The Death Tax

Editorial

A small business I know which employs twenty people is owned by the surviving spouse who is aged. The son would like to continue the business and is doing what he can to prepare for the coming date when he will have to pay roughly $3 million in estate taxes to the government, but he does not know if the business will survive or will have to be liquidated and the employees will have to be discharged. Having worked with this business for almost thirty years I know the employees well. They are a cheerful group who like their work and the owner; they have been well paid in salary and benefits.

In the United States, more than 70 percent of family businesses do not survive to the second generation and 87 percent do not make it to the third generation. Family businesses fail because they do not have the liquidity to pay the death tax. They have paid taxes all of their lives, but the last tax kills the business they established.

Some small businesses might survive by selling to a larger corporation, but this would not be an adequate solution. If a small chemical business sold its assets to a larger firm, the larger firm would gain contracts but would absorb the new work in the larger factory. Few employees would hold their jobs or would do so only by relocation. (A large corporation is eternal as long as it does not lose money, but it never pays the equivalent of a death tax, and so has an advantage over a small business.)

From 1977 to 1990, 78 percent of all new jobs created in the United States were created by family businesses, from small Mom-and-Pop stores to large enterprises. Large, well-established corporations can be creative and have tried to be so in the last few years by internal discipline, but the creativity of the economy and of people is displayed by the number and variety of small businesses. Go into any small city in the United States and you will find new companies. The wiping out of a small business is a dagger into the heart of a healthy economy.

A survey was conducted in upstate New York in 1999 where 365 family businesses were asked how many jobs would be lost if the business were sold in whole or in part, or if money were borrowed to pay the estate taxes. Jobs lost to 365 businesses would be 5,100. The same business owners were asked how many jobs would be lost in the next five years if the principal owner died and estate taxes had to be paid. The answer: approximately 15,000 jobs.

Estate and gift taxes stifle growth. According to a study by Gary and Aldona Robbins, *The Case for Burying the Estate Tax,* if estate and gift taxes had been eliminated in 1999, by 2008

* Annual gross domestic product would be $117.3 billion, or 0.9 percent greater.

* The stock of U.S. capital would be higher by almost $1.5 trillion, or 4.1 percent.

* The economy would have created almost 236,000 more jobs.

* Between 1999 and 2008, the economy would have produced over $700 billion annually more in GDP.

Disregarding the cost of collecting estate and gift taxes, which is almost the same as revenue gained, the loss of income from estate and gift taxes would be more than offset by increased income and payroll taxes.

* Between 1999 and 2008, eliminating the estate tax would cost the Treasury $191.5 billion.

* But the over $700 billion in additional GDP would yield $18.7 billion annually in higher income, payroll, excise, and other federal taxes.

* In other words, higher growth would offset 98 percent of the estate revenue loss over the first ten years.

* By 2006, the dynamic revenue gain from eliminating the estate tax would be enough to offset the annual static revenue loss completely.

We should note the comparison of the top marginal death tax rates. The average rate is 24 percent. Argentina, Australia, Canada, China, India, Indonesia, and Mexico have no death taxes. (China and India have no money.) France and the United Kingdom have 40 percent death taxes, while socialist Sweden has 30 percent. Japan tops the list at 70 percent followed by the United States at 55 percent. On the other hand, Japan's top rate is based on $15,268,000 of assets while the U.S. rate applies to $3 million. It would seem that the death tax in the United States is the highest in the world.

In 1998 estate and gift tax collections amounted to $23 billion, less than 1.4 percent of the federal government's annual budget; but the costs associated with this income were just about equal to the money collected. Why then have the tax?

When the death tax was established in 1916, Congress said the purpose was to "break up the swollen fortunes of the rich," and that has been accomplished to a certain extent. With the largest estates of $20 million or more, less than a third goes to the heirs. The rest goes to state governments and the federal government with about 40 percent going to charity. The latter is a stratagem used by wealthy people to prevent the government from getting more than if charity were not supported.

The other argument in favor of death taxes is that the prevention of wealth to the heirs levels the field of opportunity and prevents heirs from lives of sloth. Said Andrew Carnegie a century ago,

> The parent who leaves his son enormous wealth generally deadens the talents and energies of the son, and leads him to lead a less useful and less worthy life than he otherwise would.

There is truth to the statement of Andrew Carnegie. We see in the election process multi-millionaires paying enormous funds from their pockets to be elected and who campaign on a program of giving money right and left to worthy and unworthy causes. Those who inherit large sums of money are often ignorant of the strains of life, without the experience of suffering to accomplish goals. Perhaps they suffer from a guilty conscience. Perhaps they are ignorant of the difficulty of building a business and accumulating wealth, and, with compassion want everyone to have as soft a life as they have known. The left-leaning children of wealth are certainly a contrast to the founders of great empires and act contrary to those who built the fortunes they have inherited. Not all wealthy heirs betray their heritage, of course. We do not hear of those who use their wealth to create more wealth by investment or new ventures.

Heirs to great fortunes are heirs for only a little while. Fortunes are dissipated by children, and children's children, whether or not the fortunes they received have or have not been used wisely. I am told that some of the Rockefellers have money, but it was not the amount it was fifty years ago, and it will be next to nothing in another couple of generations. Some of them will dissipate what they were given and some of them will be good stewards, helping others by gifts or investments. One way or another the money will be well used, either by the owners of wealth or the dissipation of wealth into more able hands.

The defense of the death tax is not persuasive. Whether or not it is good for children to inherit large or small amounts of money is irrelevant. It came into being as part of the growth of socialism and Communism and repeated the belief of Karl Marx that inheritance should be abolished. The death tax is based on envy. The death tax destroys the most creative sector the economy and creates unemployment. *Ω*