The Rich (Families) Are Different

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Allison Anna Tait, *The Law of High-Wealth Exceptionalism*, 71 **Ala. L. Rev.** __ (2019), available at SSRN.

In April of 2019 lawyers representing the “Kimberley Rice Kaestner 1992 Family Trust” argued a case against the North Carolina Department of Revenue before the Supreme Court of the United States. A few months later the Court unanimously ruled in favor of the trust in that case. The Court’s decision was a major victory for wealthy families; not so much for ordinary folks who pay state income taxes. You may not have heard of the *Kaestner* case. No news about it appeared in the *New York Times*. Ever. But you can and should read Allison Anna Tait’s insightful article, *The Law of High-Wealth Exceptionalism*. It’s about the *Kaestner* case. Well, it’s not really about the *Kaestner* case; actually Tait doesn’t even mention it. But her article is, at least in part, about the category of cases that the *Kaestner* case belongs to and it is about the state of affairs that brought about the case, and many others like it, and so much more.

In her article, Tait gives us a panoramic perspective—a bird’s eye view—of what she calls “the law of high-wealth exceptionalism.” The law of high-wealth exceptionalism is not any particular law, but rather a collection of favorable laws that, functionally, apply only to high-wealth families. Because, in theory, while anyone could take advantage of a scheme like that which the Kaestner family’s lawyers concocted to externalize the cost of governmental goods and services provided to Kimberley Kaestner by the State of North Carolina, in practice you really need to have a lot of wealth to do so. And as Tait points out, wealthy families “benefit not only from their material resources but also from the fact that most of the population is not familiar with the vast network of laws that govern family wealth and may even be disinterested in [legal] events that are of core concern to the family oligarchs.”

Tait’s larger point is that rich families avail themselves of what she calls “high wealth-exceptionalism,” a phenomenon that she maintains inflicts harm on those of ordinary wealth and is antithetical to democratic governing. More specifically, she shows how wealthy families organize themselves under wealth-management “tools” like family constitutions, private trust companies and private foundations, and take advantage of favorable laws governing trusts and taxation to shift financial risk and tax burdens to those without great wealth. She makes her larger point by breaking down her analysis into three categories: governance, power and privilege.

In the area of governance, high-wealth exceptionalism depends primarily on a concept called the “family constitution.” Tait explains how and why wealthy families cohere under this “widely marketed wealth-preservation tool,” as a way to protect against what is perhaps the family’s biggest fear: generational erosion of family wealth. The family constitution is designed to be the bulwark that gives the lie to the age-old aphorism “from shirtsleeves to shirtsleeves in three generations.” Tait describes how professional wealth managers help families inscribe family constitutions, and the ways in which they unify the family to the common cause of safeguarding family wealth.

Tait further identifies three “critical building blocks” to securing family wealth: private trust companies, family offices and private foundations. Private trust companies are entities that are legally sanctioned to manage family trusts but, unlike ordinary trust companies, they are “exempt from most state regulation.” In return for this light treatment by the state, these companies serve only the wealthy family, “broadly defined.” Private trust companies ensure privacy by evading state reporting requirements thereby keeping most “sensitive financial information” from being revealed to persons outside the family unit. They are also free to invest trust property in investments that might be outside the range of regulated trust companies, such as illiquid assets or stock in a private family business. While taking advantage of trust laws increasingly favorable to the wealthy, these entities also reinforce the sense that the family is a separate sovereign entity, “populated, animated and superintended by the family” itself.

The bulk of family financial management (and sometimes more personal services) is undertaken by the “family office.” The family office is the locus of general family business. Tait points out that family offices enjoy a special exemption from regulatory requirements otherwise imposed on investment advisors. Exemption from SEC registration means that investments can be made in privacy. Family offices are also exempt from compliance with rules for commercial financial institutions, which gives the family substantially more control over investment decisions. Given these and other advantages of family offices, it is no surprise that family offices are “how the super-rich invest.”

The family foundation is the third “critical building block for high-wealth families.” These entities preserve family wealth by substantially reducing the family’s exposure to the federal transfer taxes while “allowing the foundation to fund administrative activities performed by family members.” Properly managed, the private foundation can hold family wealth for generations, sheltering it from taxation while the family maintains control of that wealth. Private foundations are required to distribute only 5% of their income from investments to charity annually, and those distributions are often made to “family –controlled” donor-advised funds. Importantly, family members receive compensation for services to the foundation and can be reimbursed for expenses incurred for foundation business.

After showing us the tools high-wealth families use to preserve and increase their wealth, Tait moves on, in the section of the paper she calls “the measurement of family power, to their negative consequences to the population at-large. Here Tait explains some of the potential consequences of the preferential legal treatment received by high-wealth families. She maintains, for example, that these include increased systemic risk and exposure of the broader population to financial harms. Further, the privileges of conducting private operations free from regulations also makes the discovery of tax avoidance and evasion more difficult, increasing the tax burdens of others. Here she also looks at “the role that family constitutions and the coterie of family-wealth rules unquestioningly play in entrenching” wealth inequality. In this section she also addresses “costs to the democratic state.” The law of high-wealth exceptionalism, she concludes, “is deeply and essentially patrimonialist,” and thereby at odds with democratic functioning.

Having outlined the problems with high-wealth exceptionalism in such detail, Tait concludes by offering some prescriptive ideas to address the phenomenon and “the plutarchic society it cultivates.” These include retracting high-wealth legal privileges, reforming the transfer taxes, and reframing the rights of citizenship. Tait’s suggestions are good and deserve your attention. But the most refreshing aspect of Tait’s work in this piece consists of the light she shines on laws that far too few, even among those interested in the problems wrought by wealth inequality, give their consideration. Unfortunately, most of the rest of us “remain unaware of the many behind-the-scenes efforts to change family-wealth law, what effects those changes might have on their lives, and what the changes might mean on the larger scale, looking forward.” Tait’s article is a step towards fixing that. The *Kaestner* case, for example, mentioned at the outset of this review, was not just a boring trust tax case that concerned only the wealthy few. Instead, it was a prime example of high-wealth exceptionalism that affects us all and deserves the nation’s attention.

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