TAXING WEALTH: POLICY CHALLENGES AND RECENT DEBATES

ECFIN Taxation Workshop

November 13, 2014

Outline

- Context
- Capital income and/or capital taxes?
- Differentiating across assets?
- Tax competition and EOI

Context

Revival of interest

- Marked increase in income inequality—especially at very top—and in wealth-income ratios
  - Cannot “leave equity objectives to spending side”
- Increased, post-crisis perception of unfairness
  - Bail outs, bonuses, tax avoidance/evasion for some…
  - Austerity for others
- Recognition redistribution may help growth
- Revenue!

Instruments—Recurrent wealth tax

- Rationale?

—To address non-income benefits associated with high *K*?

—*K* adds information to income/consumption/bequests?

- Gross or net?
  - Net closer to ability to pay, but avoidance possibilities if some assets untaxed
- All assets or subset?
  - E.g. property taxes (real estate, cars..); Benefit tax aspect
  - Land

Instruments—Some others

Non-recurrent (capital levy)

– Alternative to default; but few successful examples

Non-market transfers

- Estate/accessions—gift tax as corollary

—motive matters—unintended bequests (up to 100%) vs. warm glow (subsidy?

Market transfers

- Stamp duties, FTT

—Convenient! Stability?

Also…

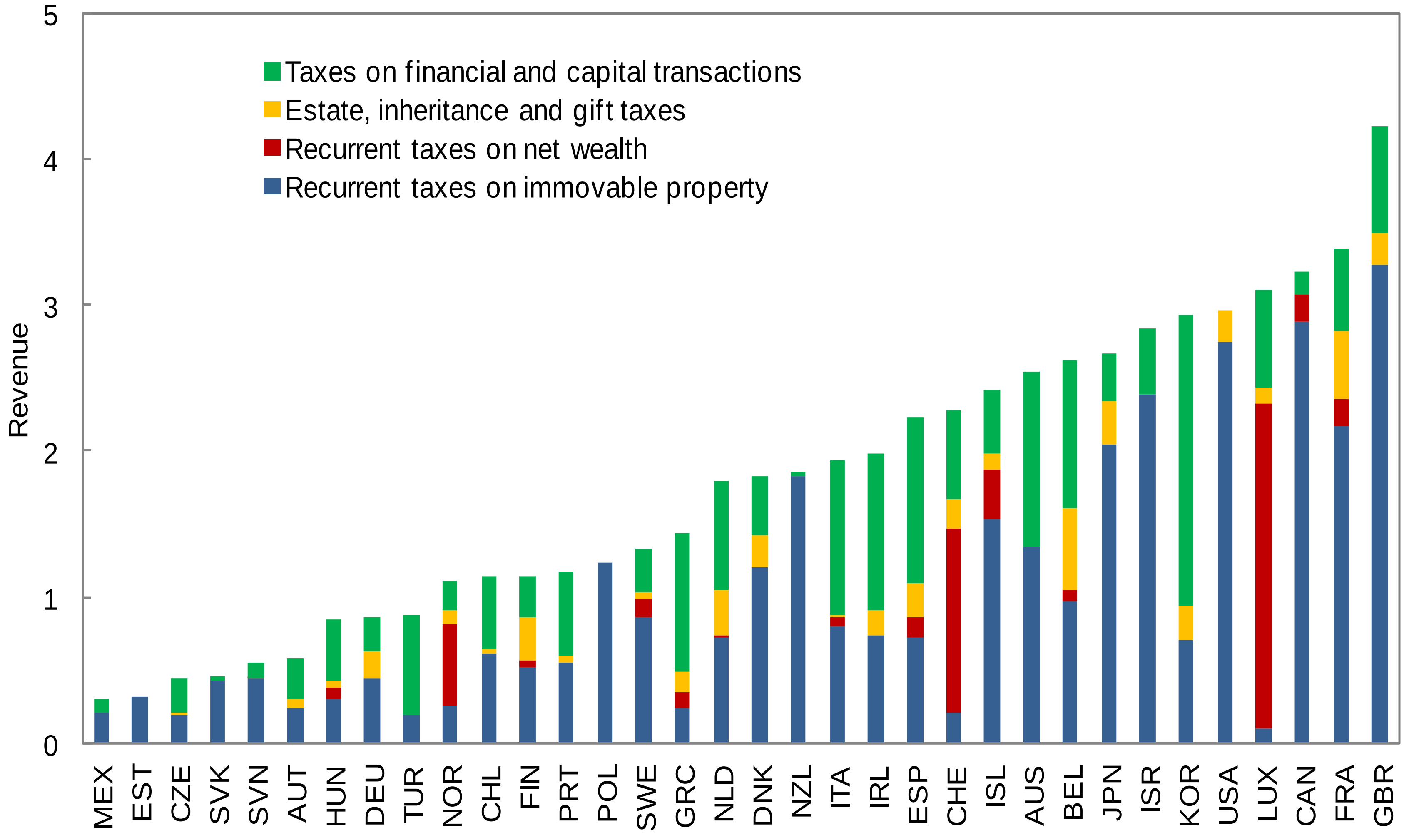
Links with other taxes:

- Capital gains tax (realization events)
- And capital income taxation more generally
- And income tax more generally
  - E.g. comprehensive vs. dual income tax
- Looking ahead: income taxation conditional on assets?

Incidence issues

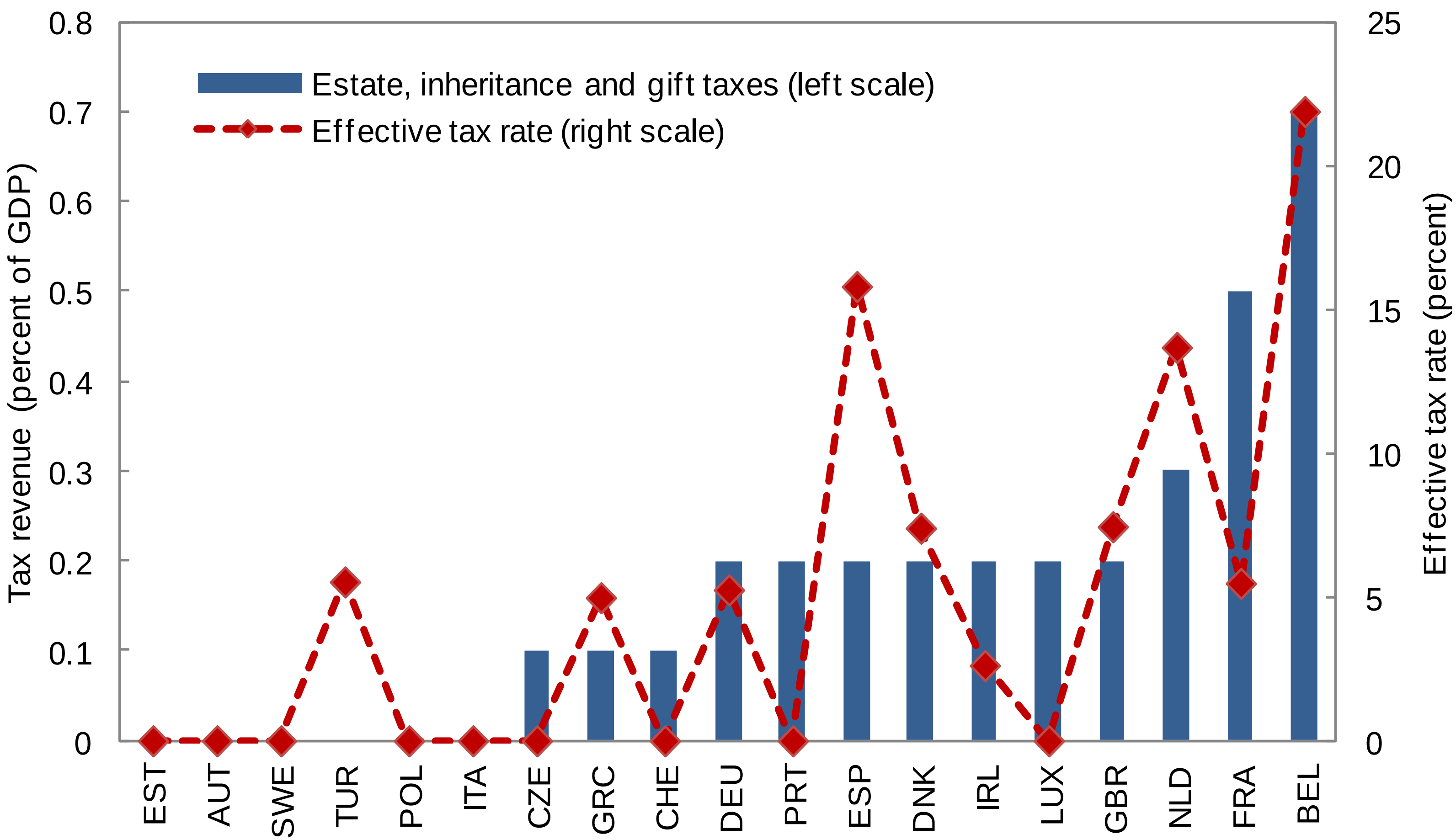
- Little discussed in this literature

Current state (2000-12)



Source: OECD Revenue Statistics

Estate, inheritance and gift taxes



<u>Source</u>: Calculations described in October 20i3 Fiscal Monitor

Recurrent wealth taxes

- Demise
  - Removal in Canada, Sweden, Australia, Pakistan… (but France, Norway, Switzerland…)
  - Reflecting
    - Tax competition
    - “Healthy, wealthy and well-advised” manage to escape
- But some revival? Spain, Iceland
  - Still (increasingly?) implicit in ‘standard of life’ checks
- Historically, a major tax base—What happened?

Capital income and/or capital taxes?

Equivalence relation

Taxing wealth at rate T_K has same effect as taxing capital income at T_R if

$$(1-T_K)(1+R) = 1+(1-T_R)R$$

which requires $T_R = T_K(1+R)/R$; with implication that a 'low' T_K capital tax is equivalent to 'high' T_R

—E.g. With $R = 5\%$, $T_K = 1\%$ equivalent to $T_R = 21\%$

(Similar for non-linear taxes)

Differences—Conceptual (1)

- If rates of return vary, a uniform T_R does not imply a uniform tax on capital
  - Regressive in K if richer earn systematically higher R
- With notional return would be proportional (in K)
  - Dutch scheme
- In principle, imputed rate could vary with capital holdings—equivalent to progressive capital tax

Differences—Conceptual (2)

- Treatment of losses
  - Liability with loss zero/negative tax under t_K; remains positive under t_K

  A timing issue, but differing volatility and automatic stabilization properties may matter

- Distinguishing capital and labor incomes and values an issue for both
  - Except not present under comprehensive income tax

Differences—Practical (1)

- Withholding/3rd party reporting well developed for at least some forms of capital income
  - May, inter alia, reduce resistance (cf. estate tax)?

  Same tools could in principle apply to stocks

- Unrealized capital gains problematic for T_R…
  - Though there are schemes to address this

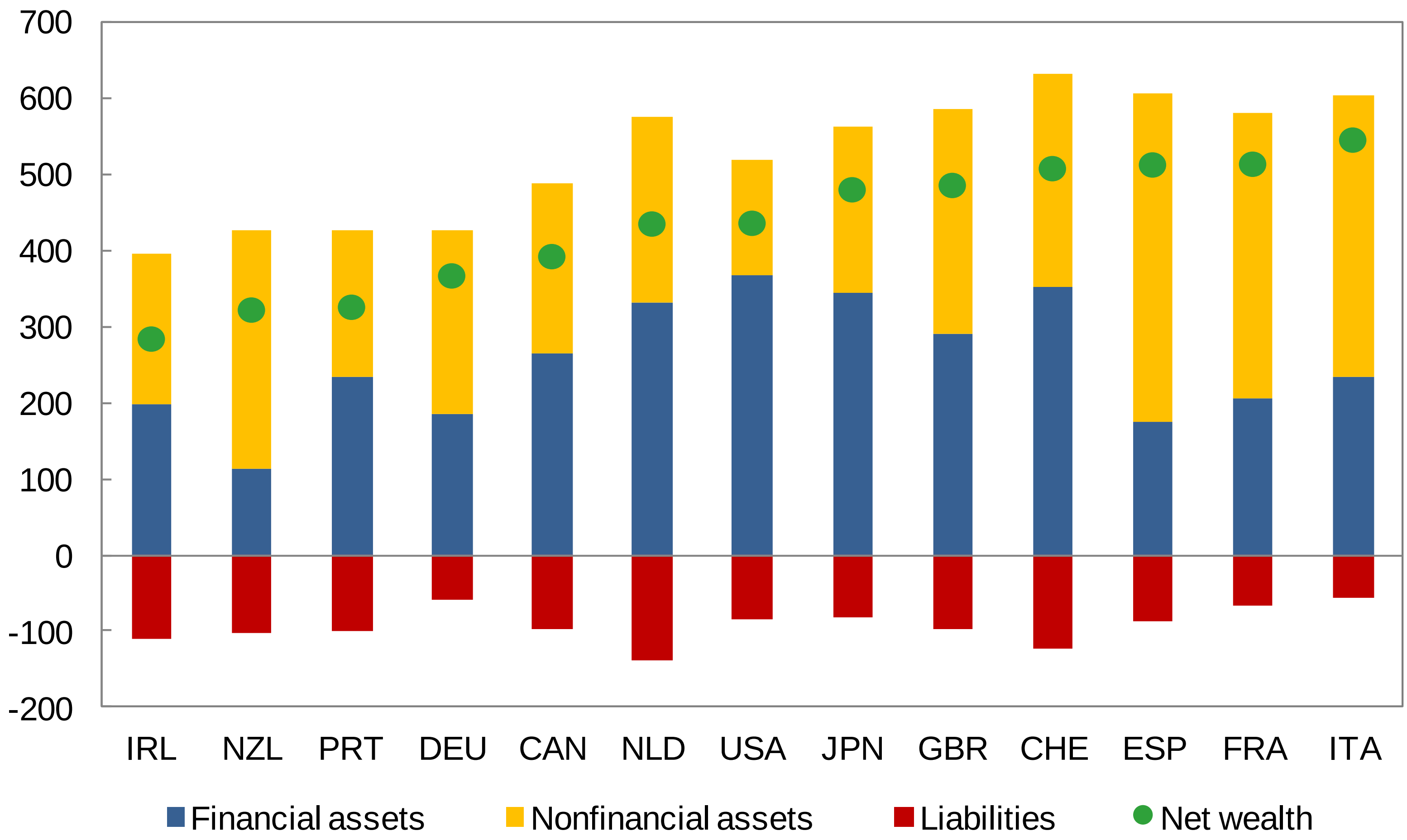
  …less so for T_K if asset can be valued (though then could also tax the gain)

Differences—Practical (2)

- Non-cash asset returns—e.g. owner-occupation
  - less of an issue for T_K if asset can be valued, though in that case could also impute a return
- Has T_R proved more robust against exemptions/special treatment than T_K?
- Merits in greater familiarity with T_R?

Differentiating across assets?

Non-financial assets are important

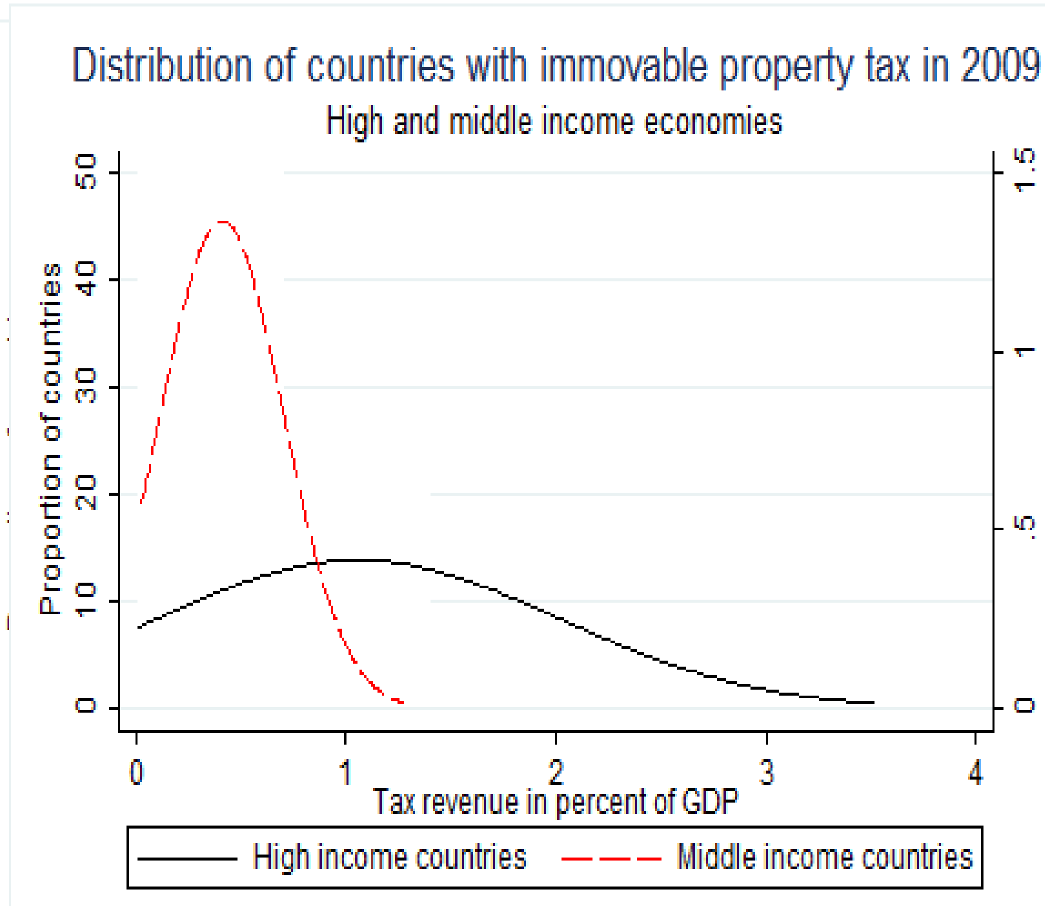


Assets in percent of GDP. Source: Fiscal Monitor October 2013

Recurrent taxes on immovable property

- Scope to do more:

- Top of hierarchy of relatively growth-friendly taxes



Source: Fiscal Monitor October 2013

Reasons to differentiate?

In terms of ability to pay, no

- Except if concerned by liquidity considerations

But possible reasons:

- Discourage some positions: e.g. debt
  - But better may be to address e.g. interest deductibility
- Wealth inequality may be mainly from a few assets
- With less than full cooperation, tax more mobile assets less heavily?
  - Which would likely mean more use of property taxation

With some challenges

- Building capacity—cadastre, valuation—can be expensive and time consuming
- Keeping (relative) valuations up to date
- Retain as marginal source local government finance—benefit principle at margin?
- What role for taxes on non-residential real estate?

Tax competition and EOI

International tax competition

Much blamed for decay of taxes on *K*/*K* income:

- Downward spiral in ‘source’ taxation (whatever that is…)
- Concealment: $4.5 trillion in havens (Zucman, 2013)

Exchange of information (EOI) can help enforce of residence-based taxes—and world is changing…

- EU Savings Directive, FATCA, AEOI as new global standard

…in a hugely important and positive way

Limits?

- Gains from cooperation—but maybe bigger gains from remaining outside
  - Money may flow to non-participating jurisdictions: Johannesen and Zucman (2013)
  - Value of remaining a haven increases as others close: Elsayyad and Konrad (2012)

- Personal mobility
  - Inversions a warning
  - Non-doms
  - Link to citizenship? Can be (and is) renounced
  - Exit charges (EU issues?)