
THE ROLE OF INHERITANCE WITHIN CAPITALISM

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Individuals often interpret the right to bequeath wealth as being part of the capitalist system. Sean Tong takes issue with this interpretation, arguing that no such association exists, and that the curtailment of inheritance can further the capitalist ideal of economic growth and consequently foster greater societal welfare.

Introduction

There can be little doubt that the practice of inheritance contributes to the existence of wealth inequality in capitalist societies: 31% of wealth in the United States can be attributed to bequests, in addition to the 20% gained through inter vivos transfers (Gale and Scholz, 1994). As will be shown in the following section, the distribution of inheritances is highly asymmetric. A small minority of the population collect large amounts while the vast majority receive little or nothing.

It will be argued in this essay that, far from being a central tenet of capitalism, the practice of inheritance actually runs counter to its principles and undermines the meritocratic ideals we claim to espouse. The case for a significant curtailment of inheritance will be presented from a theoretical perspective, before common objections are considered. It is worthwhile first to examine the nature of inheritance in Ireland, and to show the role it plays in perpetuating social stratification.

Inheritance in Ireland

Gifts and inheritances in Ireland are currently subject to capital acquisitions tax at a rate of 30% on amounts above a certain threshold. The value of this threshold is dependent upon the relationship between the two parties, and is set at €250,000 for transfers from parents to children¹.

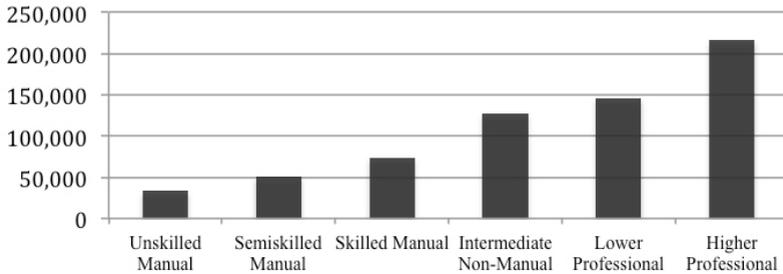
Unfortunately, there is a distinct lack of quantitative data regarding inheritance in the Irish economy, at least of late. Nolan (1992) presents the

¹ <http://www.revenue.ie/en/tax/cat/>

most recent source, the 1987 ESRI ‘Survey on Income Distribution, Poverty and Usage of State Services’. This section will discuss some of the more salient trends found in the data, which examined the value of real property and businesses inherited by different households.

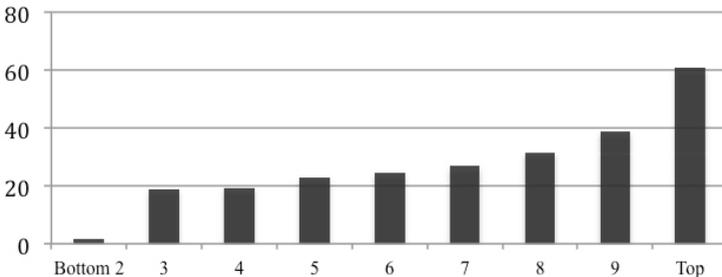
The distribution of inheritances received in the sample was highly asymmetric. Figure 1 (below) shows the mean value of inheritance received as a function of social class. There is a clear correlation between the two, with the value of the former rising steadily as we move from unskilled manual labourers (£33,216) to higher professionals (£215,732). Not only is the distribution of inheritances asymmetric, it is clearly skewed towards the more affluent classes.

Figure 1 : Mean Inheritance (£) by Social Class



Further evidence of this comes from the link between current total wealth and inheritance. Figure 2 (below) shows that households in the top wealth deciles were far more likely to have received an inheritance. The majority (60.8%) of those in the top 10% had received an inheritance, while almost none (1.6%) of those in the bottom 20% had.

Figure 2 : Beneficiaries (%) by Current Total Wealth



As well as demonstrating that the wealthy are more likely to have received inheritance, the data regarding current total wealth reflect those of Figure 1 in that those in the higher deciles also received larger mean inheritances. So while the mean value of inheritances received by those in the bottom 20% was just £25,984, the corresponding value for the top decile was £199,957.

It would appear that the practice of inheritance in Irish society, as elsewhere, serves to exacerbate wealth inequality and favour the rich. Those who have least tend to inherit least, while those who have more tend to receive more. It is this inequality that serves as the basis for the argument against inheritance.

The General Proposal

The exact form that a curtailment of inheritance (if desirable) should take is open to debate, and is not the focus of this essay. In order that arguments for and against a restriction may be considered more meaningfully, however, a general scheme will be outlined here that draws upon and incorporates suggestions from a number of different sources.

Ascher (1990) proposes full abolition of inheritance, with the property of the individual being auctioned at death and the proceeds accruing to the State. He includes a number of exemptions in this, of which I believe transfers to spouses and dependent lineal descendants have merit. Similar provision regarding inter vivos transfers would, of course, be necessary to prevent the use of gifts to circumvent the new legislation.

A suggestion made by Haslett (1986) may also be worth incorporating, as he includes a provision that would allow individuals to write a 'will' of sorts. Rather than specifying who should inherit what, this would give allocated individuals the opportunity to purchase specific items of the deceased's property at an independently-appraised price, in lieu of a free auction. This would allow for the safeguarding of family heirlooms, businesses and the like. The Government may provide loans to assist people in this regard.

This very brief outline should serve only as a reference point when considering the arguments for and against. It is clearly not the only means of curtailing inheritance: Haslett (1997), for example, believes that allowing a lifetime quota for gifts and inheritances would strike a more sensible compromise between distributive justice and cultural norms than complete abolition. It is worth stressing once more that the precise form that a restriction of inheritance should take is not the focus of this essay; rather, it is to establish whether a restriction of some sort is desirable in theory.

The Argument for Curtailment

The abolition or significant curtailment of inheritance can be justified on four primary grounds, which will be presented in this section. In brief, it will be argued that such a proposal would bring us closer to both our capitalist and meritocratic ideals, reduce wealth inequality, and provide a significant source of government revenue.

Capitalist ideals

In his lectures on jurisprudence, Adam Smith himself said that “there is no point more difficult to account for than the right we conceive men to have to dispose of their goods after death” (Fleischacker, 2004: 198). This is an entirely fabricated social right, and one that runs counter to capitalist ideals. The free enterprise system is predicated upon rewarding and, consequently, incentivising production. Remuneration is allocated to those who provide the factors of production, and in proportion to that provision. Inheritance stands in stark contrast to this principle: it is not earned, but comes about entirely as the result of a parental lottery. From a purely economic perspective, the random allocation of resources cannot possibly lead to an efficient outcome. To allow such a state of affairs is to undermine the working of the ‘invisible hand’ by which market activities are guided.

Chester (1976) rightly points out that the present arrangement of taxing incomes more heavily than inheritances is completely at odds with capitalist values, and serves to dampen productivity. A return to these values would necessitate a shift from the taxation of achievement (income) to ascription (inheritance).

Though it is often branded as a Communist proposal, the restriction of inheritance is entirely compatible with, and indeed demanded by, the central tenets of the capitalist system. Contrary to popular perception, the practice of inheritance and the advocacy of capitalism do not go hand in hand. To allow the former is to undermine the latter, and so the curtailment of inheritance must be seen as a means of returning to capitalist ideals.

Meritocratic ideals

While the practice of inheritance runs counter to our economic system, it is also in conflict with one of our social goals: that of meritocracy. If we are to expect individuals to compete in the market economy, it is imperative that the rules governing this are fair and uniformly imposed. Inheritance undermines this by significantly reducing equality of opportunity.

To be clear: the concept of equality of opportunity is entirely dis-

tinct from equality of outcome. Income disparities arise naturally in a capitalist economy and are a reward for productivity. Unequal opportunity, on the other hand, runs counter to the meritocratic ideals that we claim to espouse. Inheritance clearly contributes to this, as those born to wealthy families inherit more than those born to poor ones. Wealth is opportunity, and to receive more of the former is to have more of the latter.

Aside from the ethical implications of this, there are clear economic disadvantages to an unequal distribution of opportunity. As Stiglitz points out: “whenever we diminish equality of opportunity, it means that we are not using some of our most valuable assets—our people—in the most productive way possible” (Stiglitz, 2011). Buffett puts it more bluntly, comparing it to “choosing the 2020 Olympic team by picking the eldest sons of the gold-medal winners in the 2000 Olympics” (Sahadi, 2007).

A simple analogy, presented by Haslett (1986), makes this point easier to appreciate. We consider a hypothetical race between two competitors: in one case, the two start at the same point along the track, whereas in the second case one of the competitors is given a significant head start. It does not seem contentious to state that it is in the first of these races, which represents equal opportunities, that the effort exerted by the runners will be maximised. In the second case, poor motivation results from complacency and hopelessness, from the perspectives of the advantaged and the disadvantaged respectively.

Insofar as the capitalist system is predicated upon competition, the current state of affairs represents a rigged game. The rewards of production cannot be distributed accurately if outcomes are achieved through initial luck rather than present contribution. The practice of inheritance essentially exempts the children of the wealthy from the economic competition that others are subject to and that all have agreed upon. It is socially and economically corrosive, and for this reason its curtailment can be justified.

Wealth inequality

Though much focus has been placed on the disparity between high and low income earners, a much greater inequality is found with regards to wealth (Cagetti and De Nardi, 2006). In Ireland, the wealthiest 1% control 20% of all wealth, and the top 5% hold 40% of wealth (Bank of Ireland, 2007). While the income inequalities that arise naturally from market competition represent rewards for productivity, the wealth inequality that arises from inheritance does not. Rather, it is a means of perpetuating financial nobility, concentrating unearned wealth in the hands of an undeserving few.

By fragmenting large familial fortunes, a restriction upon inheri-

tance would bring about a number of social benefits. The economic and political power that concentrated wealth commands, and which may lead to distortions in the marketplace, would be reduced. In addition, as alluded to earlier, the incentive to work would be restored in the children of wealthy families. The reduction in wealth inequality that restrained inheritance would necessitate could thus serve a number of social and economic purposes.

Government revenue

The final, obvious benefit of this proposal is the significant government revenue that would be raised. While precise data are lacking in an Irish context, there can be no doubt that the heavy taxation of intergenerational transfers would represent a large, much-needed increase in the State's income.

What distinguishes this form of revenue from others is that it is a remarkably painless one. Jeremy Bentham (1795) considered it to be "absolutely the best" form of taxation, given that it affects prospective rather than current owners of property. Although affected heirs would doubtless feel aggrieved, this stems entirely from current expectations. Once the status quo is changed so that children no longer expect large transfers of unearned wealth, the disappointment caused by the proposal would dissipate to triviality.

The revenue raised from increased taxation on inheritance could be put to innumerable uses, some of which will be briefly referred to throughout this essay. It could, for example, be used to counteract some of the supposed negative externalities that a restriction on inheritance would bring, or to reduce rates of income tax to even further reward achievement over ascription. While the exact use of the revenue is beyond the remit of this essay, it should be clear that a curtailment of inheritance would be a significant contributor in this regard.

Response to Criticisms

In examining the literature, six primary objections to the curtailment of inheritance are seen to predominate. These will now be considered and evaluated in turn.

Violation of a natural right

It is often claimed that the testator has a 'right' to dispose of their property as they see fit, and that inheritance tax represents a violation of this right. In reality, however, inheritance is not a natural right but a civil one granted by society. This is illustrated most clearly by the heavy state involvement that is required to actually facilitate the practice of inheritance (Trout and Buttar,

2001).

The State acts as an intermediary between the original owner of property, whose claim ceases with his or her death, and the heir, whose ownership only comes into effect once the State legitimates the transfer. In the interim, assets are frozen, creditors are repaid, and competing claims are assessed. It is thus only through State involvement that the 'right' to inherit can even come about, which renders untenable any claim that such a right is a natural one.

As Haslett (1986) demonstrates, it is equally fallacious to claim that inheritance taxes are violations of property rights. To do so is to be guilty of begging the question. The right to property is already subject to a number of qualifications and exceptions, including income tax. The debate is whether or not inheritance should be considered a part of this qualified right to property. It is circular reasoning to simply claim outright that it ought to be.

Reduced incentive to work

It is argued that restricting inheritance would severely reduce the individual's incentive to work, under the assumption that the motive to bequeath is a significant contributor to the overall desire to produce. There are, however, clearly a multitude of reasons that people work, with bequests being just one of these.

Amongst these other motives are the desires to fund a good lifestyle, to achieve self-actualisation, and to guard against uncertainty. Haslett (1986) illustrates the insignificance of this effect by considering childless couples and professional athletes. There is no empirical evidence to suggest that the former group are less productive than couples with children (McClelland, 1961), and it seems risible to suggest that the latter would become less competitive should more stringent inheritance legislation be introduced. Empirical studies by both Hurd (1989) and Gan et al. (2004) estimated a very small bequest motive, and the latter concluded that most bequests are made unintentionally.

While it is unlikely that a limitation on inheritance would lead to a reduction in the incentive to work, it is quite likely that it would produce the opposite effect: that there would be an overall increase in this very incentive. Returning to the race analogy used earlier, it seems probable that an increase in equality of opportunity would increase the effort exerted by both the rich (out of newfound necessity) and the poor (out of newfound ambition).

Reduced incentive to save and invest

In a similar vein to the previous objection, it is claimed that a reduction in savings, and consequently investment, would result from this proposal (Tull-

ock, 1971). It is worth remembering at the outset that corporate and State savings would be entirely unaffected by changes in inheritance legislation, so any influence must be restricted to private savings.

As with the incentive to work, other motives clearly exist to save. Amongst these are the desires to provide for retirement and to guard against uncertainty in old age (Kessler and Masson, 1989). Given the inherent unpredictability of death, frivolous consumption is unlikely to predominate in the twilight years, even with well-developed markets for annuities. If this were not the case, the revenue raised from this proposal could easily be used to redress reductions in savings and investment, whether directly or through subsidies and the like.

The existence of other inequalities

While there is no doubt that true equality of opportunity can never be achieved, and certainly not without resorting to extreme measures, the presence of other inequalities in our society can in no way excuse the damage done by inheritance. While many forms of inequity are beyond our control, inheritance, as a socially constructed privilege, is not one of these.

The most remarkable thing about this argument, given its obvious flaws, is that so many find it convincing. Milton Friedman (1962) points out that significant individual differences exist in the allocation of natural abilities, and claims that the unequal distribution of inheritances should be similarly accepted, as there is no ethical difference between the two.

This reasoning is flawed on two accounts. As already stated, it is absurd to claim that the presence of one inequity should justify the existence of another. In addition, Friedman's suggestion that the two forms of inequality are comparable is untenable. What he fails to identify is that individual differences do not, in and of themselves, lead to income or wealth. It is, rather, the utilisation of these abilities in a manner that is valued by society that brings such a reward. It is this distinction that makes one justified, and the other not. A reform of inheritance legislation neither claims nor seeks to establish perfect equality; rather, it aims to restore some equality of opportunity in a domain over which we have complete control.

Practicalities

For the sake of brevity, this essay considers the restriction of inheritance from a purely theoretical perspective. For this reason, common practical objections such as the ineptitude of governments, administrative costs, and likely public outrage will not be considered here. While there is merit to some of these, and it is likely true that the unilateral implementation of radical measures would

be problematic, these difficulties are certainly not insurmountable. A more in-depth treatment can be seen in, for example, Ascher (1990).

Conclusion

This essay has articulated the argument for the abolition or significant curtailment of inheritance. It has been shown that it is in conflict with our economic and social ideals, and that to tax it more heavily would bring a number of ancillary benefits. Furthermore, the arguments in support of inheritance tend to be fallacious or inconsequential.

Though the practicalities of implementing a proposal of this sort, and indeed the specifics of the proposal itself, cannot be adequately considered in this essay, the conclusion remains: if we are to be consistent with our ideals, we must take measures to limit the role that inheritance plays in influencing individual outcomes.

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