Legislative Reference Bureau, Amendments of House Bill No. 377, Amendment 08080, (June 26, 2008) (on file with committee chairman); The General Assembly of Pennsylvania, House Bill No. 377, Printer's No. 4086 (Jun. 26, 2008), http://www.legis.state.pa.us/CFDOCS/Legis/PN/Public/btCheck.cfm?txtType=PDF&sessYr=2007&sessInd=0&billBody=H&billTyp=B&billNbr=0377&pn=4086 (amended by House Bill No. 377, Printer's No. 4195).

72. *See supra* note 70 (providing evidence of the controversy generated by Pennsylvania's inheritance tax).

73. *See infra* Parts IV-V.

74. *See, e.g.*, *supra* note 56 (providing examples of recent legislation attempting to repeal Pennsylvania's inheritance tax).

75. Pennsylvania Legislative Reference Bureau, Amendments of House Bill No. 377, Amendment 04399, (November 21, 2007), http://www.legis.state.pa.us/cfdocs/billinfo/split.cfm?syear=2007&sind=0&body=H&type=B&bn=0377&pn=2849&ayear=2007&an=04399.

76. LUDWIG VON MISES, THE ULTIMATE FOUNDATION OF ECONOMIC SCIENCE: AN ESSAY ON METHOD 41-44 (1962).

77. ROTHBARD, *supra* note 6, at 63.

78. *Id.* at 63-64. Praxeology examines "the formal implications of the fact that men use means to attain various chosen ends." *Id.* at 64. It does not analyze "the subjective decisions of individual human minds" or the specific content of a person's ends. *Id.* at 63. Therefore, praxeology is distinguished from psychology (why people chooses various ends), the philosophies of ethics and aesthetics (what people's ends should be), technology (how to use means to arrive at ends), and history (what man's ends are and have been, and how man has used means in order to attain those ends). *Id.* at 64.

axiom that individuals[79] act, denoting that they apply means according to an idea to achieve ends.[80] Thus, individuals act purposefully; their actions are rational[81] in the sense that they are aimed at particular objectives.[82] Inherent in this description is the fact that individuals act in time.[83] They apply means in the present according to their currently-held ideas to achieve ends in the future, however near or distant.[84]

From these initial premises, the rest of praxeological principles are syllogistically deduced.[85] For example, that individuals act in time implies that they seek to increase their satisfaction; specifically, an individual applies means in the present according to a currently-held idea to achieve a future end that will be more satisfactory than either his present circumstances or his predicted future state.[86] Thus, an individual's anticipated future satisfaction is based entirely on his subjective preferences, and the preferences that motivate one person to

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79. A central concept of praxeology is methodological individualism. *Id.* at 2. Methodological individualism recognizes that only individuals are capable of action and, thus, the study of human action must necessarily focus on individuals. *Id.* Neither praxeology nor methodological individualism contests the fact that collective bodies have significantly influenced history and will continue to do so. *Id.* However, both point out that collective bodies operate "always through the intermediary of one or several individuals whose actions are related to the collective as the secondary source," with an appropriate incorporation of this fact into their methodology. MISES, *supra* note 7, at 41-43.

80. MISES, *supra* note 7, at 11; ROTHBARD, *supra* note 6, at 1-11, 14-17.

81. As used here, the term "rational" refers to the quality of being purposeful, of being aimed at the attainment of particular ends. It is not an evaluation of the appropriateness of the ends that individuals seek; praxeology is incapable of making normative judgments because it lacks a framework of values, which is necessary to make such assertions. MISES, *supra* note 7, at 19-22.

82. ROTHBARD, *supra* note 6, at 1.

83. MISES, *supra* note 7, at 99-104; ROTHBARD, *supra* note 6, at 11-14.

84. ROTHBARD, *supra* note 6, at 2.

85. Murray Rothbard, *In Defense of Extreme Apriorism*, 23 S. ECON. J. 314-20 (1957).

86. MISES, *supra* note 7, at 13-14, 100. Mises describes this principle in the following manner:

> Action is always directed toward the future; it is essentially and necessarily always a planning and acting for a better future. Its aim is always to render future conditions more satisfactory than they would be without the interference of action. The uneasiness that impels a man to act is caused by a dissatisfaction with expected future conditions as they would probably develop if nothing were done to alter them. In any case action can influence only the future, never the present that with every infinitesimal fraction of a second sink down into the past. Man becomes conscious of time when he plans to convert a less satisfactory present state into a more satisfactory future state.

Id.

act in a particular way may be wholly insufficient to induce another person to act in the same manner for identical purposes.[87]

An additional corollary is the concept of time preference, which recognizes that the personal preference for a particular present gratification over an anticipated future satisfaction[88] differs by degrees for all individuals.[89] For example, Anne may be willing to forego a trip to the bar with her law school friends because she prefers the better grade that she anticipates receiving by using her time in the present to study. Bob, on the other hand, would much rather spend a night out with friends, preferring socializing in the present to any anticipated grade benefits that would result from studying. Assuming, perhaps unrealistically, that both Anne and Bob are equally efficient in their use of study time, Anne has a lower time preference and Bob has a higher time preference at the point they each choose to act (*e.g.*, studying or going to the bar).[90]

The concept of time preference is closely linked with saving and investing.[91] Given the general preference of all persons for present consumption over future satisfaction, with all other things being equal, no one would be willing to forego spending $100 for gratification in the present only to have $100 at a later date.[92] This wisdom is implicit in the notion of the time value of money, and only when other considerations (*i.e.*, deflation, future financial security, the ability to provide inheritances, financial power, etc.) enter the picture would this transaction even begin to be entertained as a viable course of action. Under the same circumstances, however, some individuals will likely be more willing to forego spending $100 for gratification in the present to have $105 and the consumption it would represent at a later date.[93] Likewise, even more individuals will likely be willing to postpone

87. MURRAY ROTHBARD, THE LOGIC OF HUMAN ACTION ONE 59-60 (Edward Elgar 1997); ROTHBARD, *supra* note 6, at 323-33.

88. It is logically inconceivable that a person could have an absolute preference for future consumption over present gratification. ROTHBARD, *supra* note 6, at 3-6. Mises also makes this point in stating that

> [i]f [a man] were not to prefer satisfaction in a nearer period of the future to that in a remoter period, he would never consume and so satisfy wants. He would always accumulate, he would never consume and enjoy. He would not consume today, but he would not consume tomorrow either, as the morrow would confront him with the same alternative.

MISES, *supra* note 7, at 484.

89. MISES, *supra* note 7, at 483-88.

90. *See id.* (noting the definition and relevance of time preference to human action).

91. ROTHBARD, *supra* note 6, at 482, 488.

92. MISES, *supra* note 7, at 486.

93. ROTHBARD, *supra* note 6, at 13-17 (laying out the implications of value scales and time preferences).

spending $100 in the present to have $120 in the future.[94] Those with higher time preferences would require greater "returns" on their investments to motivate them to save, and subsequently invest, when compared to persons with lower time preferences.[95]

This fact of individual action reflects a central principle of praxeological analysis: marginality.[96] The principle of marginality recognizes that individuals have infinitely varying, ordinarily-ranked preferences and the resulting value scales.[97] As a result of this variation, some individuals will always be on the "margin" of any given decision.[98] Individuals, subjectively weighing the perceived costs against the anticipated benefits, will decide whether to act based on their unique,[99] all-encompassing, personal value scales.[100] Thus, when the costs or benefits of making any given decision to act or not act change, there will be persons on the "margin" who change their actions as a result.[101] Changes in the costs or benefits of an action expressed in terms of money, which is the primary medium of exchange,[102] have a particularly apparent effect on individual decisions that serve to identify those persons who, in having acted, were doing so on the "margin."[103]

Indelibly linked to the saving and investing of persons on the "margin" are the creation of capital goods and the derivative concept of capital.[104] Capital goods are assets, necessarily created with past labor and time, that are not consumed, but rather are reserved for future production or consumption.[105] Thus, capital goods represent stored labor, assets, and time.[106] Capital goods are also a necessary factor in expanding and lengthening the production structure, which enables

94. *See id.*

95. *See id.*

96. MISES, *supra* note 7, at 119-27. *See also* ROTHBARD, *supra* note 6, at 17-28 (discussing the centrality of marginal utility to praxeological analysis).

97. MISES, *supra* note 7, at 119-23; ROTHBARD, *supra* note 6, at 18-20.

98. *See supra* note 96 and accompanying text.

99. Properly understood, personal value scales are each entirely unique. That many individuals prefer chocolate cake over pumpkin pie, and vice versa, does not itself suggest, let alone prove, that persons have identical value scales. First, even with regard to the choice between chocolate cake and pumpkin pie, there are varying degrees of preference. Second, personal value scales take into account the totality of all one's preferences, which are largely based on one's personality and experiences. Given the uniqueness of personalities and experiences, the uniqueness of value scales logically follows. MISES, *supra* note 7, at 119-23.

100. *See generally* MISES, *supra* note 7, at 119-23.

101. *See id.* at 119-27.

102. ROTHBARD, *supra* note 6, at 165. *See also* MISES, *supra* note 7, at 208-9, 462-66 (describing the role of money as a medium of exchange).

103. *See* MISES, *supra* note 7, at 119-27.

104. *Id.* at 41-44.

105. *Id.* at 490-93.

106. *Id.* at 493.

production of ever more complex, yet oftentimes more efficient, practical, and desirable goods.[107] The production of capital goods, however, requires saving and investing;[108] if all goods, including assets, are consumed in the present, there, by implication, will be nothing left for use in the future.[109] The concept of capital refers to capital assets, which includes money, that has been saved and invested and is being or will be applied to future production.[110] When the current amount of capital in a society is compared with the amount of capital at a prior point in time, three possible trends are discernible: 1) capital consumption, a decrease in the amount of capital; 2) capital maintenance, no change in the amount of capital; and 3) capital accumulation, an increase in the amount of capital.[111] These trends, in most cases, have a direct relationship with economic growth;[112] societies where capital consumption occurs have a decline in economic production and, correspondingly, standards of living,[113] while societies in which there is capital accumulation experience economic growth and realize improved standards of living.[114]

An additional principle of praxeology, implicit in the concept of time preference,[115] is the recognition that in acting in the present, individuals have the capability to take into account both the short term and the long term; individuals are able to act while taking into consideration the anticipated short term and long term effects of their actions.[116] A corollary to this principle is that governments, as entities whose "activities" are, in the most fundamental sense, comprised of the

107. *Id.* at 259-60, 490-92.

108. Once again, saving and investing is a function of an individual's value scale and is restricted or encouraged by one's time preference. *Id.* at 491.

109. MISES, *supra* note 7, at 259, 490-92.

110. ROTHBARD, *supra* note 6, at 40-61, 486-91.

111. MISES, *supra* note 7, at 514-17.

112. The term "growth" is used in the descriptive sense only and is not intended to imply any value judgments. Indeed, one's normative or ethical commitments may reject economic growth and require individuals to discourage it. *See generally* Richard Douthwaite, The Foundation for the Economics of Stability, The Problem with Economic Growth, http://www.feasta.org/growth.htm (last visited January 26, 2009). *See also* ROTHBARD, *supra* note 6, at 832-39 (arguing that endorsement of economic growth is a matter of policy that necessarily involves value judgments).

113. Like the term "growth, the terms "decline" and "standard of living" are used in the descriptive sense only and are not intended to imply any value judgments. *See* Douthwaite, *supra* note 94 (making the same observation about the use of the term "growth").

114. ROTHBARD, *supra* note 6, at 479-91. These economic results follow from the availability of capital, which enables future production, in society. *Id.*

115. *See generally supra* notes 91-95 and accompanying text.

116. ROTHBARD, *supra* note 6, at 40-61, 305-07.

actions of individual persons,[117] can also take into consideration of both the short term and long term effects of their policies.[118]

These principles do not constitute the entirety of praxeology,[119] but they do provide the basic elements necessary for outlining the four praxeologically-significant categories which are affected by Pennsylvania's inheritance tax: ante-mortem capital consumption, ante-mortem capital flight, post-mortem capital consumption, and state revenue.[120]

IV. A PRAXEOLOGICAL ANALYSIS OF THE PENNSYLVANIA INHERITANCE TAX

Using these praxeological principles, it is not only possible, but also profitable,[121] to determine the economic effects of Pennsylvania's inheritance tax in its three different formulations.[122] Given their variation, each of these will have different economic effects, even if only to a matter of degree, with regard to the four praxeologically-significant[123] categories of ante-mortem capital consumption, ante-

117. MISES, *supra* note 7, at 41-44. *See also supra* note 64 (explaining the principle of methodological individualism). In discussing methodological individualism, Mises aptly makes this point:

> First we must realize that all actions are performed by individuals. A collective operates always through the intermediary of one or several individuals whose actions are related to the collective as a secondary source. It is the meaning which the acting individuals and all those who are touched by their action attribute to an action, that determines its character. It is the meaning that marks one action as the action of an individual and another action as the action of the state or of the municipality. The hangman, not the state, executes a criminal. It is the meaning of those concerned that discerns in the hangman's action an action of the state . . . . The life of a collective is lived in the actions of the individuals constituting its body . . . . That there are nations, states, and churches, that there is social cooperation under the division of labor, becomes discernible only in the actions of certain individuals.

MISES, *supra* note 7, at 42-43.

118. ROTHBARD, *supra* note 6, at 40-61, 652-54.

119. For a more complete analysis of praxeology and the economic principles derived from it, *see generally* MISES, *supra* note 7; ROTHBARD, *supra* note 6; and other works by scholars affiliated with the Austrian School of Economics.

120. Each of these categories is praxeologically-significant because each is primarily affected by the actions of individual persons. Thus, in turn, inheritance taxes, which affect individual action, consequently affect these four categories.

121. Recognizing the economic effects of Pennsylvania's inheritance tax is useful in informing and defining the contours of the debate. *See infra* Part V (highlighting the implications that praxeological principles have on the discussion of Pennsylvania's inheritance tax).

122. *See supra* Part II (defining the three different formulations of Pennsylvania's inheritance tax).

123. *See supra* Part III (outlining the principles of praxeology).

mortem capital flight, post-mortem capital consumption, and state revenue.[124]

A. Ante-Mortem Capital Consumption

Given the lack of clear or obvious limitations on Pennsylvania inheritance tax rates,[125] the General Assembly could potentially increase rates to comparatively high levels, even including rates of seventy-five percent or more.[126] Such a course of legislative action would not be without severe economic consequences.[127] For example, high inheritance tax rates would profoundly increase ante-mortem capital consumption.[128] Among the many reasons that people save money and other property during their lifetimes is to provide inheritances to be distributed upon death to their families, friends, and favored causes.[129] Persons internally[130] weigh[131] the perceived benefits of spending their money or using their property in the present against the satisfaction each individually anticipates in both the present and future as a result of planning to provide inheritances. Of relevance to such determinations is the size of the expected inheritance to be given. If much of the satisfaction in granting inheritances comes from the knowledge that one's heirs or devisees will likely be made financially secure or afforded expanded opportunities after one has passed, the amount of the inheritance would affect the overall satisfaction realized by the saver. As the size of the inheritance increases, the likelihood of these goals being achieved after death increases, which also increases the satisfaction from present planning and saving. When individuals save for the purpose of providing inheritances, their savings will subsequently be invested.[132]

124. *See infra* Part IV.A-D (examining the economic effects of each formulation).

125. *See supra* Part II.A (concluding that there are no clear limitations on the rates imposed under the Commonwealth's inheritance tax).

126. This could easily be accomplished by simple legislative fiat with the approval of legislation amending 72 PA. STAT. ANN. § 9116(a), which designates the inheritance tax rates, by a majority of the General Assembly's members in each chamber.

127. *See infra* notes 128-47 and accompanying text.

128. *See infra* notes 139-47 and accompanying text.

129. *See, e.g.*, The General Assembly of Pennsylvania, Legislative Journal-House 83 (January 16, 2008), http://www.legis.state.pa.us/WU01/LI/HJ/2008/0/20080116.pdf.

130. This process is usually not a conscious, cognitive decision, as with most choices. However, humans are neither lightning-fast calculators nor creatures trapped by impulsive urges. They make rational decisions based on their individual subjective, relative preferences at particular moments in time. MISES, *supra* note 7, at 19-22.

131. The concept of opportunity cost is at work when individuals analyze the costs and the benefits of their alternative options. In considering a particular course of action, the opportunity cost in each situation is the anticipated benefits of the next-best, alternative option. MURRAY N. ROTHBARD, *supra* note 6, at 299.

132. Even if an individual does not invest his money or property directly, such assets will be indirectly invested, in the absence of actual, physical hoarding. When assets are

Thus, these assets will be added to the total capital stock available in the market, for which society will accrue the resulting economic benefits.[133]

Should Pennsylvania's inheritance tax rates be legislatively increased to high levels,[134] the direct result would be to substantially decrease the perceived benefits of saving to provide inheritances for heirs and devisees by considerably decreasing the amount of property transferred and, therefore, sapping the anticipated benefits of saving up inheritances. This, in turn, decreases the opportunity cost of "consuming" assets in the present, making it a more attractive option, which is even more applicable for those persons with higher time preferences.[135] Raising inheritance tax rates to extremely high levels would change the internal cost-benefit analysis of many individuals to a considerable extent. As a result, many more people would be rendered on the "margin" of the choice between saving to provide inheritances and spending in the present for personal satisfaction.[136] Given this altered

used to purchase debt instruments or deposited with a bank, broker, or other financial institution, they are indirectly invested in other business enterprises. In this way, such assets are still added to the total capital stock available in the market.

133. *See infra* notes 141-47 and accompanying text.

134. Given the lack of unambiguous limitations on the General Assembly's ability to increase the inheritance tax, increasing Pennsylvania's inheritance tax rates to levels in excess of seventy-five percent is not beyond the realm of possibility. *See supra* Part II.A.

135. Implicit in this reasoning is the assumption that saving assets to provide financial security and increased opportunities to heirs and devisees and spending assets for immediate gratification are, respectively, an individual's primary and secondary preferences (*i.e.* that personal financial security or retention of perceived power are, at best, only tertiary considerations). If an individual's primary preference is to consume in the present, taxation of inheritances will only serve to strengthen the dominance of that preference. It is not merely an unrealistic assumption made for the sake of structured analysis that there exist persons with the value scale mentioned above. First, there are those individuals who have a secure income apart from the acquisition, saving, and investment of assets and lack any pretensions of power based on net worth. Second, as some individuals increase in age and decline in health, their perception of the security and power benefits linked with accumulated assets declines. These people recognize the relatively limited timeframe in which they will be able to benefit from their accumulated assets. If providing inheritances were not the primary consideration for many of these people, they would have more incentives to plan to die insolvent or spend their last dollar on the day they die. Thus, there are necessarily those persons whose primary preference is (or in the future will become) saving to establish inheritances for family, friends, and favorite causes.

136. Praxeology questions the validity of attempting to predict economic effects with mathematical exactitude. MURRAY ROTHBARD, THE LOGIC OF HUMAN ACTION ONE 60-69 (Edward Elgar 1997). Mises also makes this point:

> Praxeological knowledge makes it possible to predict with apodictic certainty the outcome of various modes of action. But, of course, such prediction can never imply anything regarding quantitative matters. Quantitative problems are in the field of human action open to no other elucidation than that by understanding.

internal calculus, many individuals will choose to spend rather than save,[137] a problem which is only exacerbated as the tax rates applied to property inherited by classes of intended legatees or heirs increases.[138] Such a significant shift in preferences away from saving would substantially increase capital consumption by individuals who would otherwise have saved to provide inheritances.[139]

Significant increases in capital consumption resulting from high inheritance tax rates would have severe economic consequences.[140] In

> We can predict . . . that—other things being equal—a fall in the demand for *a* will result in a drop in the price of *a*. But we cannot predict the extent of this drop . . . .
>
> The fundamental deficiency implied in every quantitative approach to economic problems consists in the neglect of the fact that there are no constant relations between what are called economic dimensions. There is neither constancy nor continuity in the valuations and in the formation of exchange ratios between various commodities. Every new datum brings about a reshuffling of the whole price structure. [Praxeological] [u]nderstanding, by trying to grasp what is going on the minds of men concerned, can approach the problem of forecasting future conditions. We may call its method unsatisfactory and the positivists may arrogantly scorn it. But such arbitrary judgments must not and cannot obscure the fact that [praxeological] understanding is the only appropriate method of dealing with the uncertainty of future conditions.

MISES, *supra* note 7, at 117-18.

137. The only alternatives are not between not saving at all and saving a particular amount. There are also degrees between those two, opposite choices that could result from one's perception of the costs and benefits associated with saving to leave an inheritance. For example, someone who, absent the inheritance tax, might have intended to save $100,000 for her siblings to inherit might only save $50,000 as a consequence of the inheritance tax.

138. Pennsylvania currently has a graduated inheritance structure that imposes a higher rate on property inherited by persons in a particular class, as defined in relation to the decedent. 72 PA. STAT. ANN. § 9116(a) (West 2008). In light of this present structure, it is reasonable to conclude the likelihood that Pennsylvania's inheritance tax will continue to be graduated, even if at much higher rates.

139. MISES, *supra* note 7, at 490-93, 520-23.

> As soon as those present wants are sated and the satisfaction of which is considered more urgent than any provision for the morrow, people begin to save a part of the available supply of consumers' goods for later use. This postponement of consumption makes it possible to direct action toward temporally remoter ends. It is now feasible to aim at goals which could not be thought of before on account of the length of the period of production required. It is furthermore feasible to choose methods of production in which the output of products is greater per unit of input than in other methods requiring a shorter period of production. The sine qua non of any lengthening of the processes of production adopted is saving, *i.e.*, an excess of current production over current consumption. Saving is the first step on the way toward improvement of material well-being and toward every further progress on this way.

Id. at 490.

140. The economic effects would likely be serious, regardless of the state of the economy in general. *Id.* at 739. It is unlikely that capital accumulation resulting from other factors would be enough to offset the capital consumption caused by extremely

light of the nature of capital,[141] continued economic growth is strongly influenced by the amount of capital available in society; increases in capital levels are a strong indicator of economic growth.[142] Conversely, declining levels of capital (*e.g.*, capital consumption) have been linked to "retrogressing economies."[143] Simply put, less capital limits production, and, as a result, fewer goods and services from which income is derived are created or generated.[144] This string of economic causation, expressed within the context of time, is indicative of economic decline.[145] This economic loss, however, is not limited to Pennsylvania's economy because of the way in which capital is distributed. Much of the capital owned by Pennsylvania residents, particularly capital assets in the form of cash, cash deposits, and other liquid assets, is put to productive use outside of Pennsylvania's borders.[146] However, capital consumption of Pennsylvanians' capital assets still has an economic effect within

high inheritance tax rates. *See infra* note 156 and accompanying text (noting the importance of capital accumulation and consumption resulting from other economic factors and the aggregate economic effect).

141. MISES, *supra* note 7, at 490-93, 514-17. *See also supra* notes 104-114 and accompanying text (discussing the praxeological nature of capital).

142. ROTHBARD, *supra* note 6, at 479-83.

143. *Id.* at 483-91. Rothbard notes that

> The case of decreasing gross capital investment is defined as a retrogressing economy. The decreased investment is first revealed as aggregate losses in the economy, particularly losses to firms in the highest stages of production . . . . As time proceeds, these losses will tend to disappear, as firms leave the industry and abandon the now unprofitable production processes . . . .
>
> . . . The greater the shift from saving to consumption, the more drastic will the effects tend to be, and the greater the lowering of productivity and living standards. The fact that such shifts can and do happen serves to refute easily the fashionable assumption that our capital structure is, by some magical provision or hidden hand, permanently and eternally self-reproducing once it is built. No positive acts of saving by self-reproducing capitalists are deemed necessary to maintain it. The ruins of Rome are mute illustrations of the error of this assumption.
>
> Refusal to maintain the value of capital, *i.e.*, the process of net dissaving, is known as consuming capital. Granting the impossibility of measuring the value of capital in society with any precision, this is still a highly important concept. "Consuming capital" means, of course, not "eating machines," as some critics have scoffingly referred to it, but failing to maintain existing gross investment and the existing capital goods structure, using some of these funds instead for consumption expenditure.

Id. at 483-85.

144. *Id.*

145. MISES, *supra* note 7, at 514-17.

146. This fact is most apparent with regard to bank deposits and bonds, where banks and bond issuers apply the funds collected to companies with operations around not only the United States, but the world.

Pennsylvania's borders because individuals oftentimes make capital investments in their own localities.[147]

Pennsylvania's inheritance tax rates, as currently provided in statute,[148] also have economic consequences similar to those of high inheritance tax rates, albeit to a much lesser degree.[149] Thus, the structure of Pennsylvania's current inheritance tax also increases the rate of ante-mortem capital consumption.[150] At current inheritance tax rates, some individuals recognize the decreased satisfaction of providing inheritances that will be smaller due to inheritance tax assessments.[151] Some of these persons weigh the decreased satisfaction against the opportunity cost of present consumption and conclude the latter to be a more attractive option.[152] However, given Pennsylvania's relatively low inheritance tax rates and the correspondingly small effect on decreasing the satisfaction of saving to provide inheritances, many people are not put on the "margin" of whether to save and, thus, do save to leave inheritances.[153] As a result, capital consumption under Pennsylvania's current inheritance tax rate structure, while still present, is significantly less than it would otherwise be if the Commonwealth imposed high inheritance tax rates.

Although Pennsylvania's inheritance tax, even at current rates, encourages some level of capital consumption, this alone has not created a shrinking economy in Pennsylvania.[154] Instead, Pennsylvania's economic growth (or decline) incorporates, and will continue to incorporate, numerous other variables as well, each of which is also a

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147. Some of the best examples are sole proprietors, other small business owners, credit unions, and small banks and financial institutions.

148. 72 PA. STAT. ANN. § 9116(a) (West 2008). The current rates are zero percent for property passed to spouses, four and one-half percent for property passed to grandparents, parents, lineal descendants, or spouses of a child, twelve percent for property passed to siblings, and fifteen percent for property passed to all other persons. *Id.*; *see supra* Part II.B (describing the statutory contours of Pennsylvania's current inheritance tax).

149. *See infra* notes 150-57 and accompanying text.

150. *See supra* notes 129-39 and accompanying text.

151. *See supra* notes 135-39 and accompanying text.

152. *See supra* notes 135-39 and accompanying text.

153. One interesting effect of Pennsylvania's current inheritance tax rate structure is that one's evaluation of the satisfaction to be obtained from saving to provide inheritances changes in relation to the expected beneficiaries. An individual who intends to provide inheritances to siblings or other collaterals may conclude that he has much less incentive to save, and subsequently does not save, because the inheritance he will provide is taxed at twelve percent and fifteen percent, respectively. 72 PA. STAT. ANN. § 9116(a) (West 2008) (providing the tax rates for property inherited by siblings and collaterals).

154. *See* Pennsylvania Department of Revenue Bureau of Research, 2008-2009 Estimate Documentation 17-28 (2008), http://www.revenue.state.pa.us/revenue/lib/revenue/2008_09_Est_Doc.pdf (providing data showing Pennsylvania's economic growth in recent years).

function of individual human actions.[155] These other factors may encourage capital accumulation, unlike the inheritance tax, to such an extent that the capital "consumed" as a result of the inheritance tax would be offset, with a net economic effect of capital accumulation and subsequent economic growth.[156] Alternatively, if these other factors were also to encourage capital consumption or were collectively unable to promote a level of capital accumulation sufficient to exceed the capital consumption resulting from the inheritance tax, the net economic effect would be economic decline resulting from capital consumption.[157]

Any consideration of the economic effects of repealing Pennsylvania's inheritance tax must also be considered in the context of this broader framework. Like House Bill 377, one of the most recent examples, as of yet there have been several unsuccessful attempts to phase out Pennsylvania's inheritance tax.[158] House Bill 377, as well as those other legislative proposals seeking to phase out the tax,[159] would have considerable economic consequences, including the elimination of all ante-mortem capital consumption resulting from the current inheritance tax.[160] Repealing the inheritance tax would remove the artificial disincentive, recognized by some individuals, to saving for the purpose of leaving inheritances for families, friends, and favored causes.[161] With the inheritance tax eliminated, those individuals who would not have otherwise saved will begin putting aside assets that, together with the assets from persons who would have saved despite the inheritance tax, would result in greater capital accumulation.[162] When combined with the other factors affecting Pennsylvania's economy,[163] this capital accumulation could further contribute to any capital accumulation and economic growth or offset, either completely or

155. Some of the best such examples are economic productivity rates, the development of new markets and industries, and Pennsylvania's ability to attract existing business. Another factor is any capital accumulation that still occurs, in spite of the inheritance tax, as people save to leave behind inheritances.

156. ROTHBARD, *supra* note 6, at 339-46, 350-56.

157. *Id.*

158. *See supra* Part II.C and, in particular, note 56.

159. H.R. 1444, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 808, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 836, 190th Gen. Assem., Reg. Sess. (Pa. 2007); S. 417, 190th Gen. Assem., Reg. Sess. (Pa. 2007); and H.R. 409, 190th Gen. Assem., Reg. Sess. (Pa. 2007).

160. *See infra* notes 161-64 and accompanying text.

161. *See supra* notes 129-39 and accompanying text.

162. MISES, *supra* note 7, at 490-93, 514-17. *See also supra* notes 104-14 and accompanying text (discussing the praxeological nature of capital).

163. *See supra* note 155 and accompanying text.

partially, any capital consumption and subsequent economic contraction.[164]

B. Ante-Mortem Capital Flight

High inheritance tax rates would substantially increase the rate of ante-mortem capital flight by also affecting individuals' subjective evaluations of the perceived costs and benefits of remaining domiciled in Pennsylvania and establishing domicile in another jurisdiction.[165] The legal concept of domicile plays a primary role in determining what inherited property is taxed.[166] Under Pennsylvania law, intangible property cannot be taxed if it is inherited from a decedent who was not domiciled in Pennsylvania.[167] The only property inherited from a non-Pennsylvania resident that can be taxed is tangible property physically located within the Commonwealth.[168] Thus, persons with substantial investments in intangible property could avoid having those assets taxed when distributed to legatees or heirs by domiciling themselves in a state without an inheritance tax.[169]

However, the decision of whether to establish domicile in another state includes weighing the perceived costs of relocating with the anticipated benefits reaped from avoiding Pennsylvania's inheritance taxes, all within the context of one's individual value scale.[170] Moving to another state inherently incurs some costs, which at the very least include the expense of physically transporting one's person and possessions to another state and any increases in the cost of living resulting from the relocation. Additionally, there may be the subjectively-determined emotional costs of leaving behind one's hometown, moving away from

164. *See supra* notes 155-57 and accompanying text.

165. *See infra* notes 166-87 and accompanying text.

166. Domicile "is the place at which an individual has fixed his family home and principal establishment for an indefinite period of time." *In re* Prendergast, 673 A.2d 324, 327 (Pa. 1996) (citing Dorrance's Estate, 163 A. 303 (Pa. 1932)). In continuing to describe the concept, the court found that

> [a] domicile once acquired is presumed to continue until it is shown to have been changed and where a change is alleged, the burden of proving it rests upon whoever makes the allegation. A new domicile can be acquired only by physical presence at a new residence plus intent to make that new residence the principal home. Intent is the actual state of facts, not what one declares them to be. An established domicile, however, can be retained without physical presence or residence until it be proven that a new domicile has been acquired.

Id. at 327-28 (citing Dorrance's Estate, 163 A. 303).

167. 72 PA. STAT. ANN. § 9111(h) (West 2008).

168. *Id.* § 9107(a)-(b).

169. Other states, like Florida, are attractive jurisdictions in which to establish domicile on account of their having large retirement communities, desirable weather, and no inheritance taxes.

170. *See supra* notes 99-102 and accompanying text.

family, friends, or a job, or having to reestablish oneself in a new community.[171] Individuals will weigh the sum of these subjective costs against the anticipated benefits of establishing domicile in that state. These anticipated benefits may include moving closer to family or friends, to a warmer climate, or where employment is more easily found.

For some, the decision to relocate will also include a consideration of the inheritance tax consequences.[172] Like the decision to save,[173] an individual will determine the anticipated present and future satisfaction from providing inheritances under the Pennsylvania inheritance tax regime and compare that estimate with the anticipated present and future benefit of providing inheritances under the laws of the state to which he plans to move.[174] Inheritance tax rates necessarily affect this analysis by altering the anticipated present and future satisfaction of saving to provide inheritances, thus increasing the perceived benefits of establishing domicile in a state with a lower inheritance tax rate.[175] Were Pennsylvania's inheritance tax rates to be increased to very high levels,[176] the anticipated benefits of relocating to a state with much lower, if any, inheritance tax rates would increase dramatically. This dramatic increase in the anticipated benefits of relocating would place more individuals on the "margin" of the decision to establish domicile in another state, thus strongly encouraging ante-mortem capital flight from Pennsylvania.[177]

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171. This is far from an exhaustive list of the costs that a person might perceive in moving to another state. Given the infinite uniqueness of individuals, the possibilities are endless.

172. Not all people are concerned about the effect that inheritance taxes will have on the future distributees who inherit their property. The concept of marginality, however, ensures that there are those who would consider the effect of moving on the taxation of inherited property. This is particularly true with regard to wealthy individuals and persons consciously attempting to save with the goal of leaving behind a substantial inheritable estate.

173. *See supra* notes 129-32 and accompanying text.

174. *See generally supra* notes 86-95 and accompanying text (describing the internal process of individual decision-making based on subjective value judgments).

175. *See supra* notes 129-35 and accompanying text (concluding that high tax rates significantly decrease the anticipated satisfaction from saving to provide inheritances).

176. *See supra* Part II.A.

177. Capital flight resulting from state inheritance or estate taxes was a not a problem before the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) "decoupled" the federal estate tax from state inheritance or estate taxes by eliminating the federal estate tax credit for state inheritance or estate taxes paid. Jeffrey A. Cooper, *Interstate Competition and State Death Taxes: A Modern Crisis in Historical Perspective*, 33 PEPP. L. REV. 835, 870-80 (2006). There is still some debate as to whether capital flight actually occurs as a result of state inheritances and estate taxes. A praxeological examination concludes that, necessarily, there will be those persons who move to avoid state inheritance taxes. *See generally supra* notes 96-103 and accompanying text (discussing the concept of marginality). It also appears that many states are convinced that inheritance taxes will have the effect of encouraging capital

The nature of this cost-benefit analysis creates a situation, only further exacerbated by high inheritance tax rates, in which wealthy individuals will have a greater incentive to relocate than those of less affluent means.[178] First, it is far more likely that people who are wealthy will incur fewer costs to establish domicile in another jurisdiction, because many of these people may already have a secondary home in another state. Establishing domicile in another state could mean converting that secondary home into one's primary residence by merely taking an extended "vacation" each year.[179] Second, wealthy individuals generally are more sensitive to inheritance tax consequences, as they are more likely to be concerned with providing considerable inheritances and asset protection.[180] For affluent individuals in particular, high Pennsylvania inheritance tax rates would significantly increase the benefits of relocating to other states, with the requisite effect on the decision of whether to move.[181]

The most serious consequence[182] of capital flight away from Pennsylvania is a decrease in income[183] entering or generated within the

flight, as many states abandoned their inheritance or estate taxes after the passage of EGTRRA. Cooper, *supra*, at 874-80. Additionally, other studies have concluded that some level of capital flight does result from state inheritance and estate taxes. *See* Jon Bakija and Joel Slemrod, *Do the Rich Flee from High State Taxes?: Evidence from Federal Estate Tax Returns* (Nat'l Bureau of Econ. Research, Working Paper No. 10645, 2004) (finding that high state inheritance taxes have a statistically significant, modest effect of encouraging capital flight). *But see* Elizabeth McNichol, Center on Budget and Policy Priorities, *Research Findings Cast Doubt on Argument That Estate Taxes Harm State Economies* (2007) http://www.cbpp.org/1-9-07sfp.pdf (summarizing research arguing that state inheritance taxes do not cause capital flight and, subsequently, harm state economies).

178. *See infra* notes 179-81 and accompanying text.

179. Establishing domicile in another state could be as simple as registering one's vehicle in another state or registering to vote and actually voting in another state. *In re* Prendergast, 673 A.2d 324, 328 (Pa. 1996). In the context of owning two homes, one will not be considered a domiciliary or resident individual of Pennsylvania if he does not spend more than a total of 183 days a year in Pennsylvania. 72 PA. STAT. § 7301(p) (West 2008).

180. Beyond being intuitive, briefly scanning through the contents of magazines marketed to individuals with high net worth will establish this fact.

181. *See supra* notes 178-80 and accompanying text.

182. An additional consequence of the capital flight resulting from Pennsylvania's inheritance tax is the loss of human capital. Avoiding Pennsylvania's inheritance tax necessarily involves establishing domicile in another state, which has an obvious effect on the size of Pennsylvania's workforce. This draining of human capital may be limited, however, in that those more likely to relocate due to inheritance tax considerations (*e.g.*, older Pennsylvanians) are also likely to be retired. Although this is probably the case, there may be other economic consequences linked to general population loss. *See* ROTHBARD, *supra* note 6, at 505 (briefly describing some of the economic effects of population growth).

183. The term "income," as used here refers to its common definition of money received, which reflects the broad meaning given it by the Internal Revenue Service. 26

Commonwealth. One of the primary features of capital assets is their ability to generate income.[184] Not only is this true for "hard" capital assets like land and industrial machinery, but it also applies to capital assets like bank deposits, bonds, and stock.[185] The time value of money necessitates that individuals who have allowed others to use their money be compensated accordingly in the form of interest and dividends,[186] which can add up to substantial amounts of income.[187] High inheritance tax rates encourage a proportionate level of capital flight, which, in turn, has a commensurate effect on the amount of income brought into or generated within Pennsylvania.

As Pennsylvania's inheritance tax is currently structured, it encourages ante-mortem capital flight, although to a much lesser degree than would high inheritance tax rates.[188] Individuals make the decision of whether to establish domicile in another state by weighing the costs of relocating against the expected benefits.[189] The current inheritance tax rates still increase, to some extent, the benefits one anticipates from relocating by providing a way to avoid Pennsylvania inheritance taxes.[190] This is particularly true for two categories of individuals: 1) affluent persons whose future estates will retain a significant amount of assets in another state[191] and 2) persons who plan to leave their estates to siblings

U.S.C.A. § 61 (West 2008). In its specific, praxeological sense, "income" refers to a much more specific category of property. MISES, *supra* note 7, at 260-64.

184. ROTHBARD, *supra* note 6, at 298-301, 319-22 (referring to this income as interest, a term with a specific praxeological definition that differs from the definition of the Internal Revenue Service).

185. *Id.*

186. Dividends from stock fall into this category as a result of the nature of stock. At some point in the past, a share of stock was issued in exchange for money that was to be used by the issuer. In return, the stock purchaser received a residual right to the income generated by the issuer and distributed in the form of dividends. Selling stock necessarily includes selling this residual right to income and, thus, is similar to selling one's interest in a note or other debt instrument.

187. ROTHBARD, *supra* note 6, at 298-301, 319-22 (referring to this income as interest, a term with a specific praxeological definition that differs from the definition of the Internal Revenue Service).

188. *See infra* notes 189-93 and accompanying text.

189. *See supra* notes 170-77 and accompanying text.

190. *See supra* notes 172-77 and accompanying text.

191. For example, if Anne plans to leave an estate of $1,000,000 in cash and stock to her children, her estate will realize inheritance tax savings of $45,000 if she establishes domicile in a state that does not levy an inheritance tax. On the other hand, if Bob plans to leave an estate of $250,000 in cash and stock to his children, his estate will realize inheritance tax savings of $11,250 if he relocates to a state without an inheritance tax. Assuming that both Anne and Bob recognize an equivalent level of costs in moving from Pennsylvania and that they have substantially similar attitudes towards money and the nature of inheritances, Anne will be much more inclined to move, because the benefits of doing so would be higher for her. Furthermore, the perceived benefits of relocating

or collaterals.[192] These people are more likely to establish domicile in another state, which results in a mild[193] level of capital flight and its corresponding economic effects, namely a decrease in the amount of income in the form of interest and dividends realized in Pennsylvania.

Because some capital flight occurs as a result of Pennsylvania's current inheritance tax, repealing the Commonwealth's inheritance tax would decrease ante-mortem capital flight. Without the artificial incentive created by the possibility of relocating to avoid Pennsylvania's inheritance tax,[194] more people would be constrained by their subjective evaluations of the costs associated with moving. As a result, many people, their capital assets, and the income those capital assets would generate would remain in Pennsylvania.

C. Post-Mortem Capital Consumption

High inheritance tax rates would considerably increase post-mortem capital consumption by requiring the liquidation of considerable amounts of capital assets to pay inheritance tax assessments.[195] Necessarily, cash must be raised to pay inheritance tax assessments; Pennsylvania does not accept other forms of property as payment.[196] If enough cash is not readily available, capital assets like stock, bonds, and real property may have to be sold to raise the needed funds. After being collected by the Pennsylvania Department of Revenue, these funds are added to the Commonwealth's treasury, with much smaller amounts, if any, being converted, once again, into capital assets owned by the state.[197]

The fact that another party purchases the capital assets being sold and, as a result, those capital assets continue to exist and retain their

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would be even more considerable for individuals planning to leave estates significantly exceeding the $1,000,000 estate used in this scenario.

192. For example, if Anne plans to leave an estate of $1,000,000 in cash and stock to her great-nephew, with whom she is very close, her estate will realize inheritance tax savings of $150,500 if she establishes domicile in a state that has no inheritance tax. If Bob, however, plans to leave an estate of $1,000,000 in cash and stock to his daughter, his estate will realize inheritance tax savings of $45,000 if he moves to a state without an inheritance tax. Once again, Anne will be much more inclined to move, because the benefits of doing so would be considerably higher for her. *See supra* note 191 (using same methodology and similar scenario to come to a similar conclusion).

193. The encouragement of capital flight is "mild" under the current inheritance tax regime in comparison with what it would be with an inheritance tax that imposed high rates.

194. *See supra* notes 172-77 and accompanying text.

195. *See infra* notes 196-206 and accompanying text.

196. 72 PA. STAT. ANN. § 9136 (West 2008).

197. Under a praxeological analysis, it is necessarily impossible for governments to replace the level of savings and investment that would have occurred through private decision-making. ROTHBARD, *supra* note 6, at 815-31.

character as such[198] does not controvert the praxeological conclusion that an increase in capital consumption occurs as well. To purchase these capital assets, another individual or entity would have to expend assets that were already contributing to the total amount of capital assets already integrated into the market.[199] Withdrawing significant funds from one's accounts at a financial institution[200] has the effect of increasing capital consumption[201] by diverting funds that have already been infused into the capital market in the form of loans and bond purchases from the financial institution.[202] The result is a decrease in total capital, or capital consumption, proportionate to the amount necessary to satisfy an inheritance tax assessment.

For this same reason, using one's own funds to pay inheritance taxes and, thus, avoiding having to sell capital assets still results in capital consumption.[203] To make the necessary payments, funds will be withdrawn from accounts at financial institutions, which had previously injected at least a significant portion of those funds into the capital

198. There is no guarantee that a purchased capital asset will retain that character while under the ownership of the purchaser. For example, it is possible that a purchaser may convert real property previously rented for business use to private apartments. Assuming that capital assets will not be converted is useful only for the sake of argument.

199. The only exception to this principle is where an individual is able to pay for the property being sold solely with hoarded cash. Hoarded funds, by definition, are never deposited with financial institutions that would then feed those funds into the capital market. Still, however, hoarded cash plays a praxeologically significant economic role. MISES, *supra* note 7, at 521-23.

200. For capital consumption to occur, it is unnecessary that the actual purchaser of the assets being sold to pay for inheritance taxes withdraw the necessary funds from his bank. Rather, only one or several persons indirectly related to the transaction need to take funds from their accounts at financial institutions for the effect to be capital consumption. For example, if Anne wishes to purchase a portion of a sole proprietorship that is being sold to satisfy the inheritance taxes of the deceased sole proprietor, she will have to sell stocks that she has held to raise the necessary funds. Although Anne is selling stock and, therefore, is not withdrawing funds from a financial institution, the purchaser/s of her stock (or other individuals or entities in the chain) will need to withdraw funds in order to make the necessary payment. Thus, the effect on the availability of capital is the same as if Anne herself had withdrawn the amounts needed for the purchase.

201. An increase in capital consumption will occur as a result except where the withdrawn funds are used to fund the production of capital assets that were not previously existing or used as capital assets.

202. Not only is this one of the primary functions of financial institutions, but it is also one of their principal means of generating revenue. Reserve rates do not avoid this capital consumption, because as deposits are withdrawn, reserve rates would also decrease.

203. The only general exception to this rule is when hoarded cash is used. *See supra* note 199.

market.[204] Not having to withdraw funds from a bank, but being able to pay an inheritance tax assessment with insurance proceeds is also ineffective in avoiding capital consumption; on a macro-level, insurance companies function in ways very similar to banks and other financial institutions.[205] Therefore, funds that would be put into the capital market by insurance companies[206] would instead be diverted to satisfy Pennsylvania inheritance taxes. Post-mortem capital consumption would be significant under high inheritance tax rates, as relatively more capital assets would need to be liquidated to meet the Commonwealth's tax assessments.

Pennsylvania's current inheritance tax causes post-mortem capital consumption. Even at current, relatively low rates, the inheritance tax diverts funds from the capital market.[207] The inheritance tax and the requirement that assessments be satisfied with cash forces individuals to pay with saved funds or liquidate other assets.[208] These saved funds were previously injected into the capital markets by the financial institutions with which they were deposited.[209] Likewise, many of the liquidated assets will be capital assets purchased by another with saved funds, which also has the effect of drawing capital out of the market.[210] Although the effect of the Pennsylvania inheritance tax, as currently in statute, is to encourage capital consumption, the overall economic vitality of the Commonwealth depends on how the capital consumption is geographically distributed[211] and the role played by other economic variables.[212]

Repealing Pennsylvania's inheritance tax would eliminate the post-mortem capital consumption that results from the inheritance tax.[213]

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204. *See generally* MURRAY N. ROTHBARD, THE MYSTERY OF BANKING (2d ed. The Ludwig von Mises Inst. 2008) (discussing the economic role played by banks and financial institutions).

205. *Id.*

206. For many individuals, a primary incentive to purchase life insurance would be altered or even eliminated with certain changes to or a repeal of the Pennsylvania inheritance tax. In such situations, at least a portion of the money that comprises premiums paid to insurance companies would be directly converted into capital assets or indirectly injected into the capital market by being deposited into a bank or other financial institution.

207. *See generally supra* notes 208-12 and accompanying text.

208. 72 PA. STAT. ANN. §§ 9136-9154 (West 2008).

209. *See supra* note 204 and accompanying text.

210. *See supra* note 204 and accompanying text.

211. MISES, *supra* note 7, at 513, 517-20. Regardless of how the capital consumption is specifically distributed, there will virtually always be a significant effect within Pennsylvania itself. *See supra* note 155 (providing several reasons as to why the capital consumption resulting from an inheritance tax will affect the state that levies it).

212. *See supra* notes 154-57 and accompanying text.

213. *See supra* notes 207-12 and accompanying text.

With no reason to artificially expend saved funds or liquidate other capital assets to pay an inheritance tax assessment, these assets would remain available to the capital market to be put to productive use.[214] Capital would not be diverted from the capital market, unlike under the current regime, and, as a result, no capital consumption would be caused by inheritance taxes.

D. State Revenue

High inheritance tax rates would significantly increase state revenue in the short term, but would also have the opposite long term effect of rapidly decreasing state revenue.[215] It is apparent that high inheritance tax rates would increase state revenue to a substantial degree in the short term.[216] However, state revenue would likely decline in the long term as individuals responded to those high inheritance tax rates.[217] Rapidly declining state revenue would result from high inheritance taxes and their effect on ante-mortem capital consumption, ante-mortem capital flight, and post-mortem capital consumption.[218] Capital flight creates a situation where money from which taxable income (in the form of interest and dividends) is derived is indirectly pushed to other states that do not levy an inheritance tax.[219] Likewise, capital consumption, whether ante-mortem or post-mortem, eliminates a direct source of taxable income by "consuming" these same forms of income-generating capital assets.[220] Additionally, as capital assets used for productive use became unavailable, production would decrease, with a subsequent decline in other, related tax revenues, such as income taxes, excise taxes, sales taxes. In light of the severe consequences that high inheritance tax rates would have on capital flight and capital consumption, the effect on the decline in state revenues would be correspondingly severe.

Pennsylvania's current inheritance tax provides comparatively little state revenue. During Pennsylvania's 2007-2008 budget year, the

214. *See supra* notes 198-206 and accompanying text.

215. *See infra* notes 216-20 and accompanying text. Praxeology rejects the notion that governments have the potential to spur economic growth at rates greater than individuals in an unhampered market economy. *See* MISES, *supra* note 7, at 698-858; ROTHBARD, *supra* note 6, at 765-878.

216. This simply results from the fact that higher tax rates generate more revenue in the short term by taxing a higher proportion of income or assets.

217. *But see* Jon Bakija and Joel Slemrod, *Do the Rich Flee from High State Taxes?: Evidence from Federal Estate Tax Returns* (Nat'l Bureau of Econ. Research, Working Paper No. 10645, 2004) (concluding that declines in revenue would not occur as a result of capital flight).

218. *See supra* Part IV.A-C and accompanying text.

219. *See supra* notes 176-81 and accompanying text.

220. *See supra* notes 134-47, 195-206 and accompanying text.

inheritance tax raised $801,200,000 for the Commonwealth's coffers.[221] However, with total state revenue of $28,188,100,000, the amount generated by the inheritance tax represented only 2.8% of Pennsylvania's budget.[222] Additionally, the percentage of the state's budget raised by the inheritance tax has decreased from nearly 3.4% since the 2002-2003 budget year.[223] Likewise, even at current tax rates, Pennsylvania's inheritance tax causes some level of capital consumption and capital flight.[224] This decreases the amount of taxable income and production generated from capital not only in the present, but into the future as

221. Pennsylvania Department of Revenue Bureau of Research, 2008-2009 Estimate Documentation 1 (2008), http://www.revenue.state.pa.us/revenue/lib/revenue/2008_09_Est_Doc.pdf.

222. *Id.*

223. The amount of revenue raised by the inheritance tax, the Commonwealth's total budget, and the percentage of that total budget constituted by the inheritance tax is provided in the following chart for tax years 2002-2003 through 2007-2008:

INHERITANCE TAX REVENUE AS A PERCENTAGE OF PENNSYLVANIA'S BUDGET

Budget Year	Inheritance Tax Revenue	State Budget	Inheritance Tax as a Percentage of State Budget
2007-2008	$801,200,000	$28,188,100,000	2.8%
2006-2007	$738,200,000	$26,866,200,000	2.7%
2005-2006	$725,500,000	$25,252,600,000	2.9%
2004-2005	$719,300,000	$24,157,400,000	3.0%
2003-2004	$704,300,000	$22,191,300,000	3.2%
2002-2003	$715,700,000	$21,206,000,000	3.4%

Data compiled from: Pennsylvania Department of Revenue Bureau of Research, 2008-2009 Estimate Documentation 1 (2008), http://www.revenue.state.pa.us/revenue/lib/revenue/2008_09_Est_Doc.pdf; Pennsylvania Department of Revenue Bureau of Research, 2007-2008 Estimate Documentation 1 (2007), http://www.revenue.state.pa.us/revenue/lib/revenue/2007_08_Est_Doc.pdf; Pennsylvania Department of Revenue Bureau of Research, 2006-2007 Estimate Documentation 1 (2006), http://www.revenue.state.pa.us/revenue/lib/revenue/2006_07_Est_Doc.pdf; Pennsylvania Department of Revenue Bureau of Research, 2005-2006 Estimate Documentation 1 (2005), http://www.revenue.state.pa.us/revenue/lib/revenue/2005_06_Est_Doc.pdf; Pennsylvania Department of Revenue Bureau of Research, 2004-2005 Estimate Documentation 1 (2004), http://www.revenue.state.pa.us/revenue/lib/revenue/2004_05_Est_Doc.pdf; Pennsylvania Department of Revenue Bureau of Research, 2003-2004 Estimate Documentation 1 (2003), http://www.revenue.state.pa.us/revenue/lib/revenue/2003_04_Est_Doc.pdf.

It is interesting to note, however, that the Department of Revenue estimates that the percentage of Pennsylvania's budget derived from the inheritance tax will increase for the next five budget years. Pennsylvania Department of Revenue Bureau of Research, 2008-2009 Estimate Documentation 1 (2008), http://www.revenue.state.pa.us/revenue/lib/revenue/2008_09_Est_Doc.pdf.

224. *See supra* notes 148-57, 188-93, 207-12 and accompanying text.

well.[225] Depending upon other economic variables,[226] the progressive decrease in capital levels resulting from capital flight and direct taxation has the potential to decrease the Commonwealth's revenue in the long term.[227]

Conversely, repealing Pennsylvania's inheritance tax would decrease state revenue in the short term, but would maintain the state's tax base and has the contingent potential to increase state revenue or offset other revenue losses in the long term. Without the capital flight and capital consumption encouraged by Pennsylvania's inheritance tax,[228] income and production generated from capital that would otherwise not be available would be added to sources of current tax revenues. Furthermore, a portion of this income and production would likely be added to the stock of available capital, further increasing Pennsylvania's future tax base. Similarly, if other economic variables were to cause a depletion of Pennsylvania's capital levels, the amounts contributed as a result of repealing the state's inheritance tax would offset some or all of this other capital consumption.[229]

V. BEYOND PRAXEOLOGY: IMPLICATIONS FOR THE DEBATE

Praxeology's purpose is primarily educational; it seeks to inform individuals about the economic consequences of their actions and the policies of larger social collectives such as states, businesses, organizations.[230] With this information, people are able to apply their value judgments to the economic consequences of varying public policy options. Furthermore, praxeological insight enables individuals to

225. Each year, as less capital is available with which to generate income and production, Pennsylvania's tax base will contract. This process, year after year, when combined with subsequent increases in taxes to compensate for budget shortfalls, will create a situation primed for economic decline.

226. *See supra* notes 154-57 and accompanying text.

227. *But see* MISES, *supra* note 7, at 740-41 (indicating that it is possible for a tax at certain rates to not impair economic growth in stating that "[c]apital levies, inheritance and estate taxes, and income taxes are . . . self-defeating if carried to extremes"). Mises concluded the following:

> Businessmen complain about the oppressiveness of heavy taxes. Statesmen are alarmed about the danger of "eating the seedcorn." Yet, the true crux of the taxation issue is to be seen in the paradox that the more taxes increase, the more they undermine the market economy and concomitantly the system of taxation itself. Thus the fact becomes manifest that ultimately the preservation of private property and confiscatory measures are incompatible. Every specific tax, as well as a nation's whole tax system, becomes self-defeating above a certain height of the rates.

Id. at 741.

228. *See supra* notes 158-64, 194, 213-14 and accompanying text.

229. *See supra* note 155 and accompanying text.

230. MISES, *supra* note 7, at 10.

compare policies with competing evaluations from an economic perspective.

With regard to Pennsylvania's inheritance tax, praxeology supports the conclusion that high inheritance tax rates would cause significant economic decline by fostering both capital consumption and capital flight, with a secondary effect being a decline in state revenue.[231] Likewise, under a praxeological examination, the Commonwealth's current inheritance tax causes some capital consumption and capital flight, albeit at levels insufficient to have presently created economic decline in Pennsylvania.[232] Repealing Pennsylvania's inheritance tax would foster additional economic growth through the increase of capital accumulation and a decrease in capital flight, which could have the contingent potential of increasing state revenue in the long term.[233] In terms of the debate over the Pennsylvania inheritance tax,[234] the key praxeological insight is that the tax does not encourage economic growth.[235] Rather, Pennsylvania's inheritance tax is something of a hindrance to economic expansion.[236]

These praxeological conclusions have profound implications for the debate over the Pennsylvania inheritance tax. First, advocates of the tax should[237] not argue that it generates economic growth for the Commonwealth.[238] This is not to say that it does not generate positive economic benefits[239] for Pennsylvania; depending on one's normative values, economic decline or maintaining a certain level of production or standard of living may be a more ethical option.[240] These conclusions relate to praxeology's second implication with regard to Pennsylvania's inheritance tax debate: proponents of the inheritance tax would do well

231. *See supra* notes 134-47, 165, 176-81, 195-206, 215-20 and accompanying text.
232. *See supra* notes 148-57, 188-93, 207-12, 221-27 and accompanying text.
233. *See supra* notes 158-64, 194, 213-14, 228-29 and accompanying text.
234. *See* The General Assembly of Pennsylvania, Legislative Journal-House 83 (January 16, 2008), http://www.legis.state.pa.us/WU01/LI/HJ/2008/0/20080116.pdf (providing evidence of the debate).
235. *See supra* Part IV.
236. *See supra* Part IV.
237. This is a normative conclusion that stands outside the realm of praxeological analysis. Rather, it assumes and applies the value judgment that honesty is important in open and meaningful discussion and debate.
238. *See supra* Part IV (analyzing Pennsylvania's inheritance tax and discussing its economic effects).
239. The word "benefit" implies a value judgment that is distinct from the descriptive facts of economic growth or decline.
240. *See supra* note 112 (mentioning article by Richard Douthwaite questioning the benefits of economic growth).

to focus their energy and resources on arguments about the non-economic benefits of the inheritance tax.[241]

VI. CONCLUSION

For the purposes of analysis, Pennsylvania's inheritance tax, the oldest in the nation,[242] can be examined in three different formulations: 1) an inheritance tax that imposes a high tax rate, 2) a graduated inheritance tax, as currently in state, with lower tax rates, and 3) an inheritance tax that has been repealed or is ineffective.[243] The first of these formulations is theoretically possible due to the lack of clear, unambiguous limitations on the power of the Commonwealth to tax inherited property or the right of succession.[244] Pennsylvania's inheritance tax, as actually codified in statute,[245] provides the second of these formulations.[246] The third formulation has not yet been realized, despite numerous attempts to repeal the inheritance tax.[247]

Praxeology, as the study of human action, is appropriately suited for economic analysis of Pennsylvania's inheritance tax and its economic consequences.[248] The Commonwealth's inheritance tax is an economic variable that some individuals will consider in their decision-making processes.[249] Thus, when the praxeologically-derived principles of means, ends, value scales, time preferences, and marginality are employed as tools of analysis,[250] the inheritance tax, in each of its three formulations, is shown to affect four praxeologically-significant categories of economic factors: ante-mortem capital consumption, ante-mortem capital flight, post-mortem capital consumption, and state revenue.[251]

241. One such popular example is the argument that the inheritance tax is necessary to protect or enhance the meritocratic nature of Pennsylvania and the United States or to maximize state revenue in the short term.

242. 1825-26 Pa. Laws 227-30.

243. *See supra* Part II.

244. *See supra* Part II.A. *See, e.g.*, *Carpenter*, 58 U.S. at 456; *In re* Estate of Lander, 207 A.2d 753 (Pa. 1965); *In re* Estate of Pickering, 190 A.2d 132 (Pa. 1963); *In re* Estate of Wright, 138 A.2d 102 (Pa. 1958); *In re* Tack's Estate, 191 A. 155 (Pa. 1937); *Shugars*, 130 A. at 426; *In re* Kirkpatrick's Estate, 119 A. 269 (Pa. 1922); *Strode*, 1866 WL 6214.

245. 72 PA. STAT. ANN. §§ 9101-9196 (West 2008).

246. *See supra* Part II.B.

247. *See supra* Part II.C. *See, e.g.*, H.R. 1444, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 808, 190th Gen. Assem., Reg. Sess. (Pa. 2007); H.R. 836, 190th Gen. Assem., Reg. Sess. (Pa. 2007); S. 417, 190th Gen. Assem., Reg. Sess. (Pa. 2007); and H.R. 409, 190th Gen. Assem., Reg. Sess. (Pa. 2007).

248. *See supra* Parts III-IV.

249. *See supra* Parts III-IV.

250. *See supra* Part III.

251. *See supra* Part IV.

Were Pennsylvania's General Assembly to increase the inheritance tax rates to high levels, the Commonwealth would be faced with severe economic consequences. High inheritance tax rates would alter the value scales of many individuals, leading some of these individuals to save and invest less, with the end result being increased capital consumption.[252] Likewise, for some individuals, high inheritance tax rates would decrease the opportunity cost of establishing domicile in a state that assesses the tax at a lower rate or does not impose an inheritance tax.[253] This capital flight would take with it much of the income and production that would otherwise be generated as a result of capital investment.[254] Furthermore, high inheritance tax rates would cause post-mortem capital flight, as larger amounts of capital assets would need to be liquidated to pay inheritance tax assessments.[255] As a result of these economic trends, state revenue would increase substantially in the short term, but would decrease in the long term.[256]

As the Commonwealth's inheritance tax is currently structured, ante-mortem capital consumption, capital flight, and post-mortem capital consumption also occur, although to a much lesser degree than would result from the imposition of high inheritance tax rates.[257] However, due to other economic variables that affect rates of capital consumption and capital flight, Pennsylvania's economy has not contracted.[258] Despite the state's economic growth, the loss of capital resulting from Pennsylvania's inheritance tax could, contingent upon other economic factors, decrease the tax base over the long term, thus depleting future sources of state revenue.[259]

Repealing Pennsylvania's inheritance tax would eliminate the capital consumption and capital flight the tax currently encourages.[260] This would increase capital accumulation within the Commonwealth or offset other sources of capital consumption, which could significantly expand Pennsylvania's tax base and, thus, generate more state revenue over the long term.[261]

As a descriptive rather than a normative system of analysis, praxeology does not necessitate that a particular course of action be

252. *See supra* notes 134-47 and accompanying text.
253. *See supra* notes 176-81 and accompanying text.
254. *See supra* notes 176-81 and accompanying text.
255. *See supra* notes 195-206 and accompanying text.
256. *See supra* notes 215-20 and accompanying text.
257. *See supra* notes 148-57, 188-93, 207-12 and accompanying text.
258. *See supra* notes 154-57 and accompanying text.
259. *See supra* notes 221-27 and accompanying text.
260. *See supra* notes 158-64, 194, 213-14 and accompanying text.
261. *See supra* notes 154-64, 194, 213-14, 228-29 and accompanying text.

taken or advocate for any public policies.[262] To do so would require the application of value judgments that lie beyond the scope of praxeology.[263] Praxeology's only function is educational; praxeology seeks to provide insight into the economic consequences of both individual and public policy choices.[264] With this knowledge, options can be better understood and evaluated.[265] Praxeology's key insight with regard to Pennsylvania's inheritance tax is that the tax does not encourage economic expansion.[266] This fact, however, should be dispositive only if the values reflected in Pennsylvania law are intended to encourage economic growth as the primary end of state policy.[267] Alternatively, other normative conclusions may weigh in favor of the inheritance tax.[268] Despite the vital informational role of praxeological economics, public policy considerations, like the debate over Pennsylvania's inheritance tax, are inherently matters of normative value that must be discussed, examined, and decided in the public sphere.

262. *See supra* Part III.
263. *See supra* Part III.
264. *See supra* Part III.
265. *See supra* Parts III, V.
266. *See supra* Part IV.
267. *See supra* Part V.
268. *See supra* Part V and, in particular, note 241.