Resistance to reforming property taxes

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- Resistance: difficult topic & differs among countries. And resistance of whom?
  economists (non consensus); people (aging; my sweet home & family);
  lobbying of the rich; local government; 'politics' (popularity, ideology)
- Propositions: 'deals' (*donnant-donnant*)
  tax hikes but compensations in exchange

Outline

- An unfavorable social & wealth context (to remedy)
- ‘Current economic arguments’ (conventional view: Arnold *et al.*, 2011) & recurrent taxes on immovable property
  - Resistances
- Other taxes on household wealth (French economists)
  - Annual wealth tax, comprehensive income tax, capital gains
- Taxation of wealth transfers
  - Resistances
- Propositions: ‘deals’

Wealth context (Europe / Eurozone)

- See M. Keen (2015) & D. Bradbury (2015), from last workshop
  - Rising income inequality (immob.) & wealth concentration (at the top): 1970-80+
  - Rising wealth-income & capital-output ratios to unprecedented levels (since 1914)
    - Rising wealth => ability to pay. But mainly (latent) capital gains on housing (France)
    - Germany = outlier: no housing bubble, limited rate of homeownership, less rich…
  - Globalization & international tax competition (AEOI beginning, but difficult)
  - ➢ Efficiency: little distortions + ‘growth friendly’, revenue raising
  - ➢ Equity… + simplicity & compliance
- 2 other simultaneous phenomena other than such ‘patrimonialization’
  - Slowdown of growth: 30 ‘piteous’ years (1978-2007) & 2008 economic crisis
    - A growing feeling that growth may not come back that quickly (not a ‘crisis’)
  - Rising longevity (new & underestimated)
    - + low fertility in a number of countries, but not in France

Other elements of context: rising longevity

- Rising longevity => more old days to secure
  - Retire later: at which labor conditions & <u>wage</u>, when a senior (seniority rules)?
  - Inheritance (France) is received in <u>full property</u> as late as 60 on average
    - Also increasing rights of the surviving spouse. Average age was 40 in the 1960's
- Social transfers (France): today, same amounts under & above 60
  - Above 60 receive in % of GDP their weight in the population: unsustainable?
    - Unwritten historical rule: 6% in 1950, 20% in 2010, almost 30% in 2030?
    - ➢ Due to rising longevity + Baby-boom + women in the labor force (backlash)
  - French projections say <u>no</u>: retirement system balanced in the long run?
    - But rosy scenario, mean age of retirement higher + retirees'− relative − PP lower
  - *Per capita* transfers ratio by age (above 60/ under 60) constant: 1980->
    - <u>A pure demographic effect</u>: in a way, generational equity today
    - Problem of sustainability today leads to problem of generational equity <u>tomorrow</u>
  - ➢ Financing our social model, esp. for <u>future</u> retirees (− 20% in relative terms)

Other elements of context: low growth & rising uncertainty

- Financial sustainability of the Welfare State: a <u>global</u> issue
  - Not only pensions but also health & long-term care: rising needs
  - And education-training = a key factor of economic growth today
- ‘Ricardian’ circuit of transfers: importance has <u>doubled</u> in % of GDP during the last 30 years (France) => Piketty (2013)
  - Upward public transfers (to above 60): <u>x 2,1</u>; downward wealth transfers: <u>x1,9</u>
  - Ratio B/A (bequests to net wealth) has risen by 20% in France (not in the US)
  - ➢ Bequests: an ideal tax base for an unearned income (meritocratic view)
- Wealth more and more in the hands of the elderly (France: 1986-2010)
  - Elderly: savings = <u>low-risk reserve</u> (quasi-liquidities, homes, insurance contract)
  - Savings kept from age 60 to 90 & then transmitted to 60 years old children
  - ➢ Children are liquidity-constrained: <u>early *inter-vivos* transfers</u> ease their plans to buy housing or start up a business => Arrondel-Garbinti-Masson (2014) for France
    - ➢ <u>Relative</u> tax advantage to gifts over post-mortem bequests (positive responses)

To sum up: this unfavorable social & wealth context

- Not simply redistribution & inequality (-mobility) issues as such
- Puts high pressure on the financing of our social model
  - Both for the young & old: to foster growth & reduce inequality-poverty
  - Rise in inequality between generations if public & social debts not sustainable
- Call for <u>remedies</u> to a damaging wealth situation
  - Tax more the wealth of the rich
  - Tax more wealth transfers, whose weight & inequality are rising
  - Increase downward mobility of wealth in favor of liquidity-constrained young (<u>relative</u> tax advantages to gifts) & decrease ‘oversaving’ of senior households
  - Give incentives to long-term (financial) risky investments, fostering growth
- French wealth situation: <u>the nearest to the mean</u> in the Eurozone
  - Mean, median wealth, age profile, inequality (top 1%, 10%), wealth composition
    - A bit less homes & professional assets, stronger housing bubble, & more unequal stocks: among top 5%, 55% own stocks in the Eurozone, 63% in France

Current economic arguments (CEA) on (household) taxation:

Somewhat caricatured

- Labour income tax (increase): not favorable (esp. for the young)
  - Massive unemployment, high labor costs, decreasing labour/output ratio
- Annual wealth tax, (net?) market value, comprehensive: not favorable
  - Asking too much: large tax base, permanent asset reevaluation, <u>strong international cooperation</u> => rare & (still) utopian + innovative top 1% (Aghion)
- One-time capital levy (to reduce public debt): difficult
- Wealth transfer tax (renovated, my dream): too unpopular, vanishing
- Tax on capital gains (realized, at death, latent) & income: perhaps (?)
- Recurrent taxes on immovable property (housing-land): <u>YES!</u>
  - Shift from transaction tax to increased recurrent property tax (also imputed rent)
  - Limit relief on mortgage (interest) payments: risk of excessive household debt
  - Growth-friendly: recurrent property tax, consumption tax, first (Arnold *et al.*)

CEA and transaction property tax

- CEA, first concerned by:
  - Globalization (mobile capital) puts a lot of limits to (realistic) tax reforms
  - Economic crisis: public debt, household indebtedness, need for tax revenue
  - International tax harmonization & practical: if a tax rare in Europe, forget about it
  - <u>Some</u> French economists at least do not really share these views (see below)
    - Globalization is important but not an excuse
    - Household indebtedness is not such a major issue
    - Innovations, new taxes are welcome, even in one country alone
- Reduce transaction taxes on housing: economists' consensus
  - Leads to a more dynamic housing market & to a drop in housing prices
  - Facilitate professional mobility, etc. (but too favorable to housing investment)
- But strong resistance from <u>local government</u>
  - … which receives the tax revenue. And rich communities receive more…
  - Reform of local taxation requiring <u>national cooperation</u>?

Resistance to (increased) recurrent property tax (1)

- Increase recurrent property tax
  - Little distortions, immovable property, growth friendly, etc.
  - But low (and decreasing) in Europe, with strong heterogeneity
  - A key problem: periodic reassessment to market values
  - ➢ Call for upward harmonization? And France, the model?!
- Resistance: <u>some</u> French economists

  Piketty-Saez-Zucman – PSZ – (2013); Allègre-Plane-Timbeau – OFCE – (2012)
  - PSZ prefer a comprehensive wealth tax on <u>net</u> market value (household debt?)
  - Difficulty to reassess the market value of homes (was planned every 5 years in France) => require a complicated <u>national cooperation</u>
  - Capital losses on housing: double loss. Or reversible tax (may decrease)?
  - France far from ideal (& international harmonization not a key issue there)
    - Complaints by many about the too high level of (housing & real property) taxes
    - Strong inequalities & injustices: low tax in the center of big towns, high in suburbs; no reevaluation (or else sudden tax hikes, especially for land tax)
    - Archaic tax & rich pay little in rich communities, poor pay a lot in poor communities

Resistance to (increased) recurrent property tax (2)

- People: problems of transition
  - For the same housing service, property tax multiplied by 3 or 4! (e.g. in posh quarters in Paris), for people who do not plan to sell (just latent capital gains)
    - And even more if the tax is made progressive for equity reasons!
    - While maintenance costs have increased a lot in posh quarters
    - Does that mean that only the rich can afford to be homeowners in posh quarters?
  - For the young who plan to become homeowners
    - Is it really sure that transaction taxes will decrease to “compensate” for the rise in recurrent tax? => They will face mortgage payments + increased recurrent taxes…
- Local government
  - Is it sure that they will benefit from the rise in recurrent tax?
  - And if yes, increasing inequality between rich & poor communities
    - Again, issues of national cooperation

Resistance to reforms of housing property tax: politics

- Shift from transaction tax to increased (progressive) recurrent tax
  - A revolution: a number of heavily losers, few winners?
  - Needs strong national cooperation between State & local governments
    - Not much confidence: almost as problematic to settle as international cooperation…
  - Problems of tax base & periodic reevaluation
    - Even worse than for an annual comprehensive wealth tax (a la Piketty)
- The specific case of a (progressive) tax on imputed rent (OFCE)
  - If imputed rent taxed, there must be a tax relief on mortgage interest payments (comparable ability-to-pay for owners & renters)
  - Taxation difficult: imputed rent not known & political resistance (many losers)
  - Instead: deduce rents for renters & mortgage interest payments (horizontal equity), compensated by a general increase of the income tax (e.g.)
    - Reform would be progressive: rent/income ratio higher for low income households

Annual wealth tax, comprehensive & progressive (PSZ)

- PSZ: net wealth, market value, on an individual basis, for the <u>rich</u>
  - Largest base as possible, prefilled declarations, AEOI, financial world registry…
  - <u>Reasons</u>: consumption & income flows of the rich difficult to define
    + non-income benefits of high wealth: power, prestige, influence (Keen, 2015)
    - Rates of return *r* are high & increasing with the size of wealth => progressive tax
    - Taxing (equivalently) variation of wealth: highly volatile & rich have specific behavior
  - ➢ Millionaires, revenue = 2% of GDP => France: revenue x 8 (40 blns) / today ISF
  - ➢ Prompt rich to shift to more risky investments (higher exp. *r*) => growth-friendly?
- Resistance: objections of economists
  - Efficiency: does not distinguish between rent-wealth & productive investment
  - Equity: tax identically inherited & self-accumulated wealth
    - But PSZ tax mix also includes a progressive inheritance tax
  - High heterogeneity of *r* (assets, sectors) & capital losses (double loss)
    - A 2% (top marginal) tax rate can be sometimes confiscatory
  - <u>International tax cooperation is unrealistic</u> (=> e.g., works of art go abroad)

Annual wealth tax: discussion (1)

- ISF popular in France
  - … among people who do not expect to pay it in the next (five) years
  - Often assumed to have cause the electoral failure of the Right in 1988
  - Resistance <u>in reverse</u>: will be difficult (for the Right) to cancel this tax
- But annual wealth tax has been repelled elsewhere during the 2000s
  - Sweden (Ikea, Tetra Pak?), Italy (until 2012: Berlusconi?), Austria, Germany
  - Not likely that the wealth tax is (was) that popular in these countries
- ❑ Tax resistance is a complex phenomenon, varies between countries
  - Wealth tax only in France, Norway & Switzerland
    - & revival in Spain, Iceland (?)
  - Is the lack of international tax cooperation an impossible barrier for this tax?
  - ➢ A closer look at the French experience…

Annual wealth tax: discussion (2)

- ISF ‘works’ not so badly in France (revenue ≈ 5 blns Euros per year)
  - Revenue increasing (due to rising tax base): once good news in France!
  - The rich in France face a number of (more or less efficient) progressive taxes on income, wealth & inheritance… but seem still to do well, at least on average
- ISF should bring invaluable information on the rich over 30 years!
  - Including intra-cohort mobility: are the ‘rich’ always the same?
    - See the US debate on the rising concentration of wealth in JEP (2015)
  - But a lot of tax files have been lost or damaged (resistance of administrations?)
- Lack of international tax cooperation (in Europe)
  - Piketty does not like consumption tax (regressive) & recurrent property tax
  - But also, these are the two taxes that do not need international cooperation
  - ➢ Becoming more radical?
    - Put a ceiling to these two taxes in the Schengen zone…
    - in order to force international tax cooperation for lack of tax revenue

Comprehensive income tax, progressive (PSZ)

- First, owing to the "fuzzy frontier between capital & labor income"
  - For self-employed individuals, business owners, corporate executives…
- The comprehensive-income tax-cum-inheritance-tax consensus: 1910-1980
  - In all developed countries. Even, often tax surcharges for capital income flows
  - And imputed rent was usually part of the tax base
- French economists' & other resistance (e.g., Aghion-Cette-Cohen, 2014)
  - For a <u>flat tax</u> on capital income & moderate => innovations first!
    ➔ Limit double taxation & preserve long-term risky & productive investments (growth)
  - More stocks & shares (SS) => control of national capital + growth friendly
    - SS limited diffusion: national 'culture', taxation, but also <u>asset price expectations</u>:
    - French (2007-2011) decline of SS: not due to changing preferences (risk aversion) but drop of (5 years) expectations in SS expected return (Arrondel-Masson, 2014)
  - Alternative: compulsory, collective retirement savings??
    - Pension fund: collective management allows for long-term & risky investments

Specific taxation of capital gains (OFCE)

- Advantages
  - Mitigates the double taxation issue
  - Takes into account the heterogeneity of rates of return & capital losses
  - Take into account <u>real</u> capital gains (minus inflation & capital depreciation)
- OFCE: concept of ‘augmented’ (capital) income
  - Add capital gains (realized or latent) & imputed rent in real terms
  - France: 12% of household income on average over the period 1998-2010
  - A large part is not taxed: ‘loss’ of revenue = around 50 blns Euros per year?
- But direct taxation of <u>latent</u> capital gains is difficult (consensus?)

➢ Tax (real) capital gains <u>when transmitted</u>, especially on death

  - Avoid ‘erasing’ of latent capital gains by wealth transfers

➢ Tax <u>realized</u> capital gains, especially on housing (at a 30% tax rate)

  - Tax housing capital gains for the part not reinvested in (owner-occupied) housing?

Taxation of wealth transfers – WT – (Masson, 2015)

- Theory of optimal capital taxation: an ideal tax?
  - Cremer (2010): "… For a number of social philosophers and classical economists, estate or inheritance taxation is the ideal tax"
  - Cremer & Pestieau (2012): "Our basic goal is to finance government services with a tax that is as efficient, fair and painless as possible. On all counts, it is difficult to imagine a better tax than the estate tax"
  - PSZ: "There are strong meritocratic reasons why we should tax inherited wealth [an unearned income] more than earned income or self-made wealth"
- But strong preference everywhere for 'lifetime' capital/wealth taxation
  - Lifetime wealth (capital) taxation typically 10 (20) times more than WT tax
  - WT tax less than .5% of GDP today, except Belgian (.6%) & France (.5%)
- People resistance: WT tax becoming more & more unpopular today
  - Recent French polls, 12 different taxes: ISF most popular, WT tax least popular
  - Same elsewhere for WT tax: see, e.g., Prabhakar (2009 et 2012) for the UK

Resistance to (strong) taxation of wealth transfers (1)

- Objections to WT tax, excluding ‘existential’ & family considerations
  - Tax illusion: inheritance tax = a too visible lump sum tax / moderate annual tax
  - Tax illusion: belief or dream that I can become rich ‘one day’ (wealth mobility)
  - Inheritance tax comes <u>too late</u>, especially if limited ‘lifetime’ capital taxation
  - Uncertain & uninsurable rates of return on the long run & liquidity constraints
    - Call, under risk aversion, for higher (age-dependent?) lifetime capital taxation
  - Double taxation: weak argument, but what if parents have already paid the ISF?
  - Horizontal inequity: family harmony, sudden death, optimization
  - Strong ‘avoision’ (avoidance + evasion) among the rich
- Objections to WT tax linked to death & family values
  - A virtue tax (altruism): works more for *inter vivos* transfers
  - A death tax (double loss), if not a sudden death tax
  - A tax on family home
  - A tax on family business

Resistance to (strong) taxation of wealth transfers (2)

- To sum up: the conventional view explains the low WT tax & the collective preference for lifetime capital taxation by:
  - A coalition of the rich with (upper) middle classes having strong family values
- But over the last 40 years, <u>specific</u> growing aversion to the WT tax:
  - Declining revenue of WT tax (as a % of total tax receipts or GDP) since 1960
    - Many countries have suppressed WT tax since 1972 (Canada), esp. in the 2000s
  - Not the same decline for lifetime wealth or capital taxation
    - Ratios are higher in 2007 than in 1995 (even in the US!), owing to rising tax base
- Why has the lobbying of the rich been <u>so</u> successful for WT tax?
  - Wealth is more a sign of 'success', no matter its origin (Beckert, 2008 & 2012)
  - Rising family values & 'morality': family = <u>safe haven</u> against...
    - Growing insecurity & declining economic growth, waning trust in the Welfare State…
  - Need further qualification: H. Ohlsson is not convinced in the case of Sweden

Resistance to (strong) taxation of wealth transfers (3)

- Resistance to WT tax quite tricky: explain also historical change!
  - Inheritance tax popular in the US in the 1930s (SHOW program) & even until the beginning of the 1970s (McGovern campaign in 1972) => Beckert (2012)
  - Help of other social sciences + a new theoretical framework explaining change
- Fennel (2003) tries only to explain <u>current</u> resistance to WT tax
  - Why is the tax also unpopular among people expecting to leave few bequests?
  - Why do richer people do not use more *inter vivos* giving to reduce the WT tax?
  - Explores rational & behavioral reasons (optimism, loss aversion) & calls for...
  - Reforms of the estate tax (in the US), such as…
    - <u>Reframing</u> the tax as a “gain-reducer” (gain = bequests), not a “loss-creator” (?)
    - <u>Earmarking</u> its revenue for specific opportunity-enhancing programs for the young
    - Allowing to <u>pre-pay</u> the tax on major illiquid assets, etc.
  - Not always uninteresting, but a bit short: we need broader approaches

Towards conflicting “DOP” approaches

- Diagnosis of the defects of current situation, calling for remedies
  - Subjective (& maybe country specific): see, e.g., my first slides: social & wealth
- Objectives => priorities (see examples in Masson, 2015)
  - PSZ: re-control capital, limit wealth concentration & power of the (ultra) rich
  - Could be also: ‘rise economic attractiveness of the country’ (J.-F. Copé)
    - Efficiency-equity: just criteria or tools, not selected objectives
- Propositions (tax mix), while trying to cope with various resistances
- Full-articulated “DOP” approaches would be of real help in debates
  - In a way, PSZ & OFCE do this (& also British reports: Meade, Mirrlees?)
  - Keen (2015): very clear & careful synthesis, but not a DOP approach
    - DOP approaches should not be reserved to pure academics with no economic responsibility…
- General suggestion: proposing ‘deals’
  - Tax hikes not only justified by efficiency/justice: visible compensation to people

Deal 1: tax on wealth transfers: *Taxfinh* program (1)

- *Taxfinh*: two inseparable components (Masson, 2015)
  - Tax more (progressively) family inheritances on death
  - Multiply & facilitate the ways to sidestep this ‘surtax’ =>
    - Giving (sufficiently early before death) to children; charitable gifts & bequests
    - Invest in long-term risky assets (tax exemption on death)?
    - More possibilities to run down net wealth at retirement: reverse mortgage, ‘viager’…
  - Pitfalls: long-term credibility (insulation), transition (very old), horizontal equity…
- *Taxfinh* far superior to a standard inheritance tax
  - Gives ‘good’ incentives to families in order to sidestep the surtax
    + Decreases, accordingly, bad distortions & ‘avoision’ (also at the international level)
  - Responds to a number of objections to the WT tax (see slide 18)
    - Virtue tax; Death tax; People have to prepare in advance (tax not coming ‘too late’)
  - Would be more popular, since more equitable: ‘surtax’ would be only paid by those who “deserve” it − being too short-sighted or “selfish”

Deal 1: tax on wealth transfers: *Taxfinh* program (2)

- But *Taxfinh* first a remedy to a new, unfavorable wealth situation
  - Tax incentives given in order to remedy the unfavorable wealth situation
  - Likely sizeable revenue (but not known in advance): an order of 10 blns Euros?
  - Wealth situation due to (1) rising longevity, (2) patrimonialization, (3) lack of growth
    1. "If", death at 70, inheritance at 40 (no rising longevity)
    2. "If" the weight of bequest (B/GDP or B/wealth) and wealth (/GDP) were limited & wealth inequalities were moderate (no 'patrimonialization')
    3. And "if" economic growth was not that sluggish
    - ["if" ≈ the 1950s or 1960s], the *Taxfinh* reform would not be that necessary
- Earmarking
  - The revenue could help to finance (1) long-term care costs or, alternatively, (2) opportunity-enhancing programs for the young
  - There are good reasons for each of the two options (but better to choose)

Deal 2: seniors' wealth contributing to the financing of the Welfare state, especially for the elderly

- French campaign of 2012: 52% of the voters were above age 50
- The seniors in France (& Eurozone) have sizeable wealth on average
- Retirement pension in France: unfunded, DB, Bismarckian
- Tensions between generations: lucky first baby-boomers (born 1943-1957?)
  - 20 years old before the 'piteous years': soon all in retirement, under current system
  - Want to maintain the purchasing power of pensions: simple & mobilizing claim
  - With, maybe, a new, harder, system for the next generation to secure sustainability!

- The political choice for a sustainable Welfare State to the elderly
  1. Either turn to Beveridge: a basic safety net, to be completed by private savings
  2. Keep current system & replacement rates not declining too much with income
- Option 2: recurrent wealth tax used to build a retirement/social fund
  - Age-dependent taxes? Fund used to maintain current pensions in real terms?
  - ❑ Current & future retirees, (upper) middle class: more taxed, but life 'secured'

Deal 3: taxing the top-wealth holders: ‘good rich’ & ‘bad rich’?

Tentative, not well-articulated & debatable: divide (the rich) and rule (them)?

- Neo-liberals against moral hazard => ‘good poor’ & ‘bad (lazy) poor’
- Why not distinguish also between ‘good rich’ & ‘bad rich’?
  - The ‘good rich’ do not try to avoid taxes & their wealth trickles down (Carnegie)
  - The ‘bad rich’ are ‘selfish’ & use tax ‘avoision’ on a too large scale => exit tax?
    - St Thomas d’Aquin already made this division, asking for a higher taxation of the wealth of the bad rich (with his definition at the time!)
- Good rich should be ‘compensated’ and/or bad rich ‘disadvantaged’?
  - A too moralizing view? How to make an operational, objective distinction? And how to compensate or disadvantage? Appeal for national solidarity?
  - Example: Cl. Bébéar, founder & former CEO of AXA, on French inheritance law
    - Wants the children ‘reserve’ to be reduced in order that the rich can give (more) to charitable & other organizations: has clear ideas how to do so
  - ➢ A way to fight the efficient lobbying of the rich? To complete PSZ approach?