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Too rich to rein in? The under-utilised wealth t

countries). Between them, these two tax bases (income and expenditure) account for the vast majority of tax revenue for most countries. But taxes on wealth have never been as popular or widespread as taxes on the other two major tax bases.

It is not entirely surprising that the wealth tax base is relatively under-utilised compared to its more illustrious income and expenditure counterparts. Not only, it is argued, can wealth taxes have a negative impact upon entrepreneurial activity and economic growth, but the biggest problems of wealth taxes are the practical administrative issues (particularly related to disclosure and valuation) that are often evident when attempts are made to tax accumulations and/or transfers of capital or wealth. Thus, these taxes are not an obvious universal tax policy tool.

In spite of the practical problems and efficiency issues of wealth taxes, those in favour of attempts to tax wealth typically garner significant support. The main reason is the embedded inequality of wealth. Figure 1, for example, shows that 41 per cent of the

statistics would readily be used by wealth tax advocates to justify the imposition or retention of wealth taxes designed to effect appropriate re-distribution.

Figure 1. The Global Wealth Pyramid

Source: Global Wealth Databook 2013, Credit Suisse.

The ambivalence towards wealth taxes was neatly summarised in the United Mirrlees Review, which noted that:

> Taxation of wealth is a topic that excites strong passions. Some view it as the most direct means of effecting redistribution and key to achieving equality of opportunity. Others see it as the unjustified confiscation of private property by the state. Given these opposing viewpoints it is not surprising that this is an area of taxation where international practice differs dramatically Some countries levy taxes directly upon wealth holdings while others only tax transfers of wealth. There are some countries which do not tax wealth at all.[4]

[4] Mirrlees, James, Adam, Stuart, Besley, Tim, Blundell, Richard, Bond, Stephen, Chote, Robert, Gammie, Malcolm

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Such diverging views have contributed to major differences between countries in the use of wealth taxes, their scope, their effectiveness and their political and opportunity costs. Wealth taxes have seen different levels of commitment and different levels of success across jurisdictions. Many developed countries have reduced the scope of wealth taxation by narrowing the tax base or have abandoned this tax source altogether, whilst increasing their reliance on other tax bases. Contrastingly, several developing countries continue to use wealth taxes in attempts to capture taxation revenue to address the significant inequality in the distributions of income and wealth among their citizens.

This article considers the use or more often the under-use of wealth taxes in developed and developing countries. It includes a discussion (in Section 2) of different forms of wealth taxation together with the theoretical underpinnings and the practical problems that can arise when such taxes are implemented. Next, the current role of wealth taxation is discussed in Section 3. Trends in developed and transitional or developing jurisdictions are analysed and both country-specific and more universal wealth tax policy changes are identified. Finally, some thoughts on the likely future policy directions in wealth taxation are presented.

2. Conceptual issues

2.1 Forms of Wealth Taxation

If wealth is not easily measured, it is certainly well understood by those who enjoy it and those who do not. The essential characteristic of a capital or wealth tax is that, in principle, it relates to the whole range or genus of assets, whether tangible or intangible: cash and bank balances; real property such as houses; personal property such as jewellery, pictures, furniture, cars and boats; stocks and shares; and business assets. All these assets, taken together, comprise the tax base of any form of wealth tax, unless expressly excluded.[5] To try to encapsulate the for tax purposes wealth is usually relevant. This net wealth is typically computed by subtracting total liabilities from total assets.[6]

Wealth taxes can be grouped into three major categories: taxes on the holding or stock of wealth; on the transfer of wealth; and on wealth appreciation.[7] The first category comprises the taxes levied periodically on a aggregate net wealth.[8] These taxes can be ongoing annual wealth taxes (AWT), such as those currently levied on individuals in France, Norway, Switzerland and India and on corporate entities in Luxembourg; or they may be sporadic capital levies, typically imposed at a time of n in Japan after the Second World War. Both AWTs and once-off capital levies are relatively uncommon in both developed and developing tax systems.[9]

The second category of wealth taxes comprises those taxes levied on the recipient or the transferor of net wealth, whether *inter vivos* or at death. These wealth transfer taxes therefore include gift taxes, inheritance taxes (when imposed on the recipient of wealth on the death of the transferor) and estate taxes (when the tax is levied on the estate of the deceased).[10] Typically these taxes are imposed at the time of the wealth transfer. Most OECD countries currently have such transfer taxes.[11]

The third category comprises taxes on net wealth appreciation. These are taxes such as the

Perhaps the strongest rationale for the introduction or continuation of taxes on wealth lies in the second of the objectives for governments when they impose taxes: their ability to positively impact upon the horizontal and vertical equity of the tax system. In 1953, Nicholas Kaldor summarised the rationale for use of wealth taxes as a taxable capacity differentiator.[18] This rationale has since become a frequently cited argument by those who advocate wealth taxes:

> Equity for the [wealth] tax is that income taken by itself is an inadequate
>
> yardstick of taxable capacity than either form of taxation itself.[19]

Characteristically, person A, who earns $10 from a $100 investment, all other things held constant, has greater taxable capacity than person B who earns $10 from labour and has no investment.[20] Even if no money was earned on the investment by person A, he or she can monetise their holding. In this case, the imposition of a net wealth tax on person A would be vertically and horizontally equitable. Via the imposition of a net wealth tax, p greater taxable capacity is recognised. This is fair as it aims to reduce inequality among taxpayers. A fair tax should improve the perception of equality among taxpayers, leading to greater trust in institutions and higher levels of solidarity.[21]

When a wealth transfer tax is applied to intergenerational wealth transfers, it is also a fair tax. By placing relatively higher burdens on higher wealth transfers, this tax plays a role in tackling intergenerational inequality. This is because the quantum of physical disposable wealth of the heirs is proportionally reduced by the corresponding wealth transfer tax liability reinvestment or on human capital to the benefit of the wealth holder only. Therefore, this argument relies on creation of extraneous benefits for people other than the wealth holder.[25] An example of such benefits is reinvestment in productive assets that leads to job creation or economic growth.

Although there are a number of administrative arguments against wealth taxes (discussed below), policymakers advocating these taxes are still able to identify other, indirect, administrative benefits of wealth taxes.[26] These benefits include the potential for reduction of tax avoidance and evasion, when wealth taxation complements income taxation. In this respect, governments can collect wealth tax data and cross check it against income tax data to ensure greater compliance and that any legislative loopholes in either wealth or income taxation are not exploited.[27]

These arguments suggest that wealth taxation can be a useful policy tool, at least in theory. The arguments are also politically appealing as the wealth tax burden is placed on the more affluent sectors of the population. Nonetheless those who argue against wealth taxes are still able to enlist significant support, based upon major concerns relating to valuation, disclosure and appropriate attribution of legal and practical liability.

2.6 Pble sw Weah Taxn

Two main administrative problems disclosure and valuation prevent wealth taxes being more prevalent than otherwise might be the case.

that taxpayers disclose their wealth and cannot enter into simple and cost effective schemes to optically reduce the overall value of that wealth.[28] The problem of disclosure is obvious it is very easy to hide or export many forms of wealth, whether in the form of physical assets like diamonds or fungible assets like bank balances. Compliance becomes a real problem; hence inequities begin to arise between honest and dishonest taxpayers; and revenue authorities introduce compromises (such as exempting household articles) which inevitably undermine the efficiency, equity and integrity of the tax.

Where wealth is undisclosed or diminished, effective taxation of wealth is not possible. With this in mind, policy makers must recognise that particular taxpayers may be more likely to evade or avoid a wealth tax. An interesting example is the case of the Swedish AWT that was in force until 2007. Research has indicated that this tax was subject to more evasion by households with higher cognitive ability.[29] This trend

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25 *Tax Law Review* 1, 263.

26 in *Death, Taxes, Family and Property* *Yale Law Journal* 283.

27 *Virginia Law Review* 7, 1185 1186.

28 Taxpayers have been creative in schemes even if a no wealth tax was in force at the particular point in *British Tax Review* 183-193. This article discusses the case of Mr McGuckian, who was a party to a scheme that was designed to reduce the value of shares held by him as he feared a wealth tax might be introduced in the UK.

29 Stockholm University Working Paper).

is likely to be present in other developed countries and, intuitively, this trend would be expected to be even more pronounced in developing and transitional economies.

Asset disclosure is accompanied by an additional major problem: its valuation, especially where an actual sale of the asset does not take place to give an independent market value. In addition, if a wealth tax is to have any consistency of meaning, assets such as the capitalised value of future pension rights, or of future earning power, may need to be included in the tax base. But there is no consensus on whether they should be included, and if so, how they should be measured.

Valuation difficulties are notably seen in cases of unlisted assets when particular interests are held through companies, partnerships, trusts, or other entities.[30] This is because each interest needs to be valued. Here, issues such as control premiums and/or minority discounts are evident. Additional concerns appear where different valuations are used for different tax purposes, as in France.[31] These problems are naturally magnified for intangible property.

Wealth attribution glitches are observed when different legal ownership forms are considered. For instance, while the common law trust structure is widely used in the UK essentially a tax haven for investment income.[36] This is arguably inequitable toward labour income earners. However, it is a workable way to retain HNWIs.

Other countries seek to impose tax barriers such as exit taxes or other penalties to prevent HNWIs from leaving the country.[37] For example, in the US, HNWIs cannot renounce citizenship or terminate long-term residence status in order to avoid paying US taxes.[38] If they do so, particular wealth transfer taxes continue to apply.[39] France also imposes exit barriers in the operation of its inheritance taxes. In that country, HNWIs leaving the country do so in vain if the heirs remain in France because French domestic laws contain explicit provisions for continual inheritance taxing rights.

One final argument used against wealth taxes is that there may also be a greater administrative burden imposed upon revenue authorities in collecting wealth taxes, relative to, for example, a value added tax,[40] although this may be mitigated to some extent by relatively lower costs of compliance for the taxpayers involved.[41]

Notwithstanding these real problems with the implementation and operation of taxes on wealth, and the political controversy that often surrounds them, the powerful equity and efficiency arguments already identified mean that wealth taxes are still used in many developed and developing countries. The following section identifies how and where they are so used.

3. CURRENT GLOBAL PRACTICES IN WEALTH TAXATION

3.1 Overview

There are different combinations of wealth taxation forms used globally. The basic divergence stems from distinctions in historical, geographical, cultural and economic backgrounds. At the one extreme, tax havens such as the Cayman Islands, Monaco and Belize do not levy any form of wealth taxes. These small countries have traditionally differentiated themselves through their tax policy as attractive holding jurisdictions for the coffers of the wealthy.[42]

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wealth and even fewer on all three forms of wealth tax. These include some of the earliest adopters of wealth taxes globally, namely, France, Switzerland and Norway.[44]

In terms of specific sub-categories, transfer taxes are currently more common than net wealth taxes. This is because uncovering wealth is typically easier when the wealth transfer takes place when the legal documents tied to the transfer stipulate entitlement and value.[45] Transfer taxes are presently levied in more than half of the OECD nations and are most prevalent among the European Union members. Estate taxes are more likely to exist in common law countries, whereas inheritance taxes are predominant in civil law countries. The tax family and succession law differences lie at the root of this di(l)-4(t)46(ot)-4( )-324 622.[( )]6 the transfer stipulate entithreeoax fami3m[(-4(

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The form of wealth tax most commonly eliminated by the OECD members has been the AWT. A total of only five OECD countries still had this tax operating in a comprehensive form in 2011, a decline from a peak of 16 countries in 1995.[55] These taxes have reduced in popularity among the OECD members because, coupled with administrative difficulties, they have generated a low revenue yield and had an insignificant impact on progressivity. Germany and Sweden are examples of countries that have abandoned annual net wealth taxes in the past 15 years. In Sweden, the net wealth tax was eliminated as inconsistencies in the treatment of private wealth and operating assets lead to inefficient and inequitable outcomes.[56] In Germany, administrative and valuation issues were the cause of the demise of the AWT. to declare the net wealth tax that was in force at the time as unconstitutional.[57] Its reasoning was

and wealth transfer tax regimes. This has been were more likely to leverage their assets to avoid the net wealth tax.

of TTR.[87] Legal and illegal schemes have exploited tax base. Corruption of has contributed to the low collection rates, particularly where large fortunes are transferred at the extreme concentrations of wealth.[88]

Like developed countries, some developing nations have moved away from net wealth and transfer taxes. Sri Lanka, India, Bangladesh, Pakistan and Indonesia have all abolished elements of wealth transfer taxes that were previously utilised.[89] In Sri Lanka, it was shown that when the broadest form of net wealth and transfer taxes was in force, these taxes were neither an effective revenue producer, nor an instrument to improve equality.[90] There, the compliance costs were said to outweigh the benefits derived.

Recognition of divergence between developed and developing countries in the reasons for the wealth tax trends is important. In South America especially, o evasion looks more pronounced so the wealth tax mechanism is used to capture some revenue that is lost when income escapes income taxes of these countries. In contrast, developed countries appear to have experienced greater avoidance issues as taxpayers pursued, some convergence may be anticipated.

signalling letting those in society without wealth know that it is not just they that have to make all the sacrifices in times of financial hardship (when welfare provision is continually being curtailed).