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# TAXES AND TORTS IN THE REDISTRIBUTION OF INCOME

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**Taxes and Torts in the Redistribution of Income**

*David A. Weisbach*[*]

When I was asked to give the Coase lecture, it presented somewhat of a puzzle. The lecture is supposed to introduce a topic in law and economics to first year students. I teach tax law and generally do not teach first year students. What would I have to say to them? Notwithstanding that the tax law is virtually never mentioned in first year courses such as torts, contracts, and property, or more generally in common law jurisprudence, I will argue that the tax system is actually central to thinking about such topics. The thesis is that the presence or absence of the tax system *completely changes* how one thinks about basic subjects.

The reason why this is so is because the tax system plays a central role in the redistribution of income or wealth. In thinking about legal rules, we must ask whether they should be designed to redistribute or whether they should merely be efficient. For example, we might want to know whether we have pro-tenant landlord/tenant rules on the theory that tenants are systematically poorer than landlords. Should we have pro-consumer warranty rules on the theory that consumers are systematically poorer than producers? And should we have pro-plaintiff nuisance rules?

A common thought might be that legal rules that redistribute income are a good idea because they help the poor and disadvantaged. Laws of this sort can be viewed as a means of doing social justice. Law is not some sterile instrument that comes out of a vacuum. Instead, law is a means of improving our society. A common counter-claim in law and economics is no, legal rules should not be used to redistribute to the poor. Instead, legal rules should be efficient. While we see the efficiency claim a lot, it is not always clear what it is based on. Do law and economics scholars simply not like the idea of redistribution? Are they uninterested in social justice?

I will argue that legal rules should not be designed to redistribute to the poor, but this is not out of a lack of concern for distribution or equality. My argument is that there is a better method of addressing these concerns. In particular, the tax system is a better tool for redistribution of income than legal rules. We should therefore use the tax system rather than legal rules to address income inequality and, correspondingly, legal rules should not systematically favor the poor. Without the tax system, this conclusion would not necessarily

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hold and legal rules might optimally be set to redistribute. Thus, I claim a central place for the tax system in thinking about legal rules.[1]

I will start by discussing redistribution more generally. Many of you will already be familiar with this initial material but for some of you it might be new and it will probably be helpful to review it for everyone. Then I will turn to a comparison of legal rules and the tax system as methods of redistribution.

## I. Redistribution

Why might we want to redistribute income? There are a variety of reasons. For example, the rich might be altruistic toward the poor so that redistribution helps both. Alternatively, redistribution might act as a form of social insurance. Any of us could easily be down and out someday due to misfortune. Redistribution hedges this risk.

The most commonly cited reason for redistribution, and the one I will focus on, is that individuals have declining marginal utility of income. All this means is that is as individuals get wealthier, each dollar is less important. One reason why individuals might have declining marginal utility of income is simply that individuals will tend to satisfy their most important needs first. Once they have enough income to satisfy these, they move on to lesser needs. This type of planning or maximization means that the first dollar one receives is more important than the millionth. Another reason we might believe in declining marginal utility is just introspection – the extra brass and teak fittings on a gazillionaire's yacht seem to be less important to him than food or housing to a pauper.

If individuals have declining marginal utility of income, redistribution can be a good idea because the loss in utility to the wealthy from whom we take a dollar is not as great as the gain to the poor, who receives the dollar. If we continued the analysis without thinking further, we might conclude that significant redistribution is appropriate. In fact, at the extreme, we would redistribute until everyone had equal incomes. So long as there is declining marginal utility, it is always a good idea to take from the wealthier and give to the poorer until all incomes are equal.

The problem is that redistribution is costly. Not only are there the costs of the administrative apparatus of redistribution – measuring income, collecting the money, etc. There are costs in terms of incentives. In particular, if we take income from people, then each hour of work or unit of savings brings less to them. For example, if you previously earned \$10 an hour and we start taking 40% of your income, your take home pay is now \$6 per hour. This means that the trade off between working and doing other things – which I

[1]When I use the term "tax system" I mean it broadly to include the transfer system as well. We can have government payments to individuals as well as collections.

will call leisure – is changed. Work is relatively less attractive than leisure. As a result, we can expect people to work less. Why spend those extra hours, for example moonlighting at a second job, for not much reward?

This distortion, which is generally called a distortion in labor/leisure choice, results in efficiency losses. The overall size of the pie, including how much there is to redistribute, goes down because people work less. A metaphor that is frequently used is that redistribution is a leaky bucket. When we take money away from one person to give to another, we lose some during the transfer.

What is the size of the distortion? There are, as you might guess, a lot of studies and, as you might also guess, they produce conflicting results.[2] It turns out to be very difficult to measure. One story is that the distortion is small in part because people tend to work relatively fixed hours. If your job demands 40 hours per week, you don't have the choice to reduce it to 35 hours when tax rates go up.

Another story is that the distortion is large, particularly for various subclasses of individuals. Our moonlighter has the choice of working the extra hours. Second earners in a family are also thought to be very responsive to changes in tax rates. And even primary earners putting in their 40 hours can be responsive to tax rates in a variety of subtle ways, such as how much they invest in education or training, how hard they work for advancement, and similar nonhours elements of work. This empirical debate will continue on for the indefinite future. For our purposes, unless you think the distortion is zero, there will be a cost to redistribution.

In addition, regardless of the absolute size of the cost initially, it is generally thought to go up with taxes, so the more we wish to redistribute, the higher the cost. Worse, it is thought to go up very fast – with the square of the tax rate – so even small distortions can become very large if tax rates are high enough.

The million dollar question is how we balance these concerns. Redistribution seems like a good idea but it is costly. How do we decide how much to do? To make this decision, we need a theory of what is good for society – we need some philosophy. I'm not going to do philosophy here – I probably couldn't even if I tried. Instead, I'm going to simply demand that, whatever answer we get, we make it explicit.

Such an expression of beliefs about this trade off is called a social welfare function. It tells us how well off a society is based on the welfare of the individuals in that society. This means it tells us when more redistribution at a given cost is a good idea. I will, for purposes of our discussion, put two restrictions on the social welfare function.

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[2] See, for example, the papers contained in "Does Atlas Shrug? The Economic Consequences of Taxing the Rich" (Joel B. Slemrod, ed., 2000).

First, I will restrict the social welfare function to be a function of the welfare of individuals. Society is better off when individuals in society are better off. Concepts like justice can affect social welfare, but they must do so by making individuals better off rather than by satisfying an abstract ideal. Second, I want the social welfare function to be consistent with Pareto efficiency. This means that if the welfare of one individual goes up and the welfare of nobody else goes down, we should think of society as better off.

What are some prominent examples of social welfare functions that meet these criteria? One of the most prominent is the utilitarian social welfare function. Utilitarians hold that we can measure how well society is doing by adding up the utilities of the individuals in society. Each person is weighted equally under this social welfare function.

The philosopher John Rawls proposed a different measure of social welfare known as the maximin. While not exactly what he said – he was concerned with items other than individual welfare – a crude version of the maximin is that the welfare of society is measured by the welfare of the worst off individual in society. Rawls' formulation is generally thought to be more egalitarian than the utilitarian social welfare function.

We can also come up with intermediate versions, that are more egalitarian than the utilitarian social welfare function but less so than the maximin. One example is the product of individuals' welfare. While we can debate the merits of various social welfare functions, I am not going to concern myself with this choice except to ask that it be explicit and meet the few minimal conditions I have mentioned.

I should note before moving on that there are many very difficult problems with this formulation of what makes a good society. For example, we must decide whether to count hateful preferences in social welfare – if someone is happy when another is injured, do we count that perverse happiness? We also have to decide who is included. Do we count foreigners? What about embryos or animals? There is a whole literature devoted to studying these problems. This is a talk about law and economics, not philosophy, so I will ignore these problems here. I will assume that we have a social welfare function and get on with the analysis.

Once we have had our ethical debates and chosen a social welfare function, we can think fairly clearly about redistribution. It actually becomes a mathematical problem. We want to maximize social welfare given constraints about the costs of redistribution, and we can solve for the optimal system.

The original work along these lines was done by James Mirrlees in 1971, and he was later awarded the Nobel Prize in part for this work.[3] The actual mathematics are very complex and of little interest to the nonspecialist. It might be helpful, however, to demonstrate the principles with a simple example because the discussion so far has been somewhat abstract. An article by Joe Bankman and Tom Griffith has an example that serves well for our purposes.[4]

Suppose we have three individuals in a hypothetical society. (Obviously in a real society, there are more than three individuals. We can think of the three as three representative classes of individuals in a more realistic society.) Their wage rates are as indicated in the table.

| *Individual* | *Wage Rate* |
|---|---|
| Alice | $10/hour |
| Betty | $20/hour |
| Cindy | $40/hour |

I will also assume that they have a utility function that combines both their consumption and their time off from work, or leisure. In particular, I am going to assume that their utility is the log of the product of consumption and leisure, or:

$$\text{Utility} = \text{Log}\,[\text{consumption} \bullet \text{leisure}]$$

The reason I use the log function is that it goes up but at a declining rate, which gives us declining marginal utility. I use the product of consumption and leisure so that individuals will want to balance the two – both count and if either is too low utility will decline. For example, if the individual is a beachcomber and has only leisure and no consumption, utility will be low. Similarly, if the individual is a workaholic and has consumption but no leisure, utility will decline. Our individuals want a mix of free-time and wealth, like most individuals that I know. Note also that the utility function gives us implicitly the labor/leisure distortion because it determines how much individuals will reduce work when they are taxed. It tells us their trade-off between work and leisure.

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[3]James Mirrlees, An Exploration in the Theory of Optimum Income Taxation, 38 Rev. Econ. Stud. 175 (1971).

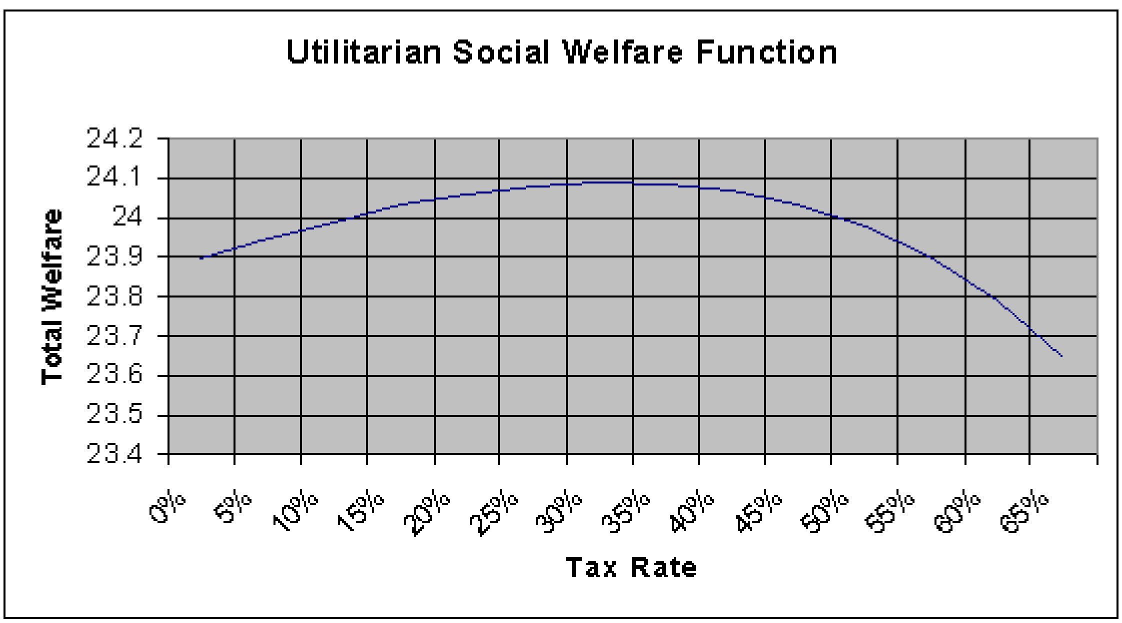
[4]See Joe Bankman and Thomas Griffith, Social Welfare and the Rate Structure: A New Look at Progressive Taxation, 75 Cal. L. Rev. 1905 (1987). This article also has an excellent summary of welfarist and nonwelfarist theories of redistribution and of the data as of 1987 concerning the efficiency effects of redistribution.

Given this society, we can set a tax rate or rates to raise revenue. I will assume that we set a single rate on everyone and use the money raised to pay for a public good that benefits all equally. We can think of this as simply giving them back money – the public good counts as consumption in their utility functions. This system is progressive because they pay in based on a percent of income, so Cindy pays more than the others, but they all get back the same amount. We can do the calculation with more complex tax structures but it just makes it more complicated without changing the basic ideas.

Given this tax and spending system, we calculate how much each one works and their utility for any given tax rate. We then plug this into our social welfare function and determine overall social welfare. The problem is to find the tax rate that maximizes social welfare.

I won't bore you with the mathematics of the solution – in this simple example, the math is fairly straightforward but in more realistic cases the math can be formidable. But I've calculated social welfare for the utilitarian and Rawlsian social welfare functions.

Here is the utilitarian case. On the y-axis we have the sum of utilities. On the x-axis we have the tax rate. So the graph shows how total social welfare, the sum of utilities, varies with the tax rate. From examination of the graph, we can see that social welfare is maximized when the tax rate is approximately 31%.

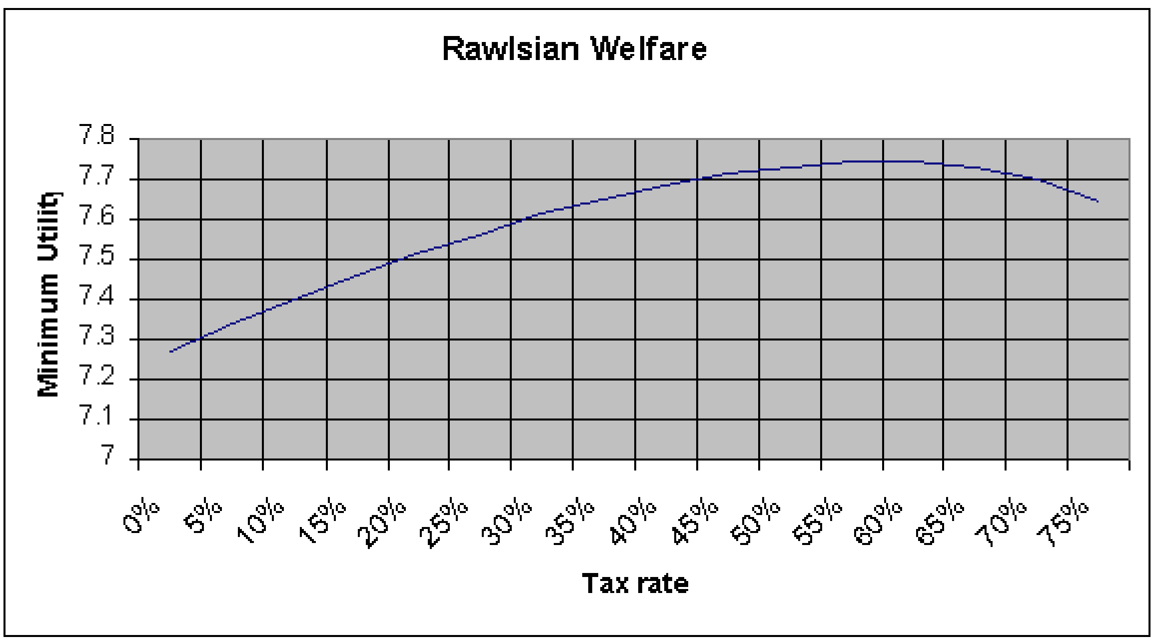



Here are the income and welfare numbers at the optimum. We can see that even at the optimum, our sample society is not completely equal – not even close. The wealthiest individual, Cindy, has more than three times as much income as the poorest and is better of in terms of utility as well. Notwithstanding this inequality, further redistribution would be a mistake because it would reduce total utility.

**Optimum with Utilitarian Social Welfare Function**

| | *Income* | *Utility* |
|---|---|---|
| Alice | $118 | 7.61 |
| Betty | $201 | 7.98 |
| Cindy | $366 | 8.49 |
| Total | $686 | 24.08 |

Here is the same society, but using a Rawlsian social welfare function. Note the change to the graph. Previously we had total utility on the y-axis. Now the y-axis has the utility of the worst off individual. The optimal tax rate has gone up to somewhere around 60%.




Here are the income and welfare numbers at this optimum. The numbers are more equal – the best off now has only two and one half times the wealth of the worst off. But there is still substantial inequality in both income and utility. Cindy is still much better off than Alice. Note also that total wealth and total utility went down. For example, total wealth went down from $686 under utilitarianism to $480 under the minimax. We have traded off these totals for more equality.

**Optimum with Rawlsian Social Welfare Function**

| | *Income* | *Utility* |
|---|---|---|
| Alice | $96 | 7.74 |
| Betty | $144 | 7.86 |
| Cindy | $240 | 8.19 |
| Total | $480 | 23.79 |

Why would a Rawlsian social welfare function leave us with this sort of inequality when it cares only about the welfare of the poorest? Why wouldn't it tell us to have more redistribution? The reason is that we cannot help the worst off any more – raising the tax rate to transfer more to her actually makes her worse off because the extra taxes she has to pay and the reduction in the amount we redistribute to her because the efficiency losses from taxation. The pie shrinks so much, the efficiency losses are so high, that we cannot do any better.

Is this an artifact of our limited tax structure? We are limiting ourselves to a single tax rate, so raising Cindy's taxes also raises Alice's taxes. It is hard in this structure to take from Cindy without hurting Alice. The answer, it turns out, is not very much dependent on our limited model. Even under quite general tax structures there is still substantial inequality with a Rawlsian social welfare function. The leaky bucket remains very important.

That's the background. The core idea is that redistribution of income is probably a good thing. It most likely increases social welfare. Unfortunately, redistribution creates inefficiencies, such as the distortion in the choice between labor and leisure. Redistribution is a leaky bucket. Therefore, we have to trade the benefits of redistribution with its efficiency costs, and we end up with some desirable amount of redistribution that may leave us far from equal We are now finally ready to discuss the main topic, which is whether legal rules should be used to redistribute income. I want to compare legal rules to the tax system as methods of redistributing income.

## II. The Legal System Compared to the Tax System as a Method of Redistributing Income

Suppose we have a legal rule and a tax system that have similar redistributive effects. They both, for example, take similar amounts from those with high income and give to those with low incomes. Which one do we prefer?[5]

[5]The argument made here is primarily due to Louis Kaplow and Steven Shavell, Why the Legal System is Less Efficient than the Income Tax in Redistributing Income, 23 J. Legal

Consider a legal rule that redistributes income by varying from the efficient result. The legal rule redistributes income, which is good. It also creates inefficiencies. Because it redistributes, it reduces the return from working, and, therefore, it causes labor/leisure distortions. But, and this is the key fact, it also deviates from the efficient legal rule, so it causes inefficiencies along that boundary as well. It will cause individuals to take too much or too little care, breach contracts inappropriately, under or over invest in property, and so on. The legal rule affects two margins: the decision to work and the decisions relevant to the legal rule.

Compare that to an income tax. It too causes a labor/leisure distortion. We have the same disincentives to work. But it does not cause inefficiencies along other margins. It will not change incentives to take care, incentives to breach, and so forth. This means we can get the same redistribution at a lower cost. Or we can get more redistribution at the same cost. But either way, the tax system is a more efficient method of redistributing than the legal rule.

That, in a nutshell, is the main argument. We can develop the intuition further by stating the argument slightly differently. Suppose we are considering a legal rule that favors the poor. Say we deviate from efficient tort damages so as to redistribute toward the poor. The wealthy in this case will expect to pay more or receive less in tort and there is a corresponding benefit to the poor. Suppose instead we make the legal rule efficient and adjust the tax system to redistribute the same amount by increasing its progressivity. By making this adjustment, we have identical distributional consequences. The wealthy pay more and the poor receive more. There are, therefore, identical benefits from redistribution and also identical distortions of the labor/leisure choice. But we have increased the efficiency of the tort system, because now we resort back to efficient tort rules. So we are better off.

In fact, strong versions of this argument claim we have made a Pareto improvement – we have redistributed in exactly the same way by using the tax system but increased total resources because the tort system is more efficient. The argument is consistent with *any* of the social welfare functions we might pick, regardless of how egalitarian we might be. Therefore, we get our conclusion: the income tax is the better instrument for redistribution and legal rules should, therefore, not be so used.

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Studies 667 (1994). For additional discussion, see, Chris Sanchirico, Taxes versus Legal Rules as Instruments for Equity: A More Equitable View, 29 J. Legal Studies 797 (2000); Louis Kaplow and Steven Shavell, Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistributing Income, 29 J. Legal Studies 821 (2000); and Chris Sanchirico, Deconstructing the New Efficiency Rationale, 86 Cornell L. Rev. 1003 (2001).

The argument is a comparative argument. We consider equivalent redistribution accomplished through two different methods, tax and legal rules. The tax system will be a better method. I think the argument, as it is, is fairly compelling. But we can actually go further in the comparison. The argument I just made assumed that legal rules were actually able to redistribute income fairly well and merely argued that the tax system would do better. But there are separate reasons to believe that the legal system is often an ineffective instrument for redistributing income at all. These arguments go under the rubrics of "contracting around" and "haphazardness."

The contracting around argument states that attempts to redistribute through legal rules will often be defeated because prices will adjust to offset the effect of the legal rule. For example, if we require landlords to make their apartments habitable through an implied warranty of habitability, landlords will simply raise the rent to cover their costs.

The initial story seems quite intuitive here. We can examine the extent to which prices change in various markets and therefore when the effects of legal rules get passed on. Sometimes prices might not rise so legal rules work might seem to work.

When one digs further into this argument, however, it turns out to be very messy and much less favorable to the use of legal rules for redistributing income than we might have initially thought. The core problem is that legal rules change the very product under consideration. For example, a mandated warranty changes the good being sold from simply a good to a good plus a warranty. Buyers will value the benefit of the warranty, perhaps more or perhaps less than its cost. The extent to which prices change reflects how much buyers value the warranty. If they value it highly, we might expect them to agree to pay a lot more for the product with the warranty. And if they do not value it at all, they may not be willing to pay more. Therefore, the extent of the price change is misleading. A big price increase (relative to the cost of the legal rule) might indicate that the legal rule has made buyers better off, while a small price increase might indicate that the legal rule has made buyers worse off. The intuition should be completely flipped from what we might have first thought.[6]

To make it messier, individuals will value the warranty differently, with some valuing the benefit of the legal rule more than its cost and others thinking otherwise. When prices adjust, there will be redistribution among consumers. If our goal was, say, to redistribute from sellers to purchasers or landlord to tenants, we might instead have mostly redistributed among purchasers or among tenants. It is not even clear what it means to have pro-tenant or pro-consumer rules in this case. Sorting out the actual effects becomes very difficult. The theoretical questions are hard and the empirical questions are probably even more difficult.

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[6]For a more complete analysis, see, Richard Craswell, Passing on the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships, 43 Stanford L. Rev. 299 (1991). See also, Henry Smith, Ambiguous Quality Changes from Taxes and Legal Rules, 67 Chicago L. Rev. 647 (2000).

For example, we are not entirely sure whether labor laws help workers as a whole – they might, for example, help workers who are employed but make finding work more difficult for those who are unemployed. Similarly, it is not clear that consumer protection laws help consumers. I don't want to take a position on this – there is a large literature on these various rules – some probably help their intended beneficiaries and some probably do not. The only point is that attempting to redistribute income through legal rules is a precarious exercise.

The other standard argument against using legal rules is known as the haphazardness problem. Consider a pro-plaintiff tort rule. We might want such a rule because, say, plaintiffs are systematically poorer than defendants. The problem with such an approach is that it is likely to be both under- and over inclusive. It is under inclusive because many poor individuals are never part of a tort suit so they would not benefit from the rule. Similarly, the rule is over inclusive because there will inevitably be some rich plaintiffs who benefit.

Once again, like in the contracting around case, the argument gets much more complex once we get into the details. For example, even if people are never subject to a lawsuit, they might bargain in the shadow of the law and, therefore, receive benefits or detriments indirectly. Similarly, in the tort case, insurance prices will be based on expected damages, so to the extent individuals buy insurance, they are all affected even if they are never party to a lawsuit.

Before drawing any conclusions about the strength of the contracting-around and haphazardness arguments, we must compare the legal system to the tax system. The argument must always be a comparative argument – it does't help to criticize one method of redistribution without comparing it to other methods. The tax system might very well be subject to the same criticisms as the legal system. Prices might adjust to undo the effect of tax redistribution and the tax system might be over- and under-broad, taxing the wrong people sometimes and missing the right people other times.

While these criticisms of the tax system are undoubtably true, I tend to think that they are likely to be less severe in the tax system than in the legal system. The reason is that the tax system is a dedicated system that can be tailored and designed to minimize these effects. But there is no a priori or slam-dunk argument that tells us this will happen. We have to do a detailed institutional comparison. Still, my initial view is that it is extremely unlikely that the legal system would compare well.

Taking these arguments altogether, the double distortion argument and the problems with contracting around and haphazardness, I believe the case against using legal rules to redistribute to the poor becomes almost overwhelming. The tax system is a dedicated system designed to measure the variables relevant to redistribution and act only on those margins. It is hard to imagine that legal rules are likely to do a better job.

One key point to note is that I have not argued that legal rules should be efficient. All the argument has shown so far is that legal rules should not be used to redistribute income. But income is not the only source of inequality. Race, gender, disability, or health all might be sources of inequality in our society. If we value equality of all sorts not just income equality, we might want to redistribute based on other sources of inequality.

Maybe legal rules should be used to redistribute on other grounds and, therefore, should not be efficient, even if they should not be used to redistribute income. Here is an example. Suppose the severely disabled are less well off than others of equal income. Their costs may be higher, their needs greater, and so on.

An income tax won't help much here. Income won't necessarily correspond to disability. We can even imagine the case where everyone has the same income but differ along this dimension. Then an income tax would have nothing to do even though there is inequality in our society.

Legal rules, however, might help. We could adjust the legal rules to favor the disabled and thereby redistribute away from everyone else and to the disabled. For example, we could, as we actually do in real life, impose a mandate on employers that they provide accommodations for the disabled to allow them to work.

Nothing in the argument so far tells us not to do this. The income-tax-only argument is only about income redistribution. It does not tell us that legal rules should not be adjusted to favor nonincome sources of inequality. That is, we need to distinguish between an argument for efficient legal rules, which I have *not* made, from an argument that legal rules should not be used to redistribute income.

Note in the disabilities case, legal rules might seem to favor the poor. If the disabled are systematically poorer than others and legal rules favor the disabled, then legal rules favor the poor. But this could easily have gone the other way. If the less well off class happens to be wealthier than others (the idea might be that they are less well off at any *given* level of wealth even though they tend to have more wealth) then the adjustment would favor the rich. Another way to phrase this point is that if we think of the income tax as the best tool for handling distribution between income classes, we should think of other types of redistribution as working within an income class. Accommodation mandates for the disabled can be thought of as redistributing between individuals with the same income but with and without disabilities.

While the arguments I have made so far only concerned income and left room for this type of redistribution, we should not jump to the conclusion that legal rules are a good method of redistributing on this basis. The arguments about income redistribution might very well translate to redistribution on other bases.

For example, much has been written about whether rules that appear to help a given class, such as the disabled, really do – this is the contracting around argument. There is literature indicating that the disabilities law helped the disabled who already had jobs but hurt those who are seeking jobs. This means that it might primarily redistribute within the class of disabled rather than from the healthy to the disabled.

Haphazardness is also a serious problem – the disabilities law seems to be both over broad and too narrow. It might apply to individuals who are not really worse off because of their disabilities and does not apply to the seriously disabled who are completely unable to work.

Finally, a version of the double distortion argument also might translate to this case. Suppose we compare a direct redistribution of money to the disabled with a modification to legal rules to help the disabled. Direct redistribution would have the same redistributive benefits and costs but would not skew employment relationships. Legal rules skew employment relationships. Thus, direct redistribution may be superior to legal rules.

I don't want to condemn the various disabilities laws without serious and focused analysis of those rules. There may be much to be said for them. There are really only two points I am trying to make. First, the analysis about whether legal rules should favor the poor leaves room for this sort of redistribution. The primary argument I have made is not an argument for efficiency. It is an argument against using legal rules to redistribute income. But second, the analysis about whether legal rules should favor the poor suggests parallel analysis for whether legal rules should redistribute on other bases that should make us very leery of such redistribution. There are good reasons to think that legal rules should be efficient and not redistribute at all.

That is the basic argument. Let me mention three potential counter arguments. First, a common criticism of the arguments I have made is that adjustments to the tax system are not feasible. Just because we identify a social problem, say inadequate housing, doesn't mean that the tax system will be adjusted to resolve it.

This argument is correct to some extent. If the tax system is unavailable, we would want to resort to the next best alternative. If our only alternative is legal rules, we may want to use them. But there is no particular reason to believe that legal rules will be more available than taxes. The tax system is adjusted all the time – it is famous for constantly changing. Moreover, the extent of redistribution is a constant topic of discussion, so much so that many observers complain that it dominates discussion to the exclusion of other considerations. Think how much you have heard about whether the Bush tax cuts help the rich too much.

Moreover, if some political coalition would block additional redistribution through the tax system, there is no reason to believe it would not block the same redistribution when done indirectly through legal rules. It might fight even harder against legal rules because of the additional costs imposed by the inefficiencies.

Maybe using legal rules gets around these coalition problems because courts can make decisions about redistribution using legal rules, and courts are largely outside the political process. But one needs a complex view of the appropriate roles of courts and legislatures to argue that if redistribution cannot be passed through the democratic process that it should occur in a more expensive manner through courts.

The feasibility intuition is very strong among lawyers. I'm not sure exactly why – perhaps because lawyers are focused on legal rules so they consider them more malleable than the tax system. Perhaps it is because lawyers tend to see what looks like an immediate injustice in a given case without thinking systematically about the problem. On close examination, it has little force.

Second, the tax system is a mess. While using legal rules has problems, the tax system is riven with loopholes, it is costly to administer, and it is byzantine in its complexity. It is not the efficient and sleek method of redistribution portrayed so far. How can I defend such a monstrosity?

I don't intend to defend the income tax from these attacks. I make them myself all the time. But there is no reason to believe that other broad-based redistributive systems would be any better along these grounds and they could easily be much worse. All the problems that lead to loopholes and complexity in the income tax would pervade any alternative attempt to measure and redistribute income.

A final point is that people might respond differently to redistribution through the tax system than through legal rules.[7] For example, people might notice the redistribution through the legal rules less and, therefore, redistribution through legal rules might distort work incentives less. To make this slightly more formal, suppose that legal rules apply only infrequently, so that there is a low probability of them applying. A common claim about humans is that they underestimate infrequent events. If this is true in this case, people may systematically underestimate the redistribution through legal rules and, therefore, not adjust their labor/leisure choice.

We can't know the truth of this claim without more investigation. I have been assuming that people respond to real incentives, that there are no systematic, longstanding illusions. If there are such illusions, there might be many opportunities to take advantage of them, not just with respect to redistribution. I would think, however, that to the extent there is any significant redistribution, it would be difficult to retain illusions of this sort.

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[7]See, e.g., Christine Jolls, Behavioral Economics Analysis of Redistributive Legal Rules, 51 Vand. L. Rev. 1653 (1998).

In addition, if insurance is available so that the legal rule applies through insurance prices, it is much more difficult to tell a story that involves systematic bias. And if we are relying on lack of insurance, so that legal rules apply only probabilistically, haphazardness becomes a serious problem. Therefore, I do not think arguments of this sort get us very far.

## III. Conclusion

My conclusion is quite simple: legal rules should not be used to redistribute income. Let me give a slightly softer conclusion as well. Even if one rejects some of the particulars of the argument – and you should know that there is literature that does[8] – the central place of the tax system in thinking about the appropriate goals for legal rules cannot be denied. That is, even if there is some scope for redistribution of income through legal rules in certain contexts, the existence of the tax system very much narrows it. We would have to think completely differently about legal rules if we did not have the tax system or other broad-based redistributive systems.

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[8]See, e.g., Sanchirico, note 5.

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