Is inheritance of wealth good for our society?

Quest for Knowledge Essay *Rob Maher* *Presented November 15, 2023*

Queen Elizabeth II passed away on September 8, 2022. The late Queen had been princess and heir presumptive to the throne of the constitutional monarchy of the United Kingdom from when her father became King George VI in 1936, and upon her father's death in 1953, she ascended to the throne as Queen Elizabeth II according to the rules of the monarchy. Similarly, the Queen's eldest son, Prince Charles, became King Charles III upon his mother's death.

Americans often tend to scoff at the idea of someone becoming a monarch simply by heredity. We wonder "why should someone get the 'royal treatment' simply because of who their parents were?" And "why would a modern country still have 'royal treatment' anyway??" The concept seems to offend the American legend of individual accomplishment and rags-to-riches opportunity.

The storyline of American success is the meritocracy of being *self-made* and extolling the virtues of *pulling yourself up by your bootstraps*. While some Americans may feel romantic about the enchanted lives of modern-day princes and princesses, there is also a question about the justification that certain family lines are afforded a position of luxury just because of who the genetic father and/or mother may be, not because of a selection process based upon merit. What positive purpose does hereditary monarchy serve in contemporary societies?

In this paper, I would like to consider the validity of the American sense that we did away with hereditary lines of succession when *We The People* ratified our Constitution and the Bill of Rights. <u>Specifically, I would like to examine the American practice of inheritance of property and inheritance of prerogatives based upon one's family line, not upon individual merit of some kind, as a lingering vestige</u>

of the hereditary systems, like the British monarchy, that we claim to have left behind. My observations are spurred by recent reports about the increasing disparity of wealth among American families, and particularly the reports about the upward concentration of wealth by the richest Americans.

For this paper, I ask you to perform a thought experiment with me in which we imagine a fictional social tradition in which the concept of wealth inheritance along hereditary lines is NOT assumed. Without this assumption, one might ask what sort of alternative traditions for distributing accumulated wealth could be conceivable? For example, we might try to imagine a social tradition in which the monetary wealth of the decedent passes into control of, perhaps, a lawful receiver, whose role it is to liquidate all of the assets for broad benefit of the community, such as using an auction, lottery, financial formula (e.g., dividend to all citizens), or some other method of transfer—and presumably skim some funds as taxation to support the local, state, and federal governments. I will look at some of the advantages and disadvantages to society by changing our tradition of hereditary inheritance in comparison to our current system of wealth inheritance.

Social hierarchies

The social and economic organization of modern societies includes various hierarchical constructs. In the United States, for example, we have social structures surrounding certain religions that tend to direct members to socialize, marry, and seek educational opportunities primarily with others sharing the same religious practices. We also have nebulous groups colloquially known as White Collar and Blue Collar based on occupation. In other world societies we find hierarchical constructs that reflect more significant differences in lifestyle and prospects, such as the caste system in India that derives in some manner from Hindu religious and social life. Members of the various formal and informal castes traditionally live in different communities and do not interact in the same social and educational realms.

These social hierarchies are very closely tied to family heredity. The offspring of families belonging to a particular element of the social hierarchy tend to adhere to the same customs and traditions of that social strata. In the case of social hierarchies based upon family wealth, a similar adherence to customs and traditions associated with high net wealth tends to occur. The American story of rewarding individual initiative, merit, and *earned* wealth tends to be at odds with the traditions of inherited social hierarchies.

Wealth

Many descriptions of the American social system refer to Upper Class, Middle Class, and Lower Class, which are categories determined in some manner by *personal wealth*. This leads to an important question for this paper, which is how to define "wealth"? For the purposes of this paper, I will define two attributes of wealth: *monetary wealth* and *social wealth*.

The first attribute, monetary wealth, is based upon the total net market value of an individual's physical and intangible assets. Typical examples of monetary wealth include stocks and bonds, money in bank accounts, real property like a home, land, cars, and other physical possessions, and I would include things like private ownership of a business, which is often worth more than the value of its tangible assets. It goes without saying that an individual's monetary wealth is determined after subtracting any liabilities for money owed and so forth.

The second attribute, social wealth, is not something that I believe is a commonly agreed upon attribute, but I will use it in this paper to refer to the special prerogatives associated with levels of social status and recognition, such as coming from a "good family," owning land, having a good credit score, being inducted as a member of an exclusive club, serving honorably in an exclusive branch of the military special forces, or having a degree from an Ivy-League school like Harvard or Yale. I should note that social wealth also can be negative, such as coming from a historically underrepresented or underprivileged group subject to discrimination (race, ethnicity, gender, sexual preference, etc.).

In considering wealth, it is essential to separate consideration of *income* from consideration of *wealth*. Most discussions of economic disparity use statistics about annual income, and certainly we would expect those with higher annual income to be able to accrue greater wealth over time. Describing someone as being *rich* would include income, but our notion of being rich really encompasses the concept of monetary wealth, whether or not the monetary wealth produces annual income to the owner (i.e., unrealized capital gains do not show up as income in the annual statistics, but definitely represent wealth using our definition.)

Inheritance of Monetary Wealth

The concept of passing wealth from one generation to another is so firmly established in most human societies that the framework of wealth inheritance is assumed as a given. Civil jurisdictions provide rules for the manner in which inheritance of monetary wealth takes place, and even many formal religious sects have rules and customs governing the process.

One can imagine early civilizations in which individuals started to possess durable items of value, like clothing, tools, and cookware. At the time of death, some tradition for how to pass along these items to others had to evolve, and it seems reasonable that those closest to the deceased would gather up those belongings. As the trappings of wealth eventually included possession of land, agricultural animals, slaves, boats, ships, etc., the rituals of inheritance steadily became part of common law.

Judeo-Christian teaching from the Bible include the importance of ensuring family lines from generation to generation, and praise of virtues like "The good leave an inheritance to their children's children" (Proverbs 13:22). Jewish traditions are that inheritance comes from the father to the male descendants (patrimonial estate), with the firstborn son receiving twice the inheritance than the other sons (Deuteronomy 21:15-17). Similar traditions and rules presumably exist in all societies. Because these traditions have been established and maintained down through history, it can be argued that the normal processes of social evolution must have sifted and winnowed the options for inheritance so that current practices are optimized or are at least sustainable in some sense.

So, is the current practice of inheritance in the United States "good" for our society and social order? We know that not every traditional practice of human social activity remains acceptable today. We now forbid child labor, polygamy, enslavement, cruel punishment like crucifixion, forms of human trafficking, and so forth. We have anti-trust and consumer protection laws, require Environmental Impact Statements, and at least since 1920, we even deign to allow women to vote! We also no longer assume that the eldest male offspring is mandated as the sole or primary heir, nor do we have political leadership based upon genetic lineage. Thus, one might argue that not every well-established tradition is sustained forever, and therefore it is perhaps reasonable to reconsider from time to time our other traditions, like inheritance of wealth within a family.

Inheritance of Social Wealth

Beyond consideration of monetary wealth, the question of inheritance of intangible *social wealth* is also of interest in this paper. While financial wealth is relatively straightforward to enumerate, the precise value of social wealth is less clear, and the mechanisms of inheritance are not as easily defined in terms of laws and social policies. Social wealth is not something easily itemized in a person's will. Nonetheless, it is important to assess the "good" to society of permitting inheritance of social standing and various associated privileges. For example, there have been discussions recently about so-called *legacy* admissions to selective colleges, which have allowed the offspring of alumni preferential admissions treatment. Similarly, many universities have alumni club scholarship funds with donations from alumni to support the offspring of other alumni. Membership in social clubs, service on philanthropic boards, invitations to join business or religious organizations, and so forth, frequently come from referrals based upon family history and standing.

Is there any reason to somehow prevent inheritance of "social wealth"? There is a strong sense of allegiance to the use of letters of reference, introduction by a reputable person, granting of special privileges due to certain background information and biases. Many professionals have anecdotes about how a degree from a certain university or membership in a certain organization can move an applicant to the top of the list, just like anecdotes about how other attributes may move other applicants to the bottom of the list. Do these social customs benefit or hurt the "good" of our society? Because this paper must be of reasonable length, I will not choose to delve into all of the intangibles to any great extent, but it is important to keep these concepts and questions in mind as we look at the pros and cons of wealth inheritance.

Some arguments for moving to a different attitude about inheritance

In preparing this paper, I have found that the most common arguments for changing our traditions of wealth inheritance are (1) the need to address problems with the concentration of wealth, (2) the insidious effects of inequality of opportunity, and (3) consideration of changes to the means and methods of taxation.

Arguments about the concentration of wealth in capitalist economic systems have been going on for more than a century. Private control of capital can have the effect of giving more market power and control to those with more wealth, creating positive-feedback loops for gaining even more wealth. When that wealth is held by a corporation, our society has decided that this is OK until the wealth and power becomes a monopoly that must be broken up in accordance with anti-trust laws. When the wealth is held by individuals, however, there is no legal requirement to "break up" that private wealth. Over time, the positive feedback loop of private individual wealth results in a significant disparity such that in the United States today, the top 10% of earners own nearly 70% of the total wealth, while the lowest 50% of earners only own 2.5% of the total wealth. For those concerned about social economic welfare, having the majority of Americans unable to grow their wealth significantly while those in the top echelon keep surging farther ahead is undesirable.

The role of inheritance in the accumulation of individual wealth is significant. For many individuals, inherited wealth is not immediately spent, but is instead saved and invested in some manner. As wealth generally begets more wealth, inherited wealth serves an important role in wealth concentration. While there are examples of individuals who start out poor and end up wealthy, the likelihood of this outcome is much, much lower than the likelihood that an individual born into wealth will end up dying even more wealthy.

Is wealth concentration really a concern for our society? Are those who call into question the system that boosts the success of wealthy folks more than the less wealthy simply being jealous of those who have greater means? These questions comprise the second key issue raised by opponents of wealth inheritance, which is the resulting *inequality of opportunity*. For example, is it sensible in our society that the trope of "the family farm" has so much wholesome appeal in American culture, while we point at genealogical succession in British Royalty as being anachronistic? Why should a farmer using land originally conveyed to his or her ancestors “for free” by the Homestead Act, be selected on the basis of being a descendant of a farm owner, rather than having an open market of competition for *any* individual to become a farmer based on his or her own merit? Similarly, is it of broad value to our society to have the offspring of wealthy parents be endowed with lifetime wealth based upon nothing other than being legal heirs, while potentially very meritorious individuals born into poverty are granted no such privilege? Similarly, our current system of taxation is highly favorable to *unearned* income from investments of wealth, compared to income *earned* from wages and salaries of actual jobs. Altering the tax code to favor regular workers’ income and provide less beneficial treatment of investment income could be a choice that might allow regular folks to accumulate savings.

It is argued that our society would see increased productivity and increased equity in individual wealth if we had a system that awarded opportunities for increased wealth in the manner of awarding increased employment income, namely, having individuals able to compete on the basis of their own intrinsic merit, ingenuity, and creativity and the assessed market value of those skills and talents. In other words, providing growing wealth to those who are already wealthy has less utility than providing opportunities for growing the wealth of individuals who are poor, since the poor would be more likely to use their growing wealth to buy a home or create a retirement fund, not simply investing with the goal of passing the wealth to one’s children.

Is this argument suggesting that what society should do is serve as Robin Hood: take from wealthy individuals and redistribute it to poor individuals? I don’t think so, although there may be proponents of certain economic and political systems that do indeed propose literally taking money from the rich and giving to the poor. Instead, I believe what is being suggested by thoughtful commentators is to set some reasonable expectation about what happens to accumulated wealth in terms of taxation by the government and in terms of redirecting inheritance to benefit society more broadly.

This leads to the third key issue expressed in opposition to our current practices of bequeathing wealth at the time of death, which is how best for the government to fund itself through taxation. The U.S. tax system is complicated, but generally relies upon a combination of income taxes, property taxes, and certain excise/sales taxes. Some experts encourage the development of a tax on *wealth*, rather than on *income*, as a way to address wealth disparity, thereby allowing working people to keep more of their earned income.

In fact, there was a time during and after the Gilded Age (1870 up to about 1900) that our society began to object to the growing concentration of wealth at that time, most notably by the industrialists and financiers Andrew Carnegie, John D. Rockefeller, Andrew Mellon, and others. Public pressure pressed those individuals to set up philanthropic foundations that would hold a large fraction of their individual wealth for the benefit of society, or face a very high level of taxation on bequests. Expressed simplistically, there was a sense that huge accumulations of wealth indicated that an individual had benefited greatly from the market and commerce opportunities of many, many consumers in the economy, and therefore it could be claimed that they owed the "excess" wealth back for the benefit of the larger community that had sustained the individual's accumulation.

Throughout his career, Andrew Carnegie (1835–1919) showed reprehensible ruthlessness and exhibited negative traits toward workers and competitors that I won't comment on here. But in the last decades of his life, he came to believe that allowing the rich to transfer their accumulated wealth to offspring was likely to enforce a caste system based not on merit but on the luck of birth. Writing in 1889 about the widening gap between rich and poor in America at that point in our country's history, Carnegie proposed high inheritance taxes so that the very wealthy would not become family dynasties—as had happened in Europe—but would instead convince them *to give away their wealth over the course of their lifetime* for the net benefit of society. His 1889 essay now known as "The Gospel of Wealth" includes one of his most famous quotes, "The man who dies thus rich dies disgraced."

In 1889 Carnegie wrote:

> "This, then, is held to be the duty of the man of Wealth: First, to set an example of modest, unostentatious living, shunning display or extravagance; to provide moderately for the legitimate wants of those dependent upon him; and after doing so to consider all surplus revenues which come to him simply as trust funds, which he is called upon to administer, and strictly bound as a matter of duty to administer in the manner which, in his judgment, is best calculated to produce the most beneficial result for the community--the man of wealth thus becoming the sole agent and trustee for his poorer brethren, bringing to their service his superior wisdom, experience, and ability to administer--doing for them better than they would or could do for themselves."
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> --Andrew Camegie, "Wealth," North American Review, 148, no. 391 (June 1889).

Some today do not like Carnegie's *noblesse oblige* concept, since it implies that the "superior wisdom" of privileged people grants paternalistic knowledge about what is best for the "poorer brethren," but I think our country would benefit greatly from a broader sense of philanthropy among every wealth category.

While Carnegie chose to distribute his own wealth during his lifetime, and was in favor of high inheritance taxes as a way to induce other wealthy people to do as he did, modern wealth in America has coined terms like "the death tax" to imply that the wealthy no longer have any moral or ethical obligation to support the social environment that provided their means to succeed. Meanwhile, Carnegie's legacy lives on through his many foundations including the Carnegie Foundation for the Advancement of Teaching, the TIAA retirement system for academics, Carnegie Hall, Carnegie Libraries, etc. While there are notable contemporary examples among those in the 1% category who view the OBLIGATION of philanthropy as Carnegie did, there seem to be more who express greed and entitlement for their financial success. However, it's not just the multimillionaires and billionaires: I believe our country would benefit greatly from a broader sense of philanthropy among those of us in the 10% wealth category, too.

There have been proposals to alter the taxing of inheritance and other gifts from being the obligation of the testator to instead becoming the obligation of the beneficiary. One such proposal described by Lester Thurlow (1976) would be a *cumulative lifetime-accessions tax*, which would apply steep taxation to the beneficiary for total lifetime inheritance and gifts that exceeded some amount, e.g., $2 million. Inheritance and gifts below that amount would be tax free to the recipient. This arrangement would avoid the tax-avoidance strategy of a testator breaking a large inheritance up into smaller trusts that would individually be under the estate tax limit.

Some arguments for maintaining the status quo

Among the most common reasons for our society to continue allowing each of us to designate who will inherit our wealth at the time of our death are (1) <u>freedom</u> for each of us to do as we please, (2) <u>motivation for lifetime productivity</u> because we get to keep the wealth we accumulate, and (3) <u>all the alternatives are worse</u> for society, so "better the devil we know."

While there are dozens of economic and political organization theories competing for supremacy in societies around the world, the United States has adopted the basic principles of capitalism, with the assumption that individuals have the right and the ability to receive payment in exchange for their labor, and that individuals can own and run profit-making business enterprises that manufacture goods, offer services, and engage in free commerce. This model of personal economics comes from the rights and privileges celebrated in our nation's founding documents, and a vast body of common law and legislation that has defined the nature of our economic interconnections. There are certainly established limitations on commercial activity, such as regulation of medication, product safety, antitrust laws, taxation, and so forth, but the general principle of allowing clever and industrious individuals to capitalize—literally—on their hard work is firmly established in our national laws and traditions.

The *freedom to do as we please* implies that not only are we allowed to engage in profit-making enterprises, but that we are able to use those profits in the manner of our own choosing. Buying land, investing, giving gifts and charitable donations, and all the other things we do with money. This freedom to do what we want gives a great deal of momentum for the principle that a testator should have the freedom to declare whoever he or she pleases to receive the accumulated wealth upon the individual's death. From this viewpoint, the concept of inheritance is simply the freedom to give a gift to one's family members.

Nonetheless, if our goal is to maximize overall economic freedom in our society, the problem of wealth concentration needs to be considered. For example, a counterpoint to the freedom argument is the plausible observation that for an individual in the top 1% with, say, $100 million in accumulated wealth, providing a $1 million increment in wealth gives that individual less *incremental economic freedom* than if that $1 million were given as $100,000 payments to ten low-net-worth individuals. In other words, if the goal is to maximize total economic freedom, the ten $100,000 payments result in more *opportunity freedom* when integrated over the impact on the ten relatively poor individual recipients than the opportunity freedom gained or lost by a $1M increment to a single high-net-worth individual—who we might feel already has more than they need.

The second argument for maintaining the status quo regarding inheritance is that an individual's ability to pass on accumulated wealth serves as a powerful motivator to be inventive, industrious, and productive, to save and accumulate wealth throughout a lifetime so that it can benefit loved ones long after we die. If inheritance was abolished, the argument goes, then people would no longer feel the need to work more than just enough to get by, since any excess wealth would be extracted for some other non-family benefit, and so our economy would stagnate in lost productivity. The implication of this argument is that the inheritance opportunity is a significant motivator for individuals to excel in their economic output. However, studies often show that the primary motivator for trying to accumulate wealth is to get "as far away from zero" as possible so that a comfortable lifestyle and secure retirement is attained. So, while changing the inheritance process might lead to some impact upon the various motivations for working hard, it does not seem like those who are successful competitors in the economic game would somehow give up if they could not bequeath their wealth to their children. Individuals in our society compete for economic success and the freedom it brings, without inheritance being the prime motivator.

The third argument—stating that while there may be shortcomings in the current inheritance system, no better system has yet been proposed—is not easy to support or refute, because it assumes that the collective flaws and drawbacks attributable to the current system of inheritance are acceptable so that any other scheme would necessarily have greater negative results. Often the argument is carried by identifying policies and laws that have been tried in other eras of American history, or tried in other nations over the years, and identifying numerous negative unintended consequences of those systems of inheritance. Another oft-cited observation is that many laws and policies intended to regulate inheritance have been unenforceable because of valid legal strategies exploiting loopholes that lawmakers have put into the tax codes. For example, it is very common for wealthy people in the U.S. to set up legal arrangements that pass accumulated wealth to beneficiaries via a living trust that largely avoids consideration of estate taxes.

Conclusions

After considering just a few of the main arguments for changing our system of inheritance and the counterarguments for maintaining the status quo, my ability to make a recommendation is not at all clear. Few will argue that our trends of wealth concentration are broadly good for society, but it is not clear that the problem of wealth disparity is best solved by revamping intergenerational inheritance laws. If the U.S. instituted new rules that limited significantly the inheritance of wealth, there would undoubtedly be efforts to circumvent the restrictions by transferring wealth via other means, such as a sequence of small gifts, offshore accounts, and the creation of third-party financial holding companies to launder the money. In short, it would seem that changing our system of inheritance wouldn't work anyway.

Yet somehow our society turned away from the European model of hereditary monarchy, from the ancient assumption that the eldest son would be primary heir, and we even seem to be turning away from legacy consideration in college admissions. And there once was a time that even Andrew Carnegie encouraged those of considerable wealth to distribute the funds during their lifetime for the good of the public, not for inheritance.

Public opinion would have to change, but it is not inconceivable that our social economic expectations of one another might trend toward a stronger collective sense of philanthropy and for offering greater opportunities for the economically disadvantaged class of citizens to gain a better foothold. Home ownership is often cited as a key attribute of gaining wealth in America, for example.

Since the primary motivation for many Americans is to work hard over many decades in order to create a nest egg for a comfortable retirement, it might potentially be a popular political goal to devise ways to ensure security in retirement. If this could be done, each individual's need to squirrel away funds just in case of some sort of setback would no longer be necessary, and the accumulation of excess personal wealth for the purposes of inheritance would also no longer be needed.

In conclusion, what I call upon all of us to do when we chuckle about the Royal Family and hereditary lines in Great Britain, is to contemplate the manner in which hereditary lines continue to exist even in our great and free country.

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