Trusts and Estates Law and the Redistribution of Wealth

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Felix B. Chang, *Asymmetries in the Generation and Transmission of Wealth*, 78 Ohio St. L. J. (forthcoming 2018).

Data show that the very rich hold an ever-increasing share of global wealth while that held by the rest diminishes proportionately. And the United States stands out among developed nations for its particularly wide wealth disparities between the rich and the poor. Compared with many nations the rich in the U.S. are generally richer while many of the rest struggle to get by. This severe wealth inequality harms productivity and the broader economy and even threatens democracy and social stability.

Solutions focused on donative transfers of wealth by concerned legal academics often prescribe a tax and transfer system in the form of a robust gift and estate tax regime. But political realities continue to intervene, weakening the federal transfer taxes. Given the way current political winds blow, outright repeal of these taxes seems more likely than their rejuvenation.

Against this backdrop, Felix B. Chang, in his careful and measured article *Asymmetries in the Generation and Transmission of Wealth* suggests another path. According to Chang, trusts and estates law needs a comprehensive theory on inequality. In this, he writes, T&E lags behind business law and it is time to catch up; to “unify” asymmetries in the generation and transmission of wealth.

Chang asks us to conceptualize wealth as a (mostly closed) double-sphered system. One sphere generates wealth while the other transmits it. Legal rules affect each of these spheres. Roughly speaking, wealth is not created or destroyed but is instead “shifted in response to laws.” Imperfect rules in the wealth-generation sphere will thus aggravate imperfections in the system as a whole unless corrections are made elsewhere. So when laws in the wealth-generation sphere contribute to wealth disparities, and laws in the distribution sphere fail to mitigate those disparities, concentration of wealth continues. In Wang’s example, “a singular devotion to shareholder primacy [in business law] spurs income inequality, which in turn compounds wealth inequality when the estate tax” fails to redistribute this wealth. (P. 4.) Thus laws affecting the two spheres must be integrated to achieve our goals.

And what are those goals? Chang chooses a welfare economics approach based on an individual welfare analysis, “with priority given to wealth equality.” (P. 20.) Simply stated, laws that transfer wealth from the rich to the poor are favored, because “the poor (who begin with little wealth) value slight increases in wealth more than the wealthy (who begin with vast wealth).” (P. 21.) Further, using the Kaldor-Hicks efficiency model, a system that distributes wealth more equally is better than one that does not.

Chang poses and answers three “central questions” for trusts and estates law. First, what role does it play in “sustaining inequality?” Measured against his standard (transfer of wealth from rich to poor) he concludes that these laws are weak. The transfer taxes are anemic and laws enabling concentration of wealth (here he cites dynasty trusts) are strong. Second, who benefits? The rich, their financial institutions and advisers (including lawyers), as opposed to everyone else. Finally, what can be done inside the trusts and estates law context? Here we must confront the field’s overarching policy of freedom of disposition and “reorient the field around an equally pressing imperative: redistribution.” (P. 20.)

He divides the trusts and estates rules he analyzes into two categories. These are private rules that interact with the tax and transfer system (here he cites only the Rule Against Perpetuities ("RAP")), and purely private rules. Purely private rules include those enabling spendthrift and asset protection trusts, fiduciary rules, and rules primarily affecting beneficiaries, such as abatement and ademption. He points out that the RAP, coupled with the generation-skipping transfer tax ("GST"), ensures that transfers to a grandchild's generation are taxed. He concedes that the GST has been weakened by increased exclusion amounts, but insists that the RAP "should occupy a central role" in redistribution, despite admitting that many RAP-focused proposals may be "politically infeasible."

Spendthrift and asset protection trusts pit settlors and beneficiaries against creditors. Tinkering with their rules might help transfer assets from the former to the latter, and would result in more equal wealth distribution if creditors are the less well-off. Chang looks at the creditor exceptions and suggests that they might be expanded, depending on whether empirical research would indicate that this would result in more equal distribution of wealth. He is similarly cautious in his suggestions for other rules, including fiduciary duties, abatement, ademption, *cy pres*, and execution formalities.

But what I found refreshing about Chang's ideas were not so much his specific proposals for rule changes but rather his willingness to confront the normative principle of testamentary freedom by offering a limiting welfare alternative. Testamentary freedom is a fairness principle which Chang concedes should not be disregarded but rather should be balanced against welfare, or "aggregate well-being." The "perils of inequality," according to Chang, are proper justification.

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