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Civilization at a Discount¹

The federal estate tax has been the subject of controversy for many years. Until very recently, conventional wisdom held that its repeal was politically impossible because the tax affected only the wealthy. But with the Republican sweep of Congressional power two weeks ago, repeal is almost reality. Why and how did this come to be?

An understanding has to begin with a very simple explanation of the estate tax. With that in hand, I will state the arguments for and against its repeal. Not to kill the suspense, but it will become obvious that I think repeal is a dreadful idea. I will suggest why the movement to abolish the tax nevertheless has support of the majority of Congress, and finally explore why much of the American public has bought in. Along the way, I hope you will find that all of this is more interesting – and far more distressing – than might appear at first blush.

A word about my perspective. I am a tax lawyer who doesn't need to know much about the estate tax. Two of my three law partners specialize in the planning and administration of large estates and trusts. Their work has allowed me to observe the practical effect of the estate tax. Although many of our law firm's clients are potentially subject to the estate tax, I don't speak as their advocate tonight. I have checked their interests at the door, in a manner of speaking, so as to ponder what is in the common good. My estate planning colleagues vigorously disagree with my views about the wisdom of estate tax repeal.

My subject is limited to estate tax *repeal*. I'm not going to address reform of the tax. The reason is that although there are numerous proposals for *reform*, President Bush and Republican congressional leaders won't discuss them. Republicans have said that permanently eliminating the tax is a defining issue for their party.²

With the preliminaries aside, please bear with me while I give you a short, oversimplified outline of the estate tax. Honest, folks, this won't hurt a bit.

¹ Henry Morgenthau, Secretary of the Treasury under Franklin D. Roosevelt, quipped that if taxes were the price of civilized society, then "too many citizens want civilization at a discount." Quoted in Thorndike, "Civilization at a Discount: The Morality of Tax Avoidance," *Tax Notes*, April 29, 2002.

² Hulse, "Battle on Estate Tax: How Two Well-Organized Lobbies Sprang into Action," *The New York Times*, June 14, 2002.

The estate tax has been with us since 1916. It was introduced partly to fund World War I, and partly in reaction to the excesses of the Gilded Age. Present law imposes a linked set of taxes on estates and lifetime gifts.³ In determining the estate that is subject to the tax, transfers to a surviving spouse, charitable gifts, debts, funeral expenses and administrative fees are deducted. Gifts and bequests of up to \$1 million are exempt from tax. If a decedent's estate includes a family-owned farm or business, it may be entitled to further deductions so long as the heirs keep the business going. In short, a married couple can pass about \$4 million to their children entirely free of tax. And with only the most basic family estate planning, the tax is payable (if at all) only upon the death of the surviving spouse. For estates above the exempt amounts, the tax rate begins at 37% and rises to 50% on taxable transfers above \$2.5 million.

There. That's all the technical information I'm going to give you. Let's move on to who pays the estate tax, and then to the debate over its repeal.

The estate tax raised about \$23 billion in 1999. This was less than two percent of total federal tax collections. Only about two percent of decedent's estates paid any estate tax in 1999,⁴ and the wealthiest one-sixth of one percent of all estates paid more than 50% of the tax.⁵ The estate tax is the most "progressive" of all federal taxes.⁶ That is, it is paid by those who can most afford to pay.

Nevertheless, estate tax repeal had become a red-hot political issue by the time of the presidential campaign of 2000. George W. Bush made it a centerpiece of his successful run for the presidency. Shortly after Bush came to office, Congress debated the options: continue the estate tax, modify it, or abolish it? Incredibly, it chose all three. The Economic Growth and Tax Relief Reconciliation Act ("EGTRRA") reduces the estate tax in the years 2002 through 2009, repeals the tax altogether in 2010, and finally restores it in 2011 as though EGTRRA had never been enacted in the first place.

EGTRRA's schizophrenic approach guarantees that the death tax is not dead. Accordingly, it has been a constant subject of agitation since EGTRRA passed, both on Capital Hill and on the campaign trail. The President has

³ There is also a generation-skipping tax that prevents a family from avoiding "layers" of estate taxes by making gifts or bequests directly to a grandchild or great-grandchild, thereby escaping tax at the child's level.

⁴ Burman and Gale, "The Estate Tax is Down but not Out," *Tax Notes*, February 25, 2002.

⁵ Krugman, "Springtime for Hitler," *The New York Times*, October 18, 2002.

⁶ By contrast, in 2000 the top one percent of taxpayers (ranked by adjusted gross income) paid 37.4% of all income taxes. They received 20.8% of all adjusted gross income. To qualify for this exclusive club, one had at least \$313,469 in adjusted gross income. Herman, "Elites' Slice of Income Grows as Does Their Share of Income Taxes," *The Wall Street Journal*, October 31, 2002.

continually prodded Congress to make estate tax repeal permanent. Last June, repeal passed the House 256-171 and failed in the Senate by only six votes.⁷

One would expect the debate over an 86-year-old part of our tax system to be based on compelling evidence and analysis. This is not the case at all. The debate is almost entirely lacking in hard facts on both sides. This is as amazing as it is discouraging. Let's review the major arguments for repeal of the tax.

The primary argument against the estate tax has traditionally been that it suppresses savings and encourages consumption. That is, it hurts those who save their wealth and favors those who spend it. The tax is therefore bad because saving is an important social goal. Furthermore, it is "not only fair but vital to the spirit of free enterprise to allow citizens to keep the wealth they [earn] . . . [T]axing wealth wrecks the incentives that have fueled the engine of American prosperity."⁸ Whether or not saving is important, there is little empirical data substantiating how saving is affected by the estate tax. The argument is therefore theoretical. Some theorists hypothesize that the estate tax discourages saving because the tax reduces the value of the estate. Other theorists point to the activities of all life insurance salespeople: the estate tax encourages those who wish to bequeath large sums to save more so that they can pay the estate tax for their children.

Whatever the effect of the estate tax on parents may be, its effect on heirs is unambiguous. Social scientists (including the rank amateur who speaks to you this evening) find that those who inherit large sums tend to consume more and work less than they otherwise would.

Another argument condemns the estate tax as inefficient. The argument is that the amounts spent avoiding it rival the amount of tax actually collected.⁹ This is certainly true in most instances. Crafty estate planning usually means the IRS doesn't get a dime. In others, however, the potential size of the tax can dwarf the avoidance costs. (I have pointed out to my estate planning colleagues that in these cases they would have to increase their fees to confiscatory levels to give the efficiency argument any credence. They have completely disregarded this helpful observation.) Treasury Secretary Paul O'Neill argues, "Too many small business owners today are forced to spend money on estate planning that could instead be invested in job-creating business expansions."¹⁰ That is certainly true, but the amount invested in a Fresno estate plan typically runs about \$2,500 to \$3,500.¹¹ That won't expand a business very much.

⁷ Hulse, "Effort to Repeal Estate Tax Ends in Senate Defeat," *The New York Times*, June 13, 2002.

⁸ Weisman, *The Great Tax Wars* (2002) (quoted in Forbes, "Where April 15 Came From," *The Wall Street Journal*, September 15, 2002).

⁹ Kessler, "Estate Tax Affects Few Heirs, yet Repeal Bid Gains Support," *The Washington Post*, June 4, 2000.

¹⁰ *Id.*

¹¹ This is a plug for my estate planning colleagues.

The estate tax is also criticized because it is excessive compared to other countries. In 1997, the United States ranked third among developed nations in transfer taxes as a percentage of overall revenues. But many developed nations have annual wealth taxes, which the United States does not.¹² It is difficult to develop an apples-to-apples comparison here.

Another complaint is the timing of the tax. It is payable nine months from date of death, when heirs can still be wrestling with the trauma of loss of a loved one. I grant the superficial appeal of this argument, but my own experience in paying an estate tax was different. To my surprise, doing so only served to remind me of my blessings. My parents were decidedly middle-class, but they had the good fortune to settle in the San Francisco Bay Area in the 60's, when housing was still cheap. Three decades later the house had appreciated 15-fold and there was an estate tax to pay when my father died. I had no objection to paying tax on what I considered a windfall. Much as I loved my parents, writing a check to the federal treasury didn't so much deepen my sense of loss as heighten my appreciation for all my parents had achieved.

By far the loudest part of the debate focuses on "small" and "family" farms and businesses. Proponents of repeal claim that the estate tax destroys small businesses, sometimes forcing family entrepreneurs to sell out to large concerns to fund their ultimate estate tax liabilities. But there is scant empirical data to support even this proposition. The evidence consists mainly of a few heart-rending anecdotes where the first generation could have taken steps to minimize the effect of the estate tax, but didn't. Small business owners and farmers do worry that they won't be able to pass on their enterprises to their children because of a crushing estate tax burden.¹³ Polls show that 37% of Americans think they will be subject to estate tax.¹⁴ Senator Rick Santorum of Pennsylvania declared that anyone who opposes estate tax repeal would be responsible for untold suicides.¹⁵ But the American Farm Bureau acknowledged to *The New York Times* that it could not cite a single example of a farm being sold to pay estate tax.¹⁶ In fact, the year 2000 list of the *Forbes* magazine Forbes 400 indicates that 137 of those listed had acquired their wealth through inheritance.¹⁷

¹² Burman and Gale, *supra* (comparing OECD nations).

¹³ Kessler, "Estate Tax Affects Few Heirs, yet Repeal Bid Gains Support," *The Washington Post*, June 4, 2000.

¹⁴ Goodman, "Taxing Family 'Fortunes' Nonissue for Most," *The Fresno Bee*, June 18, 2002.

Correspondingly, the polls indicate that 37% of respondents support complete repeal of the estate tax. *Tax Management Weekly Report*, June 17, 2002.

¹⁵ Goodman, *supra*.

¹⁶ David Cay Johnston, "Talk of Lost Farms Reflects a Muddle of Estate Tax Debate," *The New York Times*, April 8, 2001; see also Goodman, *supra*.

¹⁷ Phillips, *op. cit.*, p. 117.

Whatever weight we put on the anecdotes about how the estate tax affects family farms and businesses, the law allows them a sharply reduced tax. Farmland is taxed at its current-use value, for example, rather than its value as subdivision property. There is a special deduction for a family-owned farm or business that constitutes at least 50% of an estate, so long as the heirs materially participate. Alternatively, family businesses are often entitled to substantial valuation discounts. After all the discounting, what tax is actually assessed against a family-owned business can be paid in installments over 14 years. The rate of interest is two percent on the first \$1 million, with below-market interest rates on the balance. (Sorry. I fibbed when I said I wouldn't give you any more technical details.)

It should be noted that most of the value of family businesses tends to be represented by appreciation that was never subjected to income tax. Certainly, a tax paid at death is preferable to one paid during life. As it is, small businesses already receive federal assistance in the form of preferential income tax incentives and financial assistance. For example, San Joaquin Valley family cotton farming operations receive millions in annual federal crop subsidies. This makes cotton farming profitable, which in turn props up the values of the farmland, which in turn exposes everything to estate tax.

Most business owners I talk to are not deathly concerned about potential estate tax liability. Those for whom it is a worry concede they do not know the amount of the potential tax, again proving the adage that the devil we don't know is worse than the one we do. Nor have I witnessed destruction of any family farm or business by the estate tax. To the contrary, my sad experience is that the second generation usually has either no interest in the family business or dissipates it through mismanagement or inattention. Small businesses usually vanish once the first generation is gone, but through no fault of the estate tax. There is certainly nothing in the law that prevents the second generation from selling the farm to a developer and moving to the Coast.

Statistically, farm assets are reported on only about six percent of estate tax returns, farm real estate on about twice that amount. Farm assets account for less than three percent of the value of all estates of \$5 million or less.¹⁸ Even under the most expansive definition, assets of "family" farms and "small" businesses account for 11% of all assets reported.¹⁹ Examples of "family" businesses that have been at the center of estate tax litigation in recent years include the Kansas City Royals baseball team, Hallmark Cards, Estee Lauder cosmetics, and the S.I. Newhouse publishing empire. Each of these is a "family" business,²⁰ but none is

¹⁸ Friedman and Lee, "Estate Tax Repeal Would Be Costly, Yet Benefit only a Few," *Tax Notes*, June 24, 2002.

¹⁹ Burman and Gale, *supra*.

²⁰ The definition of "family" in the estate tax law is quite broad. It includes the decedent's spouse,

“small” by anybody’s definition. This raises the question, how small is a “small” business? In 1998, estates valued at \$600,000 to \$1 million accounted for half of all estate tax returns filed, but they had an effective rate of tax of six percent.²¹ Obviously, EGTRRA’s increase in the estate tax exemption to \$1 million has probably eliminated half of all estate tax payers. This would mean that the estate tax probably affects only the richest one percent of households today.

The last and most recent argument against the tax is that it is a moral outrage. It is said to be ethically repugnant to tax wealth that was subject to income tax during life. But most wealth as such is not subject to income tax. The bulk of most estates consists of assets that appreciated in value over the decedent’s lifetime but that were never sold. Never having been sold, they were never subjected to income tax. An example is my parents’ home. It made up the bulk of my father’s estate, but he never paid income tax on its 15-fold appreciation. In fact, I paid no income tax when I sold the home either. The law forgives income tax on appreciation of assets held at death, and does so whether or not an estate tax is paid.

To summarize, the arguments against the estate tax are that it discourages saving, is economically inefficient and psychologically inopportune, destroys small businesses and family farms, and is morally abominable. These arguments, either singly or in combination, do not present a compelling reason to repeal the estate tax. But are there compelling reasons to keep it?

Well, the estate tax is actually has virtues compared to other taxes. I recognize this is like saying that goat’s milk tastes better than cod liver oil. But think about it. We have already seen that the estate tax is imposed only on the wealth that is most able to pay, that nearly all of it is paid by the wealthiest one percent of estates, and that it is often imposed on appreciation in assets that never felt the sting of the income tax. In addition, the estate tax acts as a vital backstop to the income tax. I have from time to time seen the estate tax imposed on wealth accumulations from receipts that “somebody” forgot to report on income tax returns. Furthermore, the prospect of paying estate tax encourages the older generation to pass assets down to the younger generations during life, thus spreading wealth among family members. The estate tax is a strikingly important incentive to charitable giving, which spreads wealth even further. In 1999, estates gave \$14.6 billion to charity²² while total estate taxes paid were \$22.9 billion²³ -- only half again as much as charitable contributions. Finally, the estate tax -- alone among all taxes -- doesn’t have to be paid until death.

their children, grandchildren and great-grandchildren, their nieces and nephews and their spouses.

²¹ Kessler, “Estate Tax Affects Few Heirs, yet Repeal Bid Gains Support,” *The Washington Post*, June 4, 2000.

²² Friedman and Lee, *supra*.

²³ Burman and Gale, *supra*.

Virtues aside, a powerful argument for retaining the estate tax is the very cost of repealing it. In the spring of 2001, after the Bush Administration pushed EGTRRA through Congress, it forecast an overall budget surplus not counting Social Security. A year later, it was successfully pressing Congress to raise the federal debt limit by \$450 billion.²⁴ The Congressional Budget Office now projects that the federal budget deficit (outside of Social Security) will exceed \$350 billion in 2003,²⁵ and be mired in red ink each year for the rest of this decade. Bleak as it is, the CBO's projection was before Congress enacted its new farm bill (which disburses \$180 billion in crop subsidies), and before it authorized the President to wage war in Iraq.²⁶ So deficits now will be even worse than the CBO predicted. The ripple is being felt throughout the federal budget. An example is related by a client of mine who volunteers as congressional liaison for the national juvenile diabetes foundation. The foundation believes that a cure may have been found for juvenile diabetes, which is a particularly terrible affliction. It has been lobbying Congress for \$250 *million* in federal funding to conduct the necessary testing. But the Administration refuses to discuss the funding, citing the need to conserve funds for the war effort. The ten-year cost of estate tax repeal, by contrast, is projected to be \$740 *billion* – 3,000 times the cost of a possible cure for diabetes.

It also seems to me that our economy is entirely indifferent to the estate tax.²⁷ The decade leading up to the Bush presidential victory of 2000 was one of profound economic growth. *Income* grew significantly, especially after 1992. In the first seven years of the decade, *wealth* growth in these United States went from \$22 trillion to about \$37 trillion. The stock market has burnt about \$8 trillion since, but this is awesome by any measure. The total wealth of the American people increased by about 55 percent in seven years -- more than half of what we had accumulated since the very dawn of the Republic!

Moreover, our government and our society were so stable as to be the envy of the world. The international scene, in contrast, was pockmarked with massive political and economic instability. We witnessed war in the Balkans, massacres in Africa and Indonesia, and the threatened mutual annihilation of India and Pakistan. On the economic front, George Soros decimated the British pound in just a few days. The "tigers" of the Far East morphed into mere tabbies. Mexico melted down. By contrast, we have the power to impose *pax Americana*, which we did in the Balkans.

²⁴ Hulse, "Battle on Estate Tax: How Two Well-Organized Lobbies Sprang into Action," *The New York Times*, June 14, 2002.

²⁵ Paul Krugman, "Bush Administration's 'Just Trust Us' Doesn't Wash," *The Fresno Bee*, September 3, 2002.

²⁶ Friedman and Lee, *supra*.

²⁷ The comments about the impact of the estate tax on the economy are derived from a 2000 address by Rutgers University Law Professor Charles Davenport to the Tax Section of Bar Association of the City of New York.

These are the salient economic highlights of the '90's. And they all happened despite the estate tax!

The most disturbing aspect of estate tax repeal is that it would benefit very few. Over half of all estate tax paid in 1999 came estates exceeding \$5 million in value. The 3,283 largest estates paid 55% of the tax. The 467 largest estates paid 26% of the tax.²⁸

Repealing the tax for the benefit of these very few wealthy persons is disturbing for two reasons. One is that wealth is becoming extraordinarily concentrated in our nation. The other is that big money now controls big politics.

Wealth and income have consolidated at a breathtaking pace in the last quarter of the twentieth century. From 1976 to 1997, the share of *wealth* held by the top one percent of households more than doubled, from 19.9 percent to 40.1%.²⁹ A little more than 40 percent of American wealth was held by the top one percent of households. Remember the stock market boom? Those with retirement assets over \$1 million were the only group whose retirement wealth increased in the years 1993-1998.³⁰ No period in American history, not even the Gilded Age, have seen the likes of this.³¹

Statistics for *income* also show a striking upward redistribution. During the 22 years ended in 1999, every part of the American population, except the top one percent, received a lower share of our total income. The top one percent's average after-tax income grew 119.7%, and its share of all income grew from 7.3% to 12.9%.³² Meanwhile, inflation-adjusted, after-tax income of the bottom one-fifth of our households dropped 12%. Recall that this was also an era of reduced social spending. Data from federal income tax returns released last month shows the trend in another way. In the ten years ended in 2000, the share of all adjusted gross income reported by the top one percent of taxpayers rose from 13% to 20.8%.³³ Recent census data is similarly discouraging. For example, it shows that the inflation-adjusted income of the median California family actually dropped six percent in the 1990's.³⁴ (Do you remember so many nannies, gardeners, housekeepers and personal trainers in our midst ten years ago?)

²⁸ Friedman and Lee, *supra*.

²⁹ Phillips, *Wealth and Democracy* (Broadway Books, New York, 2001) p. 133.

³⁰ Dugas, "Retirement Crisis Looms as Many Come Up Short," *USA Today*, July 19, 2002.

³¹ Phillips, *op. cit.*, p. 396. The average compensation of chief executives of energy companies rose 22% in 2001 alone. Remember the PG&E and Enron bankruptcies? Mogul, "Executive Pay Went up in Year of Free Fall," *The San Francisco Chronicle*, November 13, 2002.

³² Phillips, *op. cit.*, p. 129.

³³ Herman, *supra*. To qualify for this exclusive club, adjusted gross income had to be \$313,469.

³⁴ Phillips, *op. cit.*, p. 115.

All of this concentration of wealth and income happened despite the presence of the federal estate tax *before* its amendment by EGTRRA. The conclusion is inescapable that even before EGTRRA, the estate tax did not hurt the top one percent at all. It appears to me that repealing the estate tax would merely gorge the opulent. American wealth distribution is beginning to resemble that of South America or Asia – a bowling ball at the top of a broomstick. When will the weight of the ball topple the broomstick?

This is my second concern, that excessive wealth concentration is a threat to democracy. It is the theme of Kevin Phillips' recent controversial book, *Wealth and Democracy*, which traces the uneasy alliance between money and politics in American history. Phillips demonstrates that throughout our history, government policy has played an indispensable role in the formation and continuation of great wealth. The federal government first minted fortunes when Alexander Hamilton successfully insisted upon the purchase of Revolutionary War debt at face amounts. Much of it had been purchased by well-connected speculators at steep discounts. A century later, the principal road to wealth was along railroad ties. Governments conferred enormous financial subsidies and about 200 million acres in land grants on the railroads. Even the newest fortunes, those of the information age, have the same pedigree. The first computer was developed by the government in 1943 to help plot artillery shell trajectories. The first applications of the transistor were for national defense and space exploration. The Internet grew from Department of Defense efforts before being turned over to private development in the late '70's. Global positioning systems went on sale to the public right after "smart bombs" helped win the first war on Iraq.

Phillips finds that great financial power has historically corroded American democracy. Most of the money from paying off the Revolutionary War debt went to speculators in just four states, and the steep excise taxes levied to pay those debts fell so heavily on rural areas as to lead to the Whiskey Rebellion. In the Gilded Age, United States senators were elected not by the voters but by state legislatures, which dangled like marionettes in the hands of the railroads, the sugar trusts, and the oil, steel and coal monopolies. Control of the Senate ensured that big business controlled the courts and the Army. Earlier this month, California Democratic Governor Gray Davis swept to re-election with a \$60 million war chest, \$10 million of which he spent on the Republican primary to ensure that his opponent would be the charismatically challenged Bill Simon. Governor Davis' unabashed largesse to his contributors has brought catcalls from Republicans about pay-to-play politics, but no calls for campaign finance reform. On the national stage, George W. Bush raised \$193 million in his successful presidential run two years ago. Calls for federal campaign finance reform by the President's primary opponent, John McCain, led to legislation that Bush signed only after vigorously opposing it. Whether the new law will be effective remains to be

seen.³⁵ It didn't apply to this month's elections, and both House and Senate campaigns produced all-time spending records. In the House of Representatives, the parties spent \$6 million battling over the West Virginia House seat won by Republican Shelley Moore Capito. The Senate record was set in North Carolina, where the parties poured another \$21 million into the seat won by Elizabeth Dole.

Threats to the democratic process have been beaten back in prior eras. The gluttony of the Federalists was that they never elected a president after John Adams. The Gilded Age was followed by such populist reforms as income and estate taxes, popular election of senators, women's suffrage, campaign finance disclosure laws, the initiative and the referendum. But can democracy survive the current wave of cashbox politics?

Phillips is not at all sanguine about this. In his view, our democracy is evolving into a plutocracy – government by the rich. He quotes Bill Bradley, the unsuccessful Democratic presidential candidate, as saying in 1996 that “Money not only determines who is elected, it determines who runs for office. Ultimately, it determines what government accomplishes – or fails to accomplish. Congress, except in unusual moments, will listen to the 900,000 Americans who give \$200 or more to their [*sic*] campaigns ahead of the 259,600,000 who don't.”³⁶ Or, as the muckraker Upton Sinclair more famously said, “It is difficult to get a man to understand something when his salary depends on his not understanding it.”³⁷ Nowhere is the power of money more evident than in the Congressional support for estate tax repeal. Our elected representatives are presenting the issue of repeal as a populist issue. For example, when estate tax repeal failed in the Senate last June, President Bush denounced the vote as a “disappointment to the American people.”³⁸

The President's remark is a striking example of the pervasive hypocrisy of our political system. Elimination of the estate tax in the face of growing budget deficits serves only the interests of the wealthy. It means making the rich richer even as we slash essential public services for the middle class and the poor. This is not populism, but an example of how wealth relies on government for its protection.

But how did sheltering the wealthiest one-hundredth of our population become clothed in the guise of *populism*? I vainly sought an explanation until Frank Powell suggested to me that I examine Malcolm Gladwell's recent book,

³⁵ Critics say the law does not adequately plug “soft money” contributions to state political committees that can then be siphoned to federal campaigns.

³⁶ Quoted in Phillips, *op. cit.*, p. 405.

³⁷ Quoted in Ivins, “Another Corporate Scandal Afoot,” *The San Francisco Chronicle*, September 1, 2002.

³⁸ Hulse, “Effort to Repeal Estate Tax Ends in Senate Defeat,” *The New York Times*, June 13, 2002.

*The Tipping Point.*³⁹ *The Tipping Point* is an inquiry into the epidemiology of ideas. How is it that an idea becomes popular? How, for example, did Mayor Rudy Giuliani reverse the epidemic of street crime in New York City? How did Hush Puppies regain their popularity at the very moment when their manufacturer was about to close its doors?

Gladwell likens crime waves, fashion trends and other examples of public acceptance of ideas to epidemics. Each is a form of contagious behavior that arises from relatively small things. Consider that a yawn begets yawns by those observing the first yawn. For Gladwell, the “tipping point” is that one moment when an idea becomes epidemic.

The tipping point is reached when three factors interact. The first of these is what Gladwell calls the “Law of the Few:” that is, social epidemics arise from the efforts of a handful of exceptional people. A classic example is the so-called Patient Zero of the AIDS epidemic. Patient Zero was a charismatic French-Canadian airline attendant who boasted of 2,500 sexual encounters. He has been tied to 40 of the earliest cases of AIDS in New York and California. Through his social connections, energy, enthusiasm and personality, one man made an epidemic. The second prerequisite to social epidemics is what Gladwell calls the “Stickiness Factor.” This rule says that how information is packaged has an enormous impact on the power of that message. If it has stickiness, you can’t get it out of your head. We all remember “Winston tastes good like a cigarette should.” That line made Winston the best selling American cigarette. Another enduring part of the American lexicon is the tag line of Wendy’s hamburger chain, “Where’s the beef?” The third prerequisite to a social epidemic is what Gladwell calls the “Power of Context.” In other words, people react to their environment. An illustration is the 1964 murder of Kitty Genovese. In the city of Queens, Genovese was stabbed by her assailant three times over a period of half an hour. Although 38 people saw the attacks, none intervened or called the police because they all thought someone else would help. Researchers studying the Genovese case later found that the fewer the number of onlookers to a crime, the more likely it is that somebody will help. Such is the power of context.

The Law of the Few, the Stickiness Factor and the Power of Context all factor into how the cause of estate tax repeal evolved into *faux* populism. We have very few elected federal representatives. There are a president, a vice president, 100 Senators and 435 members of the House of Representatives. Most of these worthies are charismatic, energetic, forcible, social and peripatetic. Despite our abiding cynicism, we want to believe what they tell us. Most of them tell us the estate tax is bad. Their chorus is powerful. The Law of the Few is in full force.

³⁹ Little, Brown and Company (2000).

How did the Few cultivate the Stickiness Factor? In the latter 20th century, successive presidents have roundly criticized federal tax policy. Jimmy Carter condemned the income tax as a “disgrace to the human race.” Ronald Reagan called it theft by government. We all remember the elder George Bush saying “Read my lips: *no new taxes.*”⁴⁰ We also remember what happened to him when Congressional Democrats inveigled him into raising taxes. In the 1996 presidential campaign, Senator Robert Dole made abolition of the Internal Revenue Service a major campaign issue. Dole lost, but Senator William Roth was there to carry on. In 1997, Roth chaired hearings by the Senate Finance Committee exposing alleged abuses by the IRS in administering the tax laws. That the IRS has fearsome power was easy for people to understand: after all, the IRS put Al Capone behind bars. Nobody mentioned that Congress created the rules under which IRS operated, or that in prior years Congress had routinely flogged the IRS for being lax in tax collection. (In fact, nobody mentioned that the secret witnesses who appeared before the Roth Committee in 1997 were in time almost completely discredited.)⁴¹ The stage was set. Legislators began referring to the tax laws as the “IRS Code.” This was the height of hypocrisy. It is the legislators who enacted the tax laws, not the IRS. Most effectively of all, legislators began referring to the estate tax as the “death tax.” This implies an enormous insult, that after a lifetime of paying federal, state and local taxes, one must also pay for the privilege of dying.

The third factor of *The Tipping Point* is the Power of Context, the profound influence of our environment. There are several environmental factors at play here. Nobody likes paying taxes. Many (especially those who don’t travel) find government wasteful, inefficient, and overbearing. Government’s interference in their lives would diminish with tax reductions. The most important context was timing. The 1990’s produced federal budget surpluses. Some predicted that these surpluses would rise to astronomical proportions. The 1990’s also produced a technology bubble from which millions briefly profited. Many of the *nouveau riche* no doubt pictured themselves newly subject to the estate tax. Minnesota Senator Paul Wellstone was a vigorous opponent of estate tax repeal. When he was killed just before the last election, many voters were ironically receiving in the mail a flier bearing the picture of a tombstone. Under the tombstone, the flier read in part, “Paul Wellstone not only wants to tax you and your business to death . . . he wants to tax you in the hereafter.”⁴² The message worked. Wellstone’s opponent was elected. Propaganda like that of the anti-Wellstone flier readily makes millions of Americans think, wrongly, that the estate tax applies to them.

⁴⁰ Quotes are from Yablon, “As Certain as Death: Quotations about Taxes,” *Tax Notes*, April 15, 2002.

⁴¹ The tide has now turned, and Congress is asking the IRS why it isn’t leaning harder on tax cheats. “Tax Analysts’ Executive Director Addresses IRS’s Split Personality,” *Tax Notes*, May 20, 2002.

⁴² Krugman, “For the People,” *The New York Times*, October 29, 2002.

And there you have it. The few have employed a sticky message in the right context to package the preservation of great wealth as populism. Such use of dissemblance is not without precedent. There are ample illustrations in our history. This instance, however, is so extraordinary that it set me to wondering. We now have two generations who have grown up getting their information from television, which dispenses knowledge in sound bites. This generation doesn't read. As a tax lawyer, I worry that if this public is so gullible as to accept estate tax repeal, the Republic may have much worse in store. What could that be?

The sum of all my fears is embodied in George Orwell's terrifying novel, *Nineteen Eighty-Four*.⁴³ Orwell envisioned a totalitarian state called Oceana, where government controls the masses by spreading propaganda, cracking down on unorthodox thought and altering history to suit its needs. America is a long ways from becoming a totalitarian state, and God willing that will always be. But America's increasing resemblance to Oceana makes me uneasy.

The Oceana of *Nineteen Eighty-Four* is perpetually at war against a vague and ever-changing enemy. Citizens know nothing about the war except what government tells them, but the war serves as a powerful vehicle to fuel hatred, nurture fear and unify the populace behind the regime's autocratic practices.

America's war on terrorism has become almost as amorphous. The President tells us that his resolve is steely and his mission is clear. It is just not clear who the enemy is. What began as a war against Osama bin Laden and al Qaeda became a war against Afghanistan. In Afghanistan we neither found bin Laden nor liquidated al Qaeda. There were then fulminations about an "Axis of Evil," the targeting of terrorists in many countries, and, as I speak, preparations for a war against Iraq. Saddam Hussein, not Osama bin Laden (with whom Hussein has no known connection) is now the poster boy for evil incarnate. Exactly what will constitute success in this war has never been defined. We know only that the war will continue indefinitely, and that the approval ratings of George W. Bush have since September 11 risen from 33% to 75%.

In Oceana, Big Brother keeps constant tabs on the populace, using two-way telescreens to monitor everyone while simultaneously broadcasting party propaganda.

Two-way telescreens are just over America's horizon, but video surveillance is already ubiquitous. Cameras gaze at us everywhere from offices to airports. A mysterious computer program called "Carnivore" monitors Internet traffic around the world. Thanks to the hastily passed USA Patriot Act that Judy Soley reviewed for us last month, the state has sweeping new powers to monitor business

⁴³ The following discussion is based on Kurtzman, "Learning to Love Big Brother: George W. Bush Channels George Orwell," *The San Francisco Chronicle*, July 28, 2002.

transactions, library reading records and even confidential attorney-client communications. It need no longer be burdened with such inconveniences as probable cause where national security is deemed to be at issue. Best of all, the 484-page Homeland Security Act that President Bush will sign this week will include a \$200 million appropriation to the Defense Department to create the largest data surveillance system ever built. This project will link government and commercial computer databanks so that the state will know everything about you. It will be run by the Total Information Office, the head of which is Vice Admiral John Poindexter. You remember Poindexter. He was convicted in 1990 on five felony counts of lying to Congress in his capacity as national security adviser to President Reagan. Think if it. A master prevaricator heads the Total Information Office.⁴⁴

In *Nineteen Eighty-Four*, Big Brother's minions spread lies and rewrite history to suit his goals. In the Bush White House, presidential transcripts are routinely sanitized to remove the President's malaprops. The facts surrounding Bush's financial dealings at Harkin Energy have been revised repeatedly. The White House's position on the estate tax is misinformation. Nevertheless, Senator Charles Grassley last month likened to Adolf Hitler those who differ with the Administration's position on estate tax repeal.⁴⁵

What would it take to turn these United States into the kind of society that Orwell warned about, one that envisions war as peace, freedom as slavery and ignorance as strength? Would it happen overnight, or would it involve a gradual erosion of freedoms with the people's consent? Does it begin when protecting the privileged passes for populism?

Because we are a nation at war -- as we are constantly reminded -- we appear willing to sacrifice many of our freedoms in return for the promise of greater security. We have been asked to put our blind faith in the Bush administration, and by this month's elections most of us appear to have done so. But when our leaders abuse that trust by straying so far from the truth-telling that is the bulwark of democratic society, can there be any turning back? If as a tax lawyer I know our leaders' estate tax rhetoric is false, then what *can* I believe?

⁴⁴ Safire, "You are a Suspect," *The New York Times*, November 14, 2002.

⁴⁵ Krugman, "Springtime for Hitler," *The New York Times*, October 22, 2002. GOP Senator Phil Gramm had early condemned those who would block tax-motivated asset expatriation by individuals as "passing laws that sound like they're right out of Nazi Germany" even though doing so would fund income tax relief for members of the armed forces. Hamilton, "Grassley Defends Mark-to-Market Tax on Individual Expatriates," *Tax Notes*, September 9, 2002.