

# **Taxing old Money: Considerations in Crafting a Rignano Tax**

**MIRANDA PERRY FLEISCHER**  
*University of San Diego School of Law*

## **Abstract**

This Article explores whether it is possible to tax “old money” differently than “new money”. In *The Inheritance of Wealth*, Daniel Halliday proposes that we tax wealth more heavily the second time it is transferred than the first, and even more heavily the third time. He envisions something like the following: Grandfather builds a business from the ground up and bequeaths \$10,000,000 to Mother. No tax is imposed, but if Mother does not create any wealth of her own and simply retransfers \$10,000,000 to Daughter, all of Mother’s estate is taxed. In contrast, if Mother creates new wealth, different portions of her estate are treated differently. The inherited \$10,000,000 that Mother re-transfers is taxed, while any newly-earned wealth is not. Although Halliday offers a few broad structural suggestions, he does not detail how such a tax—referred to as a Rignano tax—would work. This Article explores what implementing a Rignano tax requires. Crafting one is complex but feasible, and requires six key design decisions. Drawing on experience with existing transfer taxes and Halliday’s ethical premises, this Article offers specific recommendations for each.

**Keywords:** Wealth Taxation, Tax Policy, Equal Opportunity, Gifts, Bequests, Inheritance Law.

## 1. INTRODUCTION

Should we tax “old money” differently than “new money”? Could we, if we wanted to? In *The Inheritance of Wealth*, Daniel Halliday (2018) proposes that we tax wealth more heavily the second time it is transferred than the first, and even more heavily the third time. Socialist philosopher Eugenio Rignano (1924) and the libertarian Robert Nozick (1989) have proposed similar structures. Writing from three distinct perspectives, these theorists envision something like the following. Grandfather builds a business from the ground up and bequeaths \$10,000,000 to Mother. No tax is imposed, but if Mother does not create any wealth of her own and simply retransfers \$10,000,000 to Daughter, all of Mother’s estate is taxed. In contrast, if Mother creates new wealth, different portions of her estate are treated differently. The inherited \$10,000,000 that Mother re-transfers is taxed, while any newly-earned wealth is not. Proponents of a Rignano tax, as Halliday (2018: 59) deems this structure, argue that it balances the benefits of taxing wealth transfers with concerns that such taxes discourage wealth creation.

Not surprisingly – given their role as philosophers – these theorists do not detail how such a tax would work, although Halliday offers a few broad suggestions. This Article explores what implementing a Rignano tax requires. Crafting one is complex but technically feasible, and requires six key design decisions. Drawing on experience with existing transfer taxes in the United States and Halliday’s ethical premises, this Article offers specific recommendations for each. Highlights include:

- *Base*: Imposing a tax on gifts and bequests received by an individual when she is of the second generation in her family to inherit wealth;
- *Rate*: Levying a rate of 0% on first-generation transfers and a rate in the 40-50% range on other transfers;
- *Valuation*: Using the risk-free rate of return to determine what portion of a gift or bequest is second-generation wealth;
- *Frequency*: Taxing generation-skipping transfers;
- *Tracing*: Using a first-in-time approach to allocate second-generation wealth; and
- *Transition Rules*: Treating one-sixth to one-third of existing wealth as inherited.

This Article proceeds as follows. Part II briefly recounts Halliday’s argument for taxing successive wealth transfers progressively. Part III identifies the key design considerations that would shape a Rignano tax as a technical matter, and provides specific recommendations for each. Part IV concludes by briefly identifying some considerations relevant to its political feasibility.

## 2. THE CASE FOR A RIGNANO TAX

Why tax wealth differentially according to its age? Halliday (2018: 4) starts from a familiar luck egalitarian premise – that it is unjust for life prospects to depend on the chance circumstances of birth. Most theorists then argue that gifts and bequests give

## Taxing Old Money

recipients an unfair advantage, and that taxing such transfers furthers equality of opportunity by limiting the head start of those born into wealthy families (see Alstott 2007).

Halliday proceeds slightly differently. Instead of focusing on the brute luck of receiving an inheritance, he focuses on the brute luck of being born into a family that has longstanding wealth and its accompanying social and cultural capital (which I term “wealth norms”). Consider Grandfather, who starts with nothing, builds a successful business, and bequeaths his wealth to Mother. Halliday argues that this bequest confers little or no head start on Mother, whose life prospects were largely shaped while Grandfather was still building his fortune, for two reasons. First, Grandfather’s wealth did not yet exist to pay for expensive schooling or give Mother an advantage when starting her own career. Second, the fact that Grandfather is self-made suggests that Mother did not grow up in a family with wealth norms. Grandfather likely belonged to a bowling league, not the country club, and did not pass along the contacts and cultural norms of families with long-standing wealth.

The story changes, according to Halliday (2018: 7), once we get to Mother and Daughter. “Parental advantage compounds over generations”, he writes. “Families that have been wealthy for a long time possess a greater range of powers that keep their children privileged”. Grandfather’s bequest to Mother does two things. First, it enables Mother to pay for advantages for Daughter, such as private schools, tutors, and expensive camps. Second, it signals that Daughter grows up in a family with wealth norms. By now, the family belongs to a country club and golfs instead of bowls. Mother knows people who can give Daughter an internship, and Daughter knows how to dress for the interview.

Halliday (2018: 101) sees the transmission of wealth across three generations as a contributor to economic segregation, which occurs when “certain groups are able to monopolize superior life prospects for their members, thanks to their ability to retain wealth over time”. Focusing on the brute luck of being born into a group with nonfinancial capital, instead of on the brute luck of receiving an inheritance, enables Halliday (2018: 111) to differentiate among inheritances. In his view, small, first-generation inheritances are not only non-problematic, but may even reduce economic segregation by acting as a “safety net” that keeps the middle class afloat (Halliday 2018: 1-2). By maintaining a healthy middle class, some inheritances reduce the gap between the group with wealth norms and those without.

Although enticing, this argument is not impermeable. Because others will likely critique these holes in detail, I simply note a few. First is the assumption that Grandfather’s wealth creates few advantages for Mother. It is quite plausible that Grandfather adopted “old money” norms while he was still alive and Mother was still young. The second is an inconsistency in Halliday’s assumptions. He assumes that Mother inherits toward the middle or later third of her life, after which her life prospects have been largely set. But if so, Mother likely inherits too late to benefit Daughter greatly. If Grandfather dies at 90, Daughter could be as old as 40. She has already attended college and assimilated into the class norms of her youth. Mother may be able to help Daughter buy a house or start a business, but much of Daughter’s path is set by this point.

Lastly, Halliday's proposal illustrates two difficulties in distinguishing earned and unearned wealth. Most importantly, it overlooks that creating wealth is easier when you start with it. Turning \$10,000,000 into \$20,000,000 is much easier than turning \$1 into \$10,000,000. It may also overstate how much of Grandfather's wealth is due to Grandfather and understate how much is due to Grandfather being lucky enough to be in the right place at the right time. To be fair to Halliday, however, he is not attempting to tax luck as such but rather the luck of being born into a family with wealth norms.

### 3. THE BUILDING BLOCKS

Although Halliday's goal is to justify a Rignano tax, not to design one, he offers a few rough suggestions. The tax that he envisions would apply only to bequests and would focus on receipts by a donee instead of transfers by a donor. Halliday endorses an unspecified per donee exemption level, and rejects Rignano's suggestion that third-generation transfers be taxed at a rate of 100%. He does not specify, however, what rates should apply to second- and third-generation transfers and whether first-generation transfers should be totally exempted. Lastly, Halliday asks whether the age of the recipient and the time between transfers should matter.

Implementing this structure might sound simple to those unfamiliar with tax policy. Yet the devil is in the details. Implementing a Rignano tax requires resolving six design decisions, explored below: (1) the base; (2) rates; (3) valuation; (4) frequency; (5) tracing; and (6) transition rules. Although a Rignano tax is possible, it involves enormous complexity.

#### 3.1. *The Base*

Halliday's main argument – that the tax apply to bequests received by individuals whose parents or grandparents also inherited wealth – is really a question about the proper base. This section addresses three base-related decisions: Should the tax treat gifts and bequests equally? Should it measure transfers or receipts? And should it contain any exclusions or exemptions?

##### 3.1.1. *Gifts*

An initial decision is whether the tax should apply only to bequests or also gifts. Rignano (1924: 35) clearly suggests treating the two alike. Halliday (2018: 188-94) is more equivocal, but appears to favor excluding gifts on administrative grounds. This equivocation is misplaced; a Rignano tax should apply to both. As Halliday notes, gifts are often received earlier in life. They create advantages for recipient families sooner rather than later, likely magnifying economic segregation more than bequests of comparable size (Halliday 2018: 189). Moreover, their existence may signal that givers feel financially secure enough to part with wealth before death. This increases the likelihood that heirs have grown up in a family with wealth norms.

Even so, Halliday seems untroubled by gifts. He first argues that donors have strong preferences for bequests, such that taxing only bequests would not generate a

## Taxing Old Money

shift toward gifts (2018: 191-92). As evidence, Halliday notes that many donors do not take full advantage of opportunities under current U.S. law to make tax-free gifts, and that many save beyond what is necessary to cover the expenses of old age. Yet as Halliday acknowledges, this data reflects decisions in an era of low transfer tax rates and likely underestimates the behavioral responses of wealthier families. Any estate planner will tell you that obtaining the numerous tax advantages of lifetime gifts is a key part of high net-worth estate planning. Indeed, much complexity in the U.S. transfer tax system stems from minimizing the ability of donors to characterize bequest-like transfers as gifts. The fact that donors do not maximize opportunities to make tax-advantaged gifts does not mean that donors ignore those advantages wholesale. Even if donors consider tax minimization alongside other factors when determining the timing of wealth transfers, excluding gifts from taxation altogether will almost certainly exacerbate this shift to gifts by the wealthy (Kopczuk 2013: 366-68). If Halliday's concern is transfers that create and maintain economic segregation, excluding gifts is counter-productive.<sup>1</sup>

Halliday (2018: 194) also implies that it is pointless to try taxing gifts. He correctly notes that bequests are documented in the probate process and hard to hide. At least in the United States, however, this is true only for transfers that pass via the decedent's will. In contrast, assets that pass via trusts or by other non-probate transfers are not documented in court as part of the probate process. Although he acknowledges that some gifts – such as real estate – will be hard to conceal, he overstates the ease of concealing other gifts. Banks track large cash transfers. Stock transfers are recorded. Even transfers of family jewelry generate records when recipients insure them in their own names. Halliday thus overstates the existence of records for bequests and understates the existence of records for gifts. To be sure, under-the-table gift giving does and will occur. But not to the extent that it renders attempting to tax gifts pointless. For the rest of this Article, references to “bequests” or “inheritances” refer to gifts and vice versa.

### *3.1.2. Transfers or Receipts?*

A second base-related decision is whether to tax receipts or transfers. An estate tax focuses on the total wealth transferred by a donor and generally does not differentiate among recipients (Fleischer 2016: 920). An accessions tax taxes an individual cumulatively on the gifts and bequests she receives over her lifetime; an inheritance tax is similar but imposed annually (Fleischer 2016: 921). Gifts and bequests could also be included in income. Although income inclusion and inheritance and accessions taxes represent distinct approaches, they are often confused. Halliday, for example, conflates inheritance taxes with the practice of including them in income (likely because Batchelder's “Comprehensive Inheritance Tax” (Batchelder 2009) includes gifts and bequests in income while imposing a surtax on them). An accessions

---

<sup>1</sup> A similar concern is the impact that exempting gifts from transfer taxation would have on the income tax base. Without a transfer tax on gifts, individuals would almost certainly gift income-producing property to family members in lower income tax brackets to minimize income taxes. In fact, during the planned phase-out of the U.S estate tax in 2010, the gift tax was retained for precisely this reason.

tax on an individual's cumulative receipt of gratuitous transfers with two key modifications is the best solution.

As Halliday (2018: 197) suggests, focusing on *receipts* by individuals whose families have previously inherited wealth reflects his normative concerns better than focusing on *transfers* made by individuals who have previously inherited.<sup>2</sup> Compare the following scenarios in which Grandfather starts from scratch, earns \$10,000,000, and leaves it to Mother: In *Childless*, Mother has no children and leaves her wealth to Friend's child. Friend neither inherits from Friend's parents nor bequeaths any wealth to Friend's child. In *Helping Hand Family*, Mother has a daughter, to whom she leaves her wealth. In one sense, both Friend's child and Daughter have inherited second-generation wealth; in each case, Mother inherited wealth and re-transmitted it.

But Halliday's concern is that Mother's inheritance either creates or signals economic segregation. In that sense, what Friend's child inherits is not second-generation wealth, since he is the first *in Friend's family* to inherit.<sup>3</sup> In contrast, Daughter is a member of the second generation *of Mother's family* to inherit. This is true even if Daughter inherits from someone other than Mother (unlikely as that may be). Daughter still grows up in a family containing inherited wealth and wealth norms, and then inherits her own wealth. Daughter is in the same position as if Mother had bequeathed her \$10,000,000. Regardless of source, the first \$10,000,000 inherited by Daughter should be considered second-generation wealth. Focusing on her receipts—instead of Mother's transfers—more accurately reflects this concern.

What is tricky is that we don't know exactly how much Mother will inherit – which affects the accession tax imposed on Daughter – until Grandfather is dead. Mother might gift wealth to Daughter before Grandfather transfers wealth to her. What if Mother gifts Daughter \$1,000,000 and five years later, receives \$10,000,000 from Grandfather? Looking solely at the first transfer makes it appear to be newly created wealth that should enjoy the lower rate. But this does not reflect Halliday's concern, which is that Mother's inheritance suggests that wealth transfers to Daughter be taxed. Whether Mother inherits before or after the gift to Daughter seems irrelevant if successive inheritances is a class marker.

An accessions tax on recipients modified to account for prior intra-family transfers by those individuals addresses this possibility. When Daughter receives \$1,000,000, the accessions tax applied to her would treat it as first-generation wealth because at that point, Mother has not yet inherited anything and Daughter has made no transfers of her own. When Mother later inherits \$10,000,000, the accessions tax as applied to her would treat \$9,000,000 as first-generation wealth and any amounts previously transferred by Mother to Daughter – here \$1,000,000 – as second-generation wealth. This serves as a “catch-up tax”.

---

<sup>2</sup> As explored in Section 3.1.1., however, Halliday would likely focus only on *bequests* received while ignoring *gifts* received. As also argued in Section 3.1.1., however, the two should be treated interchangeably.

<sup>3</sup> If Mother inherited wealth, her friends likely have similar social capital. It is probable that Friend's child has grown up with wealth norms, even if Friend didn't inherit wealth. However, that is likely also true of the offspring of initial earners, and they don't seem to be Halliday's concern.

## Taxing Old Money

If Mother consumes the \$10,000,000 she inherits and makes no further transfers to Daughter, then \$11,000,000 has been transferred. Of this, \$10,000,000 is treated as first-generation and \$1,000,000 as second-generation wealth. (Note that this possibility is what necessitates an accessions tax instead of an estate tax on transferors. If Mother consumes all \$10,000,000 that she inherits, then she makes no transfers subsequent to her initial gift to Daughter to which the catch-up tax could apply.) If Mother re-transfers the \$10,000,000 to Daughter, then the accessions tax as applied to Daughter should treat \$9,000,000 as second-generation wealth and \$1,000,000 as first (to reflect that \$1,000,000 of Mother's inheritance has already been treated as second-generation). This accurately reflects that \$21,000,000 has been transferred, broken down as follows: a \$10,000,000 first-generation transfer by Grandfather, a \$1,000,000 first-generation transfer by Mother, and a \$10,000,000 second-generation transfer by Mother.

Halliday suggests the tax should apply to anyone whose parents or grandparents have inherited, even if the parents are not the transferors to that individual. That makes sense, given Halliday's concerns, but raises three additional issues. The first is identifying which family members should be looked at when determining how to apply the tax to Daughter. Parents only? What about step-parents? Aunts and uncles? This Article does not resolve the issue but notes that the U.S. tax code defines family various ways for various purposes and this task is not unworkable. Second, the catch-up tax should apply to Mother only if she (or her spouse or parent) is the transferor of any out-of-order gifts to Daughter. It seems harsh to tax Mother more heavily because someone else makes a gift to Daughter, even if this leaves some amount of second-generation wealth unacknowledged. Third, the tax should incorporate anti-abuse provisions such as the reciprocal trust doctrine (see *Estate of Grace* (1969) 395 U.S. 316) to minimize taxpayers taking advantage of that and similar gaps.<sup>4</sup>

### 3.1.3. Exclusions and Exemptions

A final set of base-related decisions concerns exclusions and exemptions. First, as Rignano (1924: 102) and Halliday (2018: 65) both propose, each individual should have a (smallish) lifetime exemption amount. Assume that Grandfather bequeaths \$10,000,000 to Mother. Mother has several runs of bad luck, passing along only \$1,000,000 to Daughter. It seems plausible to allow Daughter to inherit some amount of wealth tax-free, even if Mother also inherited. As Halliday emphasizes, smallish wealth transfers often enable one generation to help the next maintain middle-class status, whereas larger transfers augment and perpetuate old money wealth norms. Moreover, such an exemption would help mitigate the out-of-order problem identified above. Halliday does not specify what that amount should be, but something like

---

<sup>4</sup> The reciprocal trust doctrine precludes two individuals from setting up mirror image trusts for each other's benefit to avoid adverse tax consequences that would follow from setting up trusts for their own benefit. Consider a rule that taxes trusts set up for one's children. Without the reciprocal trust doctrine, Anna could set up a trust for Bonnie's children and Bonnie could set up a trust for Anna's children to avoid the tax. With the reciprocal trust doctrine, however, Anna is treated as creating the trust for her children, and vice versa. The proposed catch-up tax only applies if a parent makes an out-of-order gift to a child. Without a doctrine similar to the reciprocal trust doctrine in place, Mother could make a gift to Niece and Aunt could make a gift to Daughter to avoid the tax.

\$500,000 or \$1,000,000 (which can help a family afford a house in most areas) seems plausible.

Second, current law in the U.S. provides an annual exclusion that shields gifts of \$15,000 per year per donee without using up any lifetime exemption amounts. The stated purpose is to recognize that some intra-family gift giving is normal and simplify record-keeping; these concerns counsel including an annual exemption in a Rignano-style tax. The current \$15,000 per recipient exclusion far exceeds what is necessary to shield regular birthday, holiday, wedding and graduation gifts and likely allows for much tax-free giving that exacerbates unequal opportunities (see McCaffrey 1994b). A smaller exclusion likely better reflects Halliday's concerns, although specifying its exact size is beyond this Article's scope.

A third issue concerns marital and charitable transfers. Transfers between spouses should not count, for they do not transmit wealth downward (See Rignano 1924: 102-103). If Grandfather bequeaths money to Grandmother, who spends it all and leaves nothing to Mother, nobody in Daughter's family should be treated as having inherited. Daughter is in the same position as if Grandfather spent all his money. Lastly, most – but not all – charitable transfers should be exempted. Many charitable transfers, such as a gift to a tutoring program for homeless children, further equality of opportunity along two dimensions. They both level down by removing wealth from a family and level up by improving opportunities for the least-advantaged. Yet other transfers may exacerbate inequality of opportunity, such as a contribution to a private foundation that employs family members or private school that provides few scholarships (Fleischer 2011; Fleischer 2007). A Rignano tax should therefore differentiate among charitable transfers where possible to reflect Halliday's concerns, although I shall not detail how that might work here.

### 3.2. *The Rate*

A key attribute of any tax is the rate. Although Halliday and Rignano (1924: 102-103) use an example in which first-generation transfers are exempted, second-generation transfers taxed at 50%, and third-generation transfers taxed at 100%, Halliday does not endorse this exact structure. He rejects an ultimate rate of 100%, and asks but does not answer whether a zero rate should apply to initial transfers and whether the tax should treat second- and later-generation transfers similarly to each other. This Article proposes a zero rate on first-generation inheritances and something in the range of 40-50% on subsequent ones. This recommendation is more tentative than others in this Article; although Halliday's arguments suggest that rates should rise with the age of a family's wealth, they do not point to specific rates. Nor does experience with existing transfer taxes reveal a given magic rate for inheritance taxes. More than any other design consideration, choosing a rate will likely reflect political considerations rather than technical knowledge. This contrasts with design elements such as taxing gifts or exempting marital transfers, where thinking through Halliday's concerns point us in a clear direction.

#### 3.2.1. *Initial Transfers*

## Taxing Old Money

Consider first whether the tax should completely exempt initial transfers, or simply tax them at a lower rate. Halliday's arguments could support either solution. With respect to the former, a zero rate on initial inheritances reflects several of his concerns: (1) first transfers of wealth often expand or maintain the middle classes; (2) the beneficiaries of such transfers often receive them too late in life to alter life prospects dramatically; and (3) the lack of prior transfers within a family suggests the recipient did not grow up with wealth norms.

At the same time, one could argue that taxing large first inheritances—albeit at a lower rate than subsequent transfers and while exempting small first inheritances—also reflects Halliday's misgivings about wealth norms. Consider Alice, whose father creates and transfers \$10,000,000 to her. It is quite likely that Alice's father began accumulating that wealth while Alice was growing up and that she at least partly grew up in a family with wealth norms, given the extent to which new money attempts to replicate old money norms. This is especially true when it comes to the opportunities provided to children. Although Alice's father may have grown up playing darts, it is more likely that Alice's father enrolled Alice in fencing lessons. Compare Bonnie, whose father creates and transfers to her only \$1,000,000 at his death. Although not nothing, it is more likely that this wealth simply enabled her family to maintain middle- or upper-middle-class norms and that Bonnie's upbringing was not as infused with wealth norms as Alice's.

This Article recommends imposing a zero rate on initial inheritances, although this suggestion is more tentative than others. Throughout *The Inheritance of Wealth*, Halliday focuses on the existence of successive wealth transfers within a family and on the age of a family's wealth much more than the size of a family's wealth. Although he occasionally refers to "small" or "large" inheritances, he makes little attempt to link the size of an inheritance to the creation or maintenance of wealth norms within a family. Instead, his main focus is the interaction of those norms with successive inheritances. Exempting initial transfers while taxing later ones provides a sharp, easy-to-understand distinction between stand-alone and successive wealth transfers. Given the cognitive biases that influence how individuals evaluate taxes (McCaffery 1994a), it is likely easier for the public to distinguish between not taxing first inheritances at all versus simply taxing them at a lower rate. This will most clearly convey the theoretical underpinnings of the tax to the public.

Moreover, a zero rate may better match the tax with public intuition. Although this Article is focused primarily on technical—not political—feasibility, it is not inappropriate to take politics into account when breaking a tie between two plausible design decisions. Dislike for wealth and transfer taxes is particularly stubborn. The ability to work hard and pass along what one has built feels intuitive to many Americans. Despite scholarly arguments to the contrary, many believe that such taxes punish success and constitute double taxation. (I am not endorsing such beliefs, simply acknowledging their persistence.) It is plausible, however, that the public may accept a tax that exempts newly-earned wealth and thereby explicitly acknowledges the innate drive to work hard to benefit one's children. By sharply distinguishing between newly-earned wealth and previously-inherited wealth, perhaps a Rignano tax can gain traction where traditional transfer taxes have failed. Although this may undermine the

theoretical purity of a tax designed to reflect equal opportunity goals, this may be an instance in which egalitarians should not let the perfect be the enemy of the good.

### 3.2.2. *Subsequent Transfers*

The zero rate would apply to all wealth inherited by someone who is the first generation in her family to inherit, as well as to wealth inherited by a later-generation recipient to the extent it exceeds amounts inherited by her parents. What of wealth that is inherited and re-transferred? Beyond rejecting Rignano's proposal to tax third- and later-generation transfers at 100%, Halliday (2018: 64-65) does not resolve whether the rate structure should distinguish between second and later transfers. Given the strong practical reasons against and weak theoretical reasons for doing so, the tax should not. Consider theory first. Halliday argues that the advantages of wealth compound over generations. The rate of increase, however, likely diminishes over time. Revisit Grandfather, Mother, and Daughter. Mother grows up in a family with first-generation wealth. On Halliday's account, she enjoys substantially fewer advantages than Daughter, who grows up in a family with second-generation wealth. Yet it is unlikely that Daughter has substantially fewer advantages than her children. The marginal advantage of growing up with third-generation wealth as opposed to second is likely much smaller than the marginal advantage of growing up with second- versus first-generation wealth. Although there may be such an advantage (and therefore some justification for taxing third-generation inheritances more heavily than second), the case is much weaker than for distinguishing first transfers from later ones. On a practical level, treating second and third inheritances alike minimizes the valuation, tracing, and record-keeping concerns addressed below, as well as simplifying the administrability of the catch-up tax described above. All that need be determined is how much an individual's parents inherited.

What should that rate be? Halliday's theory provides no clear answer. As an initial matter, it is not 100% clear what Halliday hopes to achieve by taxing inheritances. Does he simply aim to raise revenue from those with wealth norms to fund programs that aid the less-fortunate? If so, then the rate should maximize revenue, which depends not only on the rate itself but also on individuals' motives for making bequests and the extent to which inheritance taxes distort economic decision-making and impact savings and investment.

Or does he aim to eradicate or limit successive inheritances within families, much like Pigouvian pollution taxes are designed specifically to limit pollution? A goal of entirely eradicating the ability to inherit and re-bequeath leads to a rate of 100% on second transfers, while a goal of limiting that ability leads to an indeterminate rate less than 100%. The higher the rate, the less the same wealth will be inherited and re-transferred. Again consider a scenario in which Grandfather leaves \$10,000,000 to Mother, who in turn bequeaths the wealth to Daughter. Taxing second transfers at a rate of, say, 40% means that Mother's bequest to Daughter will trigger a \$4,000,000 tax and Daughter will only receive \$6,000,000 of Grandfather's wealth instead of \$10,000,000. Note however, that this does not guarantee Daughter will only receive \$6,000,000. It is possible that Mother wants Daughter to enjoy the same amount of inherited wealth as she herself enjoyed and, as a result, creates \$4,000,000 of her own

## Taxing Old Money

wealth so that Daughter still receives a total of \$10,000,000. Although Halliday seems less concerned with second-generation inheritances that include some amount of newly-earned wealth, it is unclear why Daughter's receipt of \$10,000,000 is less troubling to him when \$4,000,000 has been created by her Mother. In both instances, Daughter grows up in a family with wealth norms and inherits \$10,000,000.

Although theory does not provide clear answers, political feasibility suggests rates in the 40-50% range. Before 2001, the United States taxed estates at a top statutory rate of 55%. During this time, opponents of the estate tax successfully supported legislation that simultaneously increased exemption amounts and decreased top rates to the current rate of 40%. Even though average rates are lower—and would be even lower if first wealth transfers were completely exempted—the public tends to focus on top marginal rates (McCaffery 1994a: 1886-1905). It is likely that a top rate over 50% (which starts to feel confiscatory to some) would be hard to sustain, while something like the 40% currently in force in the United States would be feasible.

### *3.2.3. Adjusting for Age*

One further adjustment may be warranted. As Halliday recognizes, wealth transfers received early in one's life alter life prospects more dramatically than later ones. A gift of \$1,000,000 at age 25 provides seed money for a start-up, while inheriting such wealth at age 65 likely does no more than enable one to enjoy a more comfortable retirement. To that end, Halliday endorses adjusting the rates depending on the age of the beneficiary. This seems generally sensible, and could be done by adapting rules similar to those crafted by the Meade Commission (1978), which proposed such a structure in England in the 1970s. The possibility of creating an exception when minors inherit because they have lost both parents is discussed in Section 3.3.2.

### *3.3. Frequency: Determining the Number of Transfers*

A further issue is determining how many times wealth has been transferred. This Article argues not only that generation-skipping transfers be penalized, but also that no adjustments be made for deaths in rapid succession as a general rule.

#### *3.3.1. Generation-Skipping Transfers*

Halliday (2018: 63) flags but does not tackle generation-skipping transfers. Imagine that instead of leaving \$10,000,000 to Mother, Grandfather leaves \$10,000,000 directly to Daughter. In the United States, current law imposes an additional tax on such transfers so that families face similar tax burdens regardless of whether their wealth skips generations or proceeds from one generation directly to the next. A Rignano tax should contain similar rules by treating a transfer from Grandfather to Daughter as a second transfer instead of a first. This prevents families from minimizing the number of

transfers in order to evade the higher rates applicable to second transfers.<sup>5</sup> It also reflects Halliday's normative premises. If Mother is successful enough that Grandfather feels comfortable bypassing her and leaving his wealth directly to Daughter, that indicates the presence of the financial and social capital that concerns Halliday.

### 3.3.2. *Transfers in Rapid Succession*

Transfers that happen in rapid succession raise a related issue (see Halliday 2018: 63-4; Rignano 1924: 45). Imagine that Grandfather leaves his fortune to Mother, who dies unexpectedly one year later, re-bequeathing his inheritance to Daughter. Halliday hints that this should not be considered a second transfer: "A short interval between bequests may mean that a donor has had less time to save and accumulate due to an early death. It is harder to say, in that case, that this person's bequests should still be taxed as if he or she had remained idle" (2018: 63-4). Although it is true that Mother has had less time to augment Grandfather's inheritance *after* receiving it, she had time *before* either her or Grandfather's death to earn her own wealth. This is especially true as lifespans increase and Mother may be well into her 50s or 60s at Grandfather's death. Any wealth created by Mother will be taxed as first-generation wealth. Counting each transfer thus does not distort Mother's incentives.

A stickier question arises when transfers occur in rapid succession because Mother dies young, when Daughter is still a minor. In such cases, the hardship of losing a parent so young likely offsets some or all of the benefits of inheriting wealth, especially if Mother's death leaves Daughter an orphan. Treating this the same as other double transfers seems especially unfair if the rates adjust for the age of the recipient, as suggested in Section 3.2.3. Two adjustments of varying strength exist. The "soft" option is to offset the increased rates that apply to transfers received at a young age. A stronger approach would be to not count wealth inherited due to the death of both parents before reaching a certain age (perhaps 21 or 25) as having gone through an additional transfer. Halliday's premises do not point strongly in either direction; as with rates, political considerations will likely play a large role in choosing between these options.

### 3.4. *Valuation*

An as-yet unidentified issue is how to value initial wealth transfers when they are re-transferred. Again assume Grandfather starts with nothing and amasses \$10,000,000, which he bequeaths to Mother. She dies with an estate of \$50,000,000, which she leaves to Daughter. How much should be traced back to Grandfather? The simplest approach is that assumed by Rignano and Halliday. Without discussion, their examples suggest treating \$10,000,000 as a second transfer and \$40,000,000 as newly-created wealth.

---

<sup>5</sup> The existing generation-skipping transfer tax rules could be used to determine when a generation-skipping transfer has occurred. For example, if Mother predeceases Grandfather, no additional transfer would be imputed.

## Taxing Old Money

### 3.4.1. *The Problem*

This obscures the fact that asset values fluctuate over time due to a mix of factors – inflation, the time value of money, changes in market conditions, and the owner’s efforts. Take inflation. Assume that Mother invests Grandfather’s bequest in an asset that keeps exact pace with inflation. \$10,000,000 inherited in 1989 has an inflation-adjusted value of just over \$21,000,000 now.<sup>6</sup> If she bequeaths the asset to Daughter, the Rignano/Halliday default treats the \$11,000,000 increase as coming from Mother and only \$10,000,000 as coming from Grandfather. Even though Mother adds no value – the asset simply keeps pace with inflation – she is still able to transfer more than what she receives with no effort.

### 3.4.2. *Risk-Free Rate of Return as the Default Solution*

This demonstrates that attributing only \$10,000,000 of Mother’s estate to Grandfather is overly simplistic. A better approach is to impute the real risk-free rate of return to Grandfather’s bequest (that is, after taking into account inflation). This alternative best reflects the Rignano/Halliday desire to distinguish between Mother’s earned and inherited wealth by acknowledging the existence of risk and choice. To illustrate, imagine that Mother inherits a building worth \$10,000,000. She now has \$10,000,000 that she can invest as she chooses – be it in stocks, bonds, or a risky start-up.

If she chooses to continue holding the building, some – but not all – of the building’s increased value stems from Mother’s choice. The increase has different components: the risk-free rate of return, a return to risk, and (occasionally) inframarginal returns (Brooks 2013: 261 n. 25; Cunningham 1996: 23; Weisbach 2004: 19). The risk-free rate of return represents the return for investing in a project with zero risk that offers a guaranteed return, such as a U.S. Treasury bond. It is a pure time-value-of-money return that is compensation for use of the invested funds, and is sometimes referred to as the “return to waiting” (Brooks 2013: 261 n. 25; Cunningham 1996: 23). The return to risk is exactly what it sounds like—the “potentially greater, but more variable, return from investing in a risky asset, such as stock” (Brooks 2013: 261 n. 25). Some, but not all, investments also generate inframarginal returns, which are returns above and beyond the normal risk premium due to unique opportunities. As Brooks (2013: 261 n. 25) explains, “such returns are essentially economic rents due to market power, particular skills, particular access to investment ideas, or unique ideas.” Regardless of what Mother would have invested in, Grandfather’s wealth would have triggered the risk-free rate of return at minimum. Yet different investments yield varying returns to risk and inframarginal returns; such that any returns above the risk-free return should be attributed to Mother’s choices.

The default rule should therefore be to attribute the risk-free rate of return – as measured by the average U.S. Treasury bond yield – to Grandfather’s investment. For example, if Mother outlives Grandfather by 30 years, the average rate of return for a

---

<sup>6</sup> See U.S. Bureau of Labor Statistics (2020).

30-year bond should be imputed to Mother's inheritance from Grandfather. Excess wealth transferred by Mother should be treated as new, first-generation wealth.

### 3.4.3. *Complications*

The foregoing assumes both choice and successful investments. What if those assumptions are incorrect? Take choice. Perhaps Grandfather bequeaths Apple stock to a trust with an independent trustee over whom Mother has no control. In that case, none of the stock's value is rightly attributable to Mother, since Mother had no choice in investing the assets and assumed no risk. The full value of the stock at Mother's death should be imputed to Grandfather. To determine when Mother lacks control, the Rignano tax could import the grantor trust rules used in the U.S to determine when trusts are treated as owned by grantors for income tax purposes.

Next consider success (or the lack thereof). What if Mother squanders Grandfather's fortune, but then earns her own fortune in an unrelated investment? Perhaps Mother invests Grandfather's \$10,000,000 in Blockbuster Video and quickly loses it. Later, Mother gets in on the ground floor of Google and parlays a few thousand dollars into \$10,000,000, which she leaves to Daughter. Is this a first- or second-generation transfer?

It should be treated as a second transfer for three reasons (Rignano favors this approach (1924: 52-53)). First, Mother is able to transfer \$10,000,000 more to Daughter than otherwise. Grandfather's bequest allows Mother to start at \$10,000,000; lose \$10,000,000; re-earn \$10,000,000; and end at \$10,000,000. Without Grandfather's bequest, Mother starts at \$0 and ends at \$0 after losing and re-earning \$10,000,000. Second, recall that if Mother successfully invests Grandfather's wealth, we credit her with any positive returns to risk. Parity suggests that she also bear the burden of unsuccessful risk-taking.

Third, what really concerns Halliday is the mere existence of Grandfather's bequest as a signifier of familial wealth norms. Treating Mother more leniently when she dissipates Grandfather's fortune before making her own fortune—as opposed to preserving or growing Grandfather's fortune while doing so—obscures the significance of the bequest's existence. The mere fact Mother receives an inheritance suggests she and Daughter are now part of a group with wealth norms. At minimum, Mother should not be treated as bequeathing only first-generation wealth to Daughter in such situations.

Indeed, the focus on wealth norms suggests that if anything, Mother should be treated more harshly if Grandfather's dissipates because she spends it. Compare two scenarios, *Save* and *Spend*. In *Save*, Mother invests the inheritance and passes it along to Daughter at Mother's death – after Daughter's life prospects have largely been determined. In *Spend*, Mother spends the inheritance on a mansion in a gated community, country clubs, expensive cars, exclusive schools, and tutors, trips, and camps that give Daughter a leg up. In theory, Mother's actions in *Spend* perpetuate economic segregation more than in *Save* and should be taxed more heavily. The difficulty with making this distinction, however, is two-fold. First, distinguishing consumption from a poor investment can be difficult. What if, for example, Mother (and/or Daughter) love gourmet food, and Mother invests in a new restaurant? Given

## Taxing Old Money

the notoriously low success rate of new restaurants, one might view this as consumption and not a responsible investment. Second, money is fungible. In *Save*, perhaps the security of Grandfather's bequest frees Mother up to spend more of any wealth generated by Mother herself on consumption that benefits Daughter. Perhaps Mother buys a larger house than otherwise, or feels more comfortable springing for private school, knowing Grandfather's bequest is there if she saves less and spends more of her own money on Daughter. Regardless of how one feels about treating Mother more harshly when she spends down Grandfather's investment in lieu of maintaining it, there is no justification for treating her more leniently.

### 3.5. *Tracing*

A fifth issue – flagged by neither Rignano nor Halliday – is tracing Grandfather's wealth among multiple beneficiaries. Again assume Grandfather bequeaths Mother \$10,000,000, but now Mother has two children, Daughter and Son. In applying the tax to each, up to what dollar amount per recipient should be treated as second-generation wealth? The first \$10,000,000 transferred to each, or a total of \$10,000,000, allocated between the two recipients? On one hand, the former reflects Halliday's concern that what really matters is the existence of successive inter-generational transfers, because both children grew up in a family with wealth norms. Moreover, attributing \$10,000,000 to each of Daughter and Son is simple. On the other hand, Halliday also expresses concern about the potential negative effects of taxation on the incentives of heirs to generate their own wealth, and the former structure arguably creates harsher disincentives: a mother of two or three has to double or triple her inheritance before she can pass along any wealth tax-free, whereas a mother of one can pass along the first dollar she herself earns. It seems plausible that Halliday would neither want to create such disparities in Mother's incentives nor create such a deep hole for parents of two or more children.

If Grandfather's bequest is to be allocated between Daughter and Son, the next question is how. Ideally, the bequest could be allocated to Daughter and Son equally, such that the first \$5,000,000 transferred to each is considered second-generation wealth. If Mother makes no lifetime gifts and bequeaths them Grandfather's wealth at her death, it is simple enough to allocate the bequest in this manner. Lifetime gifts, however, complicate this. One possibility is allocating the bequest *pro rata* among Mother's children by giving them each a \$5,000,000 "taxable amount" that would work as a mirror-image of existing exemptions. Transfers to each of Daughter and Son would be taxed until they reached \$5,000,000 apiece; later transfers would be untaxed. This solution, however, undertaxes when Mother favors one child. If Mother gifts \$10,000,000 to Daughter and nothing to Son, only \$5,000,000 would be treated as second-generation. Moreover, assigning a per-capita amount at Grandfather's death requires knowing among how many people Grandfather's bequest should be apportioned, which may be unknowable at his death.

A simpler solution is a first-in-time approach that treats the first \$10,000,000 received by Daughter and Son as second-generation, regardless of how it is apportioned between them. This is essentially what the current system does with a donor's lifetime

exemption amount, and allows Mother to allocate the tax burden by deciding how to time her transfers.

### 3.6. *Transition Rules*

A Rignano tax contains a unique transition issue. Treating all transfers after the tax's imposition as first transfers essentially delays implementation for a generation. Only some transfers of existing wealth should be considered first transfers. As Rignano and Halliday note, a transition rule is necessary to determine what portion of existing wealth should be considered inherited. Rignano, for example, suggests assuming that one-third to one-half of current wealth is inherited (1924: 89-90). Empirical studies estimate that anywhere from 15% to 46% of current wealth is inherited (Kopczuk & Lupton 2005: 3); using a figure of one-sixth to one-third therefore seems plausible.

### 3.7. *A Word About Administration*

A Rignano tax requires more record-keeping than a traditional estate or inheritance tax, but this burden is not insurmountable. Return to the Grandfather/Mother/Daughter pattern. When Grandfather dies, his estate files a tax return. His executor would be required to make an election in order to treat any of his wealth as first-generation. If the executor makes no election, Grandfather's estate will be treated entirely as a second-generation transfer. Absent malpractice, Grandfather's executor will make the election; this creates a record for future reference. To calculate Daughter's tax liability when Mother transfers wealth to her, we need to know three things: The imputed value of the Grandfather/Mother bequest, the value of Mother's transfer, and the current value of any assets specifically bequeathed from Grandfather to Mother over which Mother had no control. The first we know by applying the real risk-free rate of return to the value of the Grandfather/Mother bequest at Grandfather's death, which is recorded when his executor makes the Rignano election. The second and third present no more difficulties than under current law. The success of the current marital deduction rules, in which a decedent's tax consequences turn on the actions of a prior decedent, suggest this is workable.

## 4. CONCLUSION

This Article explores whether it is possible as a technical matter to translate Halliday's ethical premises into reality, and concludes that it is. Based on experience with existing transfer tax systems in the United States, it provides specific recommendations for doing so. Crafting such a tax, however, involves enormous complexity—more than in alternative taxes commonly proposed to address standard equal opportunity concerns, such as traditional estate or inheritance taxes and/or annual wealth taxes. Although occasionally nodding to politics (for example, by noting that the choice of rate largely turns on political rather than technical considerations), this Article generally sidesteps questions of political feasibility.

## Taxing Old Money

Such issues are beyond the scope of this Article, although I hope that other commentators—in this volume or elsewhere—will address them. For example, political reality in the United States and Europe suggests that public attitudes to wealth and wealth transfer taxes are enormously complicated. Is there an appetite for such taxes at all? If so, should the tax system distinguish between first and later-generation transfers as a normative matter? Put another way, is a tax inspired by Halliday’s ethical premises the one that should be pursued in an ideal world? If so, is the design proposed herein the best way of pursuing those goals? Perhaps, for example, a simpler but less precise solution (such as a regular accessions tax with an unlimited exemption to individuals in the first generation to inherit wealth) gets “close enough” with much less complexity. Or perhaps an ideal inheritance tax would not exempt newly-earned wealth, but a Rignano tax provides a second-best solution. It may, for example, thread the political needle between competing intuitions that it is unfair for some to start life with a huge head start while recognizing that many hold an innate desire to work hard to benefit one’s children. Given the technical complexities of a Rignano tax, a better sense of its political feasibility is necessary for a full evaluation of whether pursuing one is a worthwhile endeavor.

### BIBLIOGRAPHY

- Alstott, A., 2007: “Equal Opportunity and Inheritance Taxation”, *Harvard Law Review* 121: 469-542.
- Batchelder, L., 2009: “What Should Society Expect from Heirs? The Case for a Comprehensive Inheritance Tax”, *Tax Law Review* 63: 1-112.
- Brooks, J., 2013: “Taxation, Risk, and Portfolio Choice: The Treatment of Returns to Risk Under a Normative Income Tax”, *Tax Law Review* 66: 261-304.
- Cunningham, N., 1996: “The Taxation of Capital Income and the Choice of Tax Base”, *Tax Law Review* 52: 17-44.
- Estate of Grace* (1969) 395 U.S. 316, 89 S. Ct. 1730.
- Fleischer, M., 2007: “Charitable Contributions in an Ideal Estate Tax”, *Tax Law Review* 60: 263-322.
- 2011: “Equality of Opportunity and the Charitable Tax Subsidies”, *Boston University Law Review* 91: 601-64.
- 2016: “Divide and Conquer: Using an Accessions Tax to Combat Dynastic Wealth Transfers”, *Boston College Law Review* 57: 913-46.
- Halliday, D., 2018: *The Inheritance of Wealth: Justice, Equality, and the Right to Bequeath*, Oxford: Oxford University Press.
- Kopczuk, W. & Lupton, J., 2005: “To Leave or Not to Leave: The Distribution of Bequest Motives”, NBER Working Paper 11767.
- Kopczuk, W., 2013: “Taxation of Intergenerational Transfers and Wealth”, in *Handbook of Public Economics, Vol. 5*, ed. A.J. Auerbach, R. Chetty, M. Feldstein, and E. Saez, 329-388, Amsterdam/Oxford: North Holland.
- McCaffery, E., 1994a: “Cognitive Theory and Tax”, *UCLA Law Review* 41: 1861-1948.

Miranda Perry Fleischer

- 1994b: “The Uneasy Case for Wealth Transfer Taxation”, *Yale Law Journal* 104: 283-365.
- Meade, J., 1978: *The Structure and Reform of Direct Taxation*, London: Allen & Unwin.
- Nozick, R., 1989: *This Examined Life*, New York: Simon and Schuster.
- Rignano, E., 1924: *The Social Significance of the Inheritance Tax*, trans. W. J. Shultz, New York: A.A. Knopf.
- U.S. Bureau of Labor Statistics, *CPI Inflation Calculator*, viewed January 30, 2020, URL = < [https://www.bls.gov/data/inflation\\_calculator.htm](https://www.bls.gov/data/inflation_calculator.htm) >.
- Weisbach, D., 2004: “The (Non)Taxation of Risk”, *Tax Law Review* 58: 19-58.