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Who Pays the Death Tax?

The underlying principle of the death tax is "Tax the Rich." No more sophisticated analysis is needed. Whatever the tax's excesses and inefficiencies, they are justified because the burden for paying it falls upon the wealthy who, after all, can afford it.

But what if the wealthy aren't who we think they are? What if the burden of the tax falls not on high-income urbanites with upscale lifestyles, but on middle-income penny pinchers, low-income workers, and small and rural communities? What justification is there then for this tax on accumulated assets?

Today's American Millionaires

Exactly who are the wealthy in America? If you believe our popular culture, the answer is easy. America's millionaires have high incomes, live in fancy homes, drive fancy cars, wear fancy clothes, and contribute little to the economy except to provide plots for Danielle Steele novels. That is the popular-culture view of millionaires, and like so many views in pop culture, it's wrong.

For a more accurate view, pick up a copy of the *New York Times* best-selling book, "The Millionaire Next Door." In writing the book, authors Thomas Stanley and William Danko spent more than two decades studying wealth in America. What did they find? To paraphrase Robin Leach, the long-time chronicler of the "rich and famous," they searched for caviar dreams, but wound up finding a blue-collar work ethic. They found typical Americans with $1 million in assets:

- Are in their mid-fifties;
- Work between 45 and 55 hours a week;
- Represent first-generation wealth;
- Drive used or moderately priced domestic cars;
- Live in modest homes worth far less than they could afford; and
- Are self-employed.

The authors also found that high incomes do not necessarily lead to accumulated wealth. The authors found workers of all incomes who managed to accumulate sizable estates through hard work, diligent savings, and living below their means. Conversely, the authors found many Americans with extremely high incomes who essentially had no assets — "Big hat, no cattle" was how the authors described them.

The death tax is levied against estates worth $1 million and more. Each taxable estate represents a lifetime of accumulated assets – consumption forgone. The death tax isn't targeted at conspicuous consumers. On the contrary, it is targeted at people who work hard, live below their means, and save for their family's future. Those savings, in turn, make up the foundation of our communities and the American economy.

Death Tax Assaults Family Farms and Businesses

Does the death tax hurt family farms and family businesses? The answer is a definitive "Yes." Among their more important findings, the authors of "The Millionaire Next Door" determined that self-employed Americans are *four* times as likely to accumulate a million dollars in net worth than those Americans who work for someone else – and thus are four times more likely to have their estates subject to the federal death tax.

Furthermore, although the self-employed make up only 20 percent of the American workforce, they account for two-thirds of the millionaires. On average, 21 percent of the assets of the wealthy is their private business. As the authors conclude, "In general, most American millionaires are manager-owners of businesses."

Yet IRS statistics show that taxable estates usually include only a small percentage of business assets. Why the discrepancy? The statistics provided by the IRS are misleading. They reflect the composition of an estate after all the estate planning and costs have been incurred. For a clearer picture of the impact of the death tax on small business, you have to look through the eyes of the taxpayer, not the tax collector.

- A June, 1999 survey by the Center for the Study of Taxation found eight of ten family-owned businesses reported taking steps to minimize the impact of the death tax.

- A 1995 Gallup poll found one-third of small business owners surveyed expected all or part of their business would be liquidated to cover future death tax liabilities.

- Yet another report by the Family Enterprise Center conducted in 1995 found 80 percent of black-owned businesses report they do not have sufficient assets to pay the death tax without selling some or all of the business.

If the death tax doesn't hurt small businesses, why are so many small business owners focused on the death tax? The evidence is clear. The death tax is a direct assault on family farms and small businesses.

What About Jobs? – The Cost of Compliance

One of the death tax's many flaws is families have no way of knowing how much they will owe or when they will owe it. Surviving family members must plan for a 55-percent tax without the usual road maps that accompany other taxes. This uncertainty results in extraordinary compliance costs that are not reflected in any IRS data.

- The Upstate New York survey found the average spending on estate planning was nearly $125,000 per business.

- A similar survey by the National Association of Women Business Owners found the death tax imposed nearly $60,000 in death-tax-related costs on female business owners.

- Finally, the National Association of Manufacturers found more than 40 percent of its members surveyed had spent more than $100,000 on attorney and consultant fees related to death-tax planning. For three out of five members, *annual* compliance costs were more than $25,000.

These death-tax compliance costs, imposed on living, breathing businesses, affect their ability to expand and hire workers. The impact of the death tax on jobs is dramatic:

- In the Upstate New York survey, an estimated 14 jobs per business already have been lost as a result of federal estate-tax planning. For the 365 businesses surveyed, the total number of jobs lost due to the death tax was more than 5,000.

- A study by Douglas Holtz-Eakin (Tax Notes, August 2, 1999) found the estate tax caused an annual 3-percent reduction in desired hiring by sole proprietors.

- And a 1995 Gallup Poll found three out of five business owners report that they would add more jobs over the coming year if the death tax were eliminated.

Jobs lost. Jobs not created. The evidence is overwhelming that the costs of the death tax include decreased job creation and decreased opportunity for small business employees. Since small-business jobs make up a disproportionate part of rural and low-income areas, those are the communities that bear the brunt of the death tax.

Death Tax and the Economy: Not Good For Each Other

Death tax supporters seldom articulate why the death tax should be collected at all. They might raise concerns about the revenue loss of repealing the tax, or the skewed distribution tables (skewed because they attribute tax benefits to the deceased) of who benefits from repeal, but a coherent argument outlining why the death tax is an essential part of our tax code is difficult to make. Perhaps that is because there is no valid reason.

Studies by the Joint Economic Committee, the National Center for Policy Analysis, the Institute for Policy Innovation, the American Council for Capital Formation, the Research Institute for Small and Emerging Businesses, the Heritage Foundation, the Cato Institute, Tax Notes, and others focus attention on the impact of the death tax on the economy.

Not surprisingly they all found the death tax causes lower savings, less capital accumulation, lower growth, and fewer jobs. Some of these studies found the economic costs of the death tax result in lower overall revenues to the federal treasury than if the tax were eliminated. Finally, the Holtz-Eakin study focused on the impact of the death tax on entrepreneurs, and found the tax discourages the risk-taking behavior that characterizes the successful American entrepreneur.

It follows that a tax designed to confiscate accumulated savings discourages industry and hurts the economy. What doesn't follow is the number of academics and politicians who continue to support this tax. As liberal death-tax critic Edward McCaffery observed in "The Moral Case Against the Death Tax" (Cato Institute, October, 1999), "The death tax rewards a 'die-broke' ethic, whereby the wealthy spend down their wealth on lavish consumption, and discourages economically and socially beneficial intergenerational saving." Lavish consumption is neither a conservative nor liberal priority.

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We all do. We pay it through lower wages and fewer jobs. In high-unemployment regions like Upstate New York and elsewhere, the death tax destroys badly needed jobs before they are created.

We pay it through the destruction of our communities. In hundreds of American towns, small, family-owned businesses are struggling to survive against the competition provided by large corporate retailers. Home Depot doesn't pay the death tax. The family-owned hardware store does. The death tax accelerates the transfer of wealth from the owners of small businesses to the owners of large, public corporations.

And we pay it through slower growth and less wealth. Study after study shows the death tax reduces savings, lowers investment, and restricts the capacity of the economy to grow. The death tax literally confiscates capital — the lifeblood of any economy. That means lower incomes and fewer opportunities for ourselves, as well as our children.

Death tax supporters argue we cannot afford to repeal this tax. All the evidence suggests just the opposite. We cannot afford to continue this destructive tax.

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