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## The Death of the "Death Tax"?: An Introduction

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*On October 6, 2000, Cleveland-Marshall College of Law, Cleveland State University, hosted a one-day conference entitled: The Death of the “Death Tax”? The keynote luncheon speaker was Joel Slemrod, Paul W. McCracken Collegiate Professor of Business Economics and Public Policy at the University of Michigan Business School. Panel participants throughout the day included, in alphabetical order, Ira Bloom, Professor of Law at Albany Law School, Patricia A. Cain, Professor of Law at the University of Iowa College of Law, Joel C. Dobris, Professor of Law at the University of California at Davis, Joseph M. Dodge, the W.H. Francis, Jr., Professor of Law at the University of Texas Law School, Carolyn Jones, Professor of Law at the University of Connecticut School of Law, James Repetti, Professor of Law at Boston College Law School, Richard Schmalbeck, Professor of Law at Duke University School of Law, and James G. Wilson, Professor of Law at Cleveland-Marshall College of Law. Several of the participants have agreed to publish their work in this symposium issue, introduced by Deborah A. Geier, Cleveland-Marshall College of Law, who organized and hosted the conference.*

## THE DEATH OF THE “DEATH TAX”? AN INTRODUCTION

DEBORAH A. GEIER<sup>1</sup>

Good morning! My name is Deborah Geier, and I am a member of the faculty here at Cleveland-Marshall College of Law. I first want to thank each and every one of our panelists today for saying “yes” to my entreaties to come to Cleveland and participate in this one-day conference considering the possible repeal of the estate tax. I next want to thank each and every one in the audience for coming to share this day of ideas with us.

In the brief ten minutes that I have reserved to introduce the day, I would like to consider the question: What brings us together today to consider the possible repeal of the estate tax? We would not likely be here today if the repeal of the estate tax were not a serious political possibility, and it would not likely be a serious political possibility if many middle-class taxpayers earning the median household income of about \$40,000 to \$50,000 per year<sup>2</sup> did not support outright repeal, rather than much-needed reform. A June, 2000, Gallup poll, for example, indicated that 60% of those polled favored elimination of the estate tax, “even though only 17% [believed that] they ‘would personally benefit.’ (Even that 17% is far higher than reality.)”<sup>3</sup> Why do they support outright repeal today when they would not have done so, say, ten years ago? As a Wall Street Journal article described, “[a] decade ago, when business groups first started campaigning against what they call the death tax, ‘we

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<sup>1</sup>Professor of Law, Cleveland-Marshall College of Law.

<sup>2</sup>Different sources quote different numbers for the current household median income. See, e.g., Diana Jean Schemo, *Colleges Post Average Rise in Tuition of 5 Percent*, N.Y. TIMES, Oct. 17, 2000, at A23 (“In the last decade, the median family income has risen 8 percent, to \$49,012 from \$45,552, after adjusting for inflation.”); Steven A. Holmes, *Incomes Up and Poverty is Down, Data Show*, N.Y. TIMES, Sept. 27, 2000, at A12 (“The Census Bureau reported today that median household income topped \$40,000 for the first time last year ....”).

<sup>3</sup>See Jacob M. Schlesinger & Nicholas Kulish, *As Paper Millionaires Multiply, Estate Tax Takes a Public Beating*, WALL ST. J., July 13, 2000, at A1.

were laughed out of rooms,' says Dan Blankenburg, a lobbyist for the National Federation of Independent Business. The tax applied only to the wealthiest Americans, and everyone in Washington, Republicans included, told him 'you'll never get that repealed.'"<sup>4</sup>

In the past, pressure for major legislative change occurred only when the tax began to reach more than 2% of those who died. The Fall 1999 issue of the IRS Statistics of Income Bulletin contained a chart with a table compiling the estate tax returns as a percentage of adult deaths in selected years between 1934 and 1995.<sup>5</sup> The number was generally between 1 and 2% for each year until you got to 1958, when it exceeded 2% for the first time, reaching 2.84%.<sup>6</sup> It exceeded 3% in 1960 and 1962, 4% in 1965, 5% in 1969, 6% in 1972, and it reached a high of 7.65% of all adult deaths in 1976.<sup>7</sup> By 1982, it was back down to 1.82%, where it has stayed relatively constant.<sup>8</sup> What happened between 1976 and 1982? The gross estate filing threshold was only \$60,000 in 1976, only \$10,000 higher than the \$50,000 threshold in effect way back in 1934,<sup>9</sup> and the corresponding increase in numbers of decedents being subjected to the tax provoked political change. By 1982, the threshold had been raised to \$225,000, and today it generally stands at \$675,000, already scheduled to go up to \$1 million, \$2 million for a married couple, even without further legislative amendment.<sup>10</sup> The point is that widespread pressure for change occurred in the past only when the tax began to hit significantly more than 2% of all adult deaths. That is not the case today.<sup>11</sup> And it would not be the case in the foreseeable future under the Democrats' reform alternative of raising the estate tax threshold to \$4 million per couple (more for family farms and small businesses) and reforming the base and rate structure, which would exempt from liability more than half of all decedents who would otherwise owe a tax under the current structure.<sup>12</sup>

So what changes in taxpayer psychology or the economy or in social attitudes accounts for support for full repeal so far down the income spectrum? After all, it's undeniable that the estate tax is extremely progressive for the very reason that it

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<sup>4</sup>*Id.*

<sup>5</sup>See 19 SOI BULLETIN, Number 2 (Fall 1999), Table 16, at 285.

<sup>6</sup>*Id.*

<sup>7</sup>*Id.*

<sup>8</sup>*Id.*

<sup>9</sup>*Id.* at 314 n.2.

<sup>10</sup>See I.R.C. §§ 6018(a), 2010(c) (1994).

<sup>11</sup>In 1997, estate tax was owed by 1.9% of all decedents. See Albert R. Hunt, *Reform the Estate Tax, Don't Repeal It*, WALL ST. J., June 8, 2000, at A25.

<sup>12</sup>See generally David Cay Johnston, *Despite Benefits, Democrats' Estate Tax Plan Gets Little Notice*, N.Y. TIMES, July 13, 2000, at C1; Martin A. Sullivan, *Estate Tax Compromise or Repeal: The Rich Versus the Super Rich*, 88 TAX NOTES 298 (2000); Tanner, *Blue Dogs Throw Estate Tax Relief a Lifeline*, TAX NOTES TODAY, available in LEXIS, Fedtax Library, TNT file, Sept. 28, 2000, 2000 TNT 189-2 (each briefly describing the Democrat proposal). The Democrat proposal "would slash by two-thirds the already small number of families facing such a tax." Schlesinger & Kulish, *supra* note 3.

collects tax from fewer than 2% of all decedents each year. Moreover, many in this room know that, of the 2% that pays tax, more than half of all revenues are collected from the top 6%.<sup>13</sup> In other words, the truly super rich pays more than half of all estate tax revenues, with the other 94% of taxable estates paying less than half of all estate tax revenues, and 98% of people who die owing no tax at all. As a New York Times editorial put it, “Seldom have so many voted for a gargantuan tax cut for so few.”<sup>14</sup>

Several of the stock responses that seek to explain this support by median income earners might, in fact, be true, such as the possibility that people severely misunderstand the tax. For example, those who support repeal have claimed again and again, and thus many people believe, that the dollars taxed under the estate tax were already taxed once under the income tax. Many in this room know that this is not entirely true, that much of what is taxed under the estate tax is capital income that escapes taxation at the individual level under our porous income tax,<sup>15</sup> with the estate tax thus serving as an important backstop to the income tax.<sup>16</sup>

And they have also repeatedly claimed that many farms and small businesses have to be sold on death to pay estate taxes.<sup>17</sup> While commentators agree that there must surely be some farm or small business somewhere that was, indeed, sold to pay estate taxes, no one seems to have ever been able to find it.<sup>18</sup> As most people in this

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<sup>13</sup>In 1998, the top 6% of the approximately 2% of all decedents who owed estate tax paid \$10.39 billion in taxes, while the remaining 94% of taxable estates paid \$9.96 billion in taxes. See Schlesinger & Kulish, *supra* note 3, at charts (drawn from the Federal Reserve’s Survey of Consumer Finances, U.S. Treasury, Edward N. Wolff, NYU). “[T]he bulk of each year’s inheritance tax is actually paid by only a few thousand multimillion-dollar estates. This really is a tax levied almost entirely on the very, very well off.” Paul Krugman, *Death and Taxes*, N.Y. TIMES, June 14, 2000, at A31.

<sup>14</sup>See Editorial, *A Gift to the Wealthiest*, N.Y. TIMES, June 11, 2000, § 4, at 1; Bob Herbert, *A Handout for the Very Wealthy*, N.Y. TIMES, June 26, 2000, at A17 (quoting the editorial).

<sup>15</sup>Much of the wealth taxed under the estate tax consists of appreciation in the value of property, such as stocks and real estate, that is taxed neither to the decedent nor the heir (because of the step up in basis at death for the heir under I.R.C. § 1014) under the income tax. See, e.g., Schlesinger & Kulish, *supra* note 3 (describing as “not entirely accurate” the notion that “the estate tax amounts to double taxation—that the government is taking still more from income it has already skimmed”).

<sup>16</sup>See, e.g., Sullivan, *supra* note 12, at 300 (referring to the estate tax as “a backstop to the leaky, progressive income tax”).

<sup>17</sup>Indeed, to make the point regarding family farms once again, Congress delivered to the White House the estate tax repeal bill passed in the summer of 2000 via a rancher driving a tractor. See Ryan J. Donmoyer, *Clinton Wields Veto Pen on GOP Estate Tax Bill*, 88 TAX NOTES 1184 (2000).

<sup>18</sup>As one newspaper article described the phenomenon:  
Professor Harl, the Iowa State University estate tax expert, said that he had heard many horror stories about people having to sell farms to pay estate taxes. But in 35 years of conducting estate tax seminars for farmers, he added, “I have pushed and pushed and hunted and probed and I have not been able to find a single case where estate taxes caused the sale of a family farm; it’s a myth.”  
Johnston, *supra* note 12.

room again likely know, farms and small businesses that are sold on death typically are sold because the kids have no desire to continue dad's business, but would rather have the cash and follow their own dreams to be a doctor or a lawyer instead. Thus, those businesses would be sold even if the tax were repealed.

While misunderstanding might, in fact, explain the phenomenon to at least some extent, I would like to suggest that *perhaps* the support actually signals a more fundamental change in taxpayer psychology and attitudes toward wealth acquisition. I would like to suggest that in decades far past, one's good fortune was taken, in part at least, as just that—as “good fortune”—in part due to luck or good genes or being in the right place at the right time in the right country in the right era. Progressive taxation, including but not limited to the estate tax, was not uncommonly viewed as an appropriately larger contribution to the public fisc to support the economic and social environment—a regulated capitalist system—that makes such top-heavy wealth acquisition possible in the first place. That doesn't seem to be the case anymore. It seems to me that Americans more and more feel that whatever wealth comes under their control is attributable solely to their own hard work and merit, and even the wealthy are viewed by the nonwealthy as having “earned” their wealth. One recent Gallup poll, for example, found that 53% believed that the rich are rich because of “strong effort,” while only 32% credited “luck” or “circumstances beyond [their] control.”<sup>19</sup> And Lawrence Lindsey, Governor George W. Bush's chief economic advisor, has said that “the envy argument ... carries a lot less weight than it used to [because Americans] have a sense that those who have money today have earned it.”<sup>20</sup>

As an aside, this change in attitude—if indeed it is a change—is occurring when, for example, nearly 40% of the Forbes 400 in 1999 achieved their wealth the easy way: they inherited it, with this 40% slice inheriting on average \$2.5 billion each.<sup>21</sup> Or as the Economist magazine put it in 1998, “In many cases, the rich have got richer by doing rather little. An American who had \$500,000 in shares and a \$500,000 New York apartment fifteen years ago, and has merely held on to them, is now \$5 million better off.”<sup>22</sup> Wealth begets wealth, sometimes without much effort, which has perhaps contributed in part to the increasing wealth concentration in this country, with the top 1% nearly doubling their share of national wealth between 1976 and 1998.<sup>23</sup>

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<sup>19</sup>Schlesinger & Kulish, *supra* note 3.

<sup>20</sup>*Id.*

<sup>21</sup>See Phil Galewitch, *There Are 268 American Billionaires ...*, CLEV. PLAIN DEALER, Sept. 24, 1999, at 2A.

<sup>22</sup>*The Challenge for America's Rich*, THE ECONOMIST, May 30, 1998, at 15.

<sup>23</sup>As reported recently:

This newfound concern about economic “fairness” to the richest families follows a quarter-century in which the upper crust has prospered more, relatively speaking, than the rest of the country. The wealthiest 1% of American families held 38.1% of the country's net worth in 1998, the most recent year for which data are available, according to calculations done by New York University economist Edward Wolff. The proportion of wealth held by the richest 1% has climbed steadily from a low of 21.8% in 1976.

Schlesinger & Kulish, *supra* note 3.

But more to the point, if I am right in my suspicions that attitudes toward the wealthy and their desert (and I'm not talking about ice cream) are changing, it is particularly ironic that this should be happening now, at the end of the 1990s and the beginning of the 21st century, if we are persuaded by the arguments made by Robert Frank and Philip Cook in their provocative 1995 book that "winner-take-all markets" are becoming ever more common.<sup>24</sup>

As described by Frank and Cook, a winner-take-all market has several characteristics. It is one in which *relative* merit, as opposed to only absolute merit, determines who wins, where differences in absolute merit might actually be quite small.<sup>25</sup> Think of the difference between the gold medal winner at the Olympics and the silver medalist. Only hundredths of a second might separate them, but the financial rewards that go to the gold medalist in endorsements, *etc.*, are huge, while no one remembers the silver medalist only days later.<sup>26</sup>

The miler who triumphs in the Olympic Games, who places himself momentarily at the top of the pyramid of all milers, leads a thousand next-best competitors by mere seconds. The gap between best and second-best, or even best and tenth-best, is so slight that a gust of wind or a different running shoe might have accounted for the margin of victory.<sup>27</sup>

Moreover, increasingly competitive market conditions due to many factors, including increasing technology and the breakdown of loyalty within organizations,<sup>28</sup> bids up the price of that relatively small group of winners to heights not commonly seen prior to the 1980s in spheres outside sports and entertainment.<sup>29</sup> Today, the authors argue that winner-take-all markets "have permeated law, journalism, consulting, medicine, investment banking, corporate management, publishing, design, fashion, and even the hallowed halls of academe."<sup>30</sup> Whereas the median income in an increasing number of professions has remained relatively constant, the distributions around that median have become far more pronounced, with the winners at the top gaining a significantly higher share.<sup>31</sup> The realm of pay reaped by

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<sup>24</sup>ROBERT H. FRANK & PHILIP J. COOK, *THE WINNER-TAKE-ALL SOCIETY* (1995).

<sup>25</sup>"Reward by relative performance is the single most important distinguishing characteristic of winner-take-all markets." *Id.* at 24; *see generally id.* at 23-25.

<sup>26</sup>"A second feature of winner-take-all markets is that rewards tend to be concentrated in the hands of a few top performers, with small differences in talent or effort often giving rise to enormous differences in incomes." *Id.* at 24.

<sup>27</sup>*Id.* at 17 (quoting JAMES GLEICK, *GENIUS* 128 (1992)).

<sup>28</sup>*See generally* ROBERT H. FRANK & PHILIP J. COOK, *THE WINNER-TAKE-ALL SOCIETY* 45-84 (describing a host of factors that have contributed to the recent growth of winner-take-all markets).

<sup>29</sup>"In effect, the reward structure common in entertainment and sports—where thousands compete for a handful of big prizes at the top—has now permeated many other sectors of the economy." *Id.* at viii.

<sup>30</sup>*Id.* at 3-4.

<sup>31</sup>*See id.* at 61-84.

CEOs is one much-discussed example. “Today’s average chief executive earns 475 times as much as the average factory worker, up from a ratio of forty-two in 1980.”<sup>32</sup>

While some positive economic effects no doubt arise from winner-take-all markets,<sup>33</sup> Frank and Cook also describe many negative effects. One is that such markets attract too many contestants, to the detriment of overall economic efficiency (*i.e.*, aggregate societal wealth). Seeing the huge payoffs that are reaped by winners like Michael Jordan, for example, may cause too many inner-city youths to spend more time on the playground shooting hoops in unrealistic hopes of making the NBA than in the classroom, where they might learn the skills to earn a perfectly satisfying living as an accountant. As a result, they (and society) lose out on their earnings as an accountant.<sup>34</sup>

Another is that, because small differences in relative merit can result in huge differences in the payoff, winner-take-all markets encourage the equivalent of unproductive positional arms races, *i.e.*, wasteful investments that are incurred by the contestants in an attempt to get that relative edge over the other contestants. Think of the taking of anabolic steroids and other performance-enhancing drugs by Olympic athletes. None would do that if they could be sure that the others would not as well, but if they cannot be sure that the others will not, they are induced to engage in this behavior as well, for no net benefit to either the contestant pool at large or society.<sup>35</sup> The authors trace the same response in such areas as competition to be admitted into the elite universities.<sup>36</sup>

And, finally, the authors note that “[w]inner-take-all markets have increased the disparity between rich and poor.”<sup>37</sup>

So a reduction of the huge payoff that goes to the small group of winners could help to ameliorate these negative effects, which leads the authors to assert that the age-old tradeoff in tax values between fairness and economic efficiency might not hold true in winner-take-all markets. It may no longer be true, they assert, that progressive taxation decreases economic efficiency. It might actually *increase* economic efficiency<sup>38</sup> and decrease the negative consequences, such as the wasteful investment in enhancement behavior, that typify a winner-take-all market<sup>39</sup> by

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<sup>32</sup>*Labour Pains*, THE ECONOMIST, Sept. 23, 2000, at *The New Economy Survey* 25.

<sup>33</sup>See FRANK & COOK, *supra* note 24, at 4.

<sup>34</sup>See *id.* at 7-9, 101-21.

<sup>35</sup>See *id.* at 9-11, 125-46.

<sup>36</sup>See *id.* at 147-66.

<sup>37</sup>See *id.* at 4; see also FRANK & COOK, *supra* note 24, at 5-7.

<sup>38</sup>“To the extent that most of society’s top earners are participants in winner-take-all markets, it follows that a more progressive tax structure would not reduce but actually increase economic efficiency!” *Id.* at 21. “In economies in which winner-take-all effects are important, output not only need not fall with increases in tax rates on high incomes, but it may very well rise sharply.” *Id.* at 123. While only anecdotal evidence, it is interesting to note that the significant marginal income tax rate increases on the wealthy enacted in 1990 (the 31% bracket) and 1993 (the 36% and 39.6% brackets) preceded the biggest increase in productivity that this nation has seen in some time. Now, of course, our increased productivity is due no doubt to a host of factors that are perhaps only dimly understood today, but nevertheless. . . .

<sup>39</sup>*Id.* at 121-23, 212-17.

forcing the winners in such markets to shoulder more of the costs of the negative externalities that can arise in such markets.<sup>40</sup> Moreover, they also note:

Winner-take-all markets have implications not only for efficiency but also for norms of fairness. The economist's theory of wages, which holds that workers are paid in proportion to the value of their productive contributions, was never intended to justify market income distributions on ethical grounds. Nonetheless, many see a certain rough justice when pay is distributed on that basis, for the system rewards not only talent but also the willingness to expend the effort. In winner-take-all markets, however, pay distributions will be more spread out—often dramatically so—than the underlying distributions of effort and ability. It is one thing to say that people who work 10 percent harder or have 10 percent more talent should receive 10 percent more pay. But it is quite another to say that such small differences should cause pay to differ by 10,000 percent or more.... The realization of how winner-take-all markets contribute to income inequality may affect the extent to which society tries to alter market distributions in the name of fairness.<sup>41</sup>

Now, I do want to make clear that the authors nowhere mention the estate tax, and I therefore do not want to impute to them any stated support for the estate tax. In fact, I have a sneaking suspicion that they would, in fact, *not* support it.<sup>42</sup> But my modest point is that I think that their work at the least suggests the irony that at a time when winner-take-all markets seem to be gaining increasing prominence and depth in our economy, where at least a *portion* of the winners' rewards is due more to current market mechanisms than their own ability and worth (particularly for the top winners, who are the most likely to be subject to the estate tax), an increasing segment of the population actually believes just the opposite—or we wouldn't all be here today discussing the very real possibility of full repeal of wealth transfer taxes.

With those introductory thoughts, let me introduce our first panelist....

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<sup>40</sup>*Id.* at 20.

<sup>41</sup>FRANK & COOK, *supra* note 24, at 17.

<sup>42</sup>The authors support progressive consumption taxation, in contrast to progressive income taxation. *See id.* at 213-17. Other commentators who support progressive consumption taxation do not support the estate tax, seeing in both a fatal flaw in the disincentive to save, whether or not that disincentive actually affects savings behavior. *See, e.g.*, Edward J. McCaffery, *The Missing Links in Tax Reform*, 2 CHAPMAN L. REV. 233 (1999) (citing and discussing his prior work that has consistently argued for a progressive-consumption-without-estate-tax regime).