Basic economics of wealth tax

- tax on future wealth (say, 2%)

$$1 + r = \underbrace{1 + \text{normal rate of return} + \text{risk} + \text{rents}}_{\text{wealth tax}}$$

- tax on capital income (say, 40%)

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($\underline{\text{2\% of } 1.05 \approx \text{40\% of } 0.05}$)

- Wealth tax shifts burden from rents/risk toward principal (ie normal rate of return)
- What can wealth tax do that capital income tax cannot: (1) impose income tax rates over 100% and (2) be an effective tool of one-time confiscation of ill-goten gains

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Externalities

- dynastic wealth — estate tax
- political power — political reform (wealth tax encourages spending, including on politics, and it also increases benefits of political spending!)
- monopoly power — anti-trust
- garden-variety rents — capital income tax
- misdirected charity — time to rethink how charity is treated/subsidized

Implementation

- Tax (observable) arm's length market transactions...
- ...that's what makes 3rd party reporting possible, keeps base easily measurable, and makes compliance costs low (eg., VAT, labor income tax)
- Where we don't tax arm's length transactions? E.g., transfer pricing, small businesses, real estate assessments
- In particular, valuation (especially, but not just, of businesses) is a major problem with the wealth tax (well tested in the case of estate taxation)...
- ...work-arounds are costly, imprecise (and therefore gameable) or very experimental
- Depth of public markets is not guaranteed

My short list of reforms

- Fixing capital gains taxation
  - Addressing step up
  - Solutions to valuation problem in wealth context are naturally solutions that allow for introducing accrual taxation
  - Auerbach's retrospective taxes (it solves liquidity and valuation) or notional liability (to address liquidity when annual valuation is possible)
- Reforming charity (credit rather than deduction; no double dipping via donation of accrued gains; valuation(!) games; what's legitimate charity?)
- Improving estate tax (enforcement and base)
- Rolling back pass-through deduction

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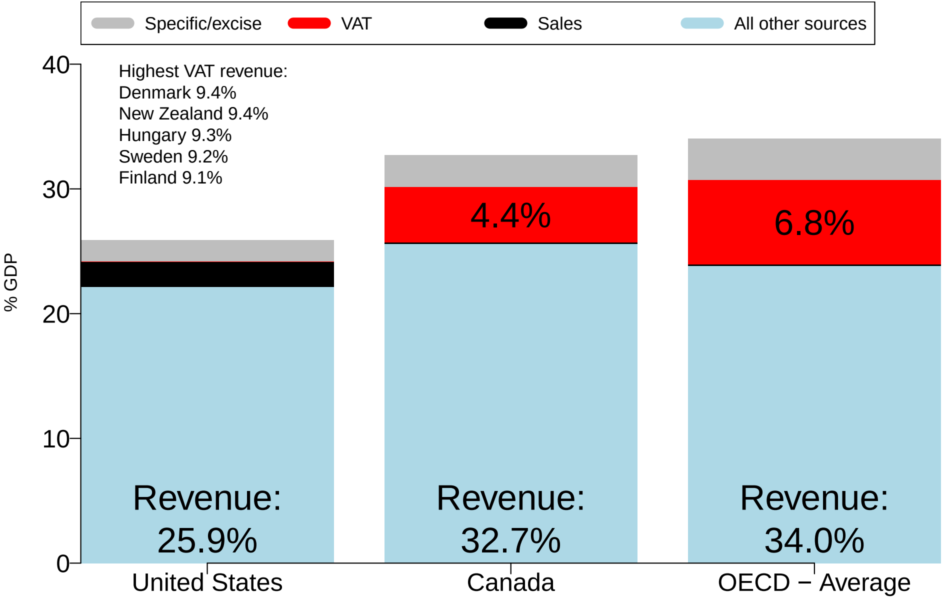
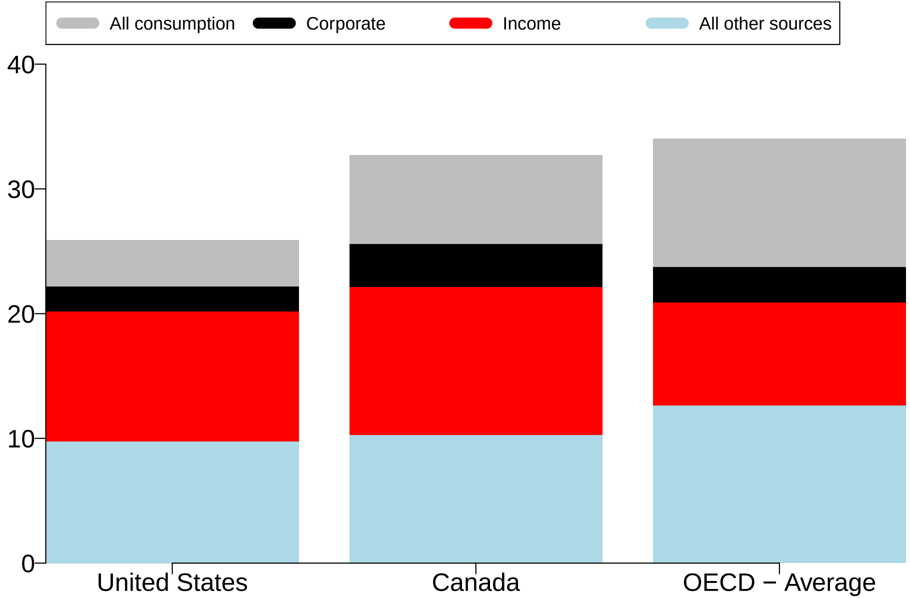
- ...and VAT

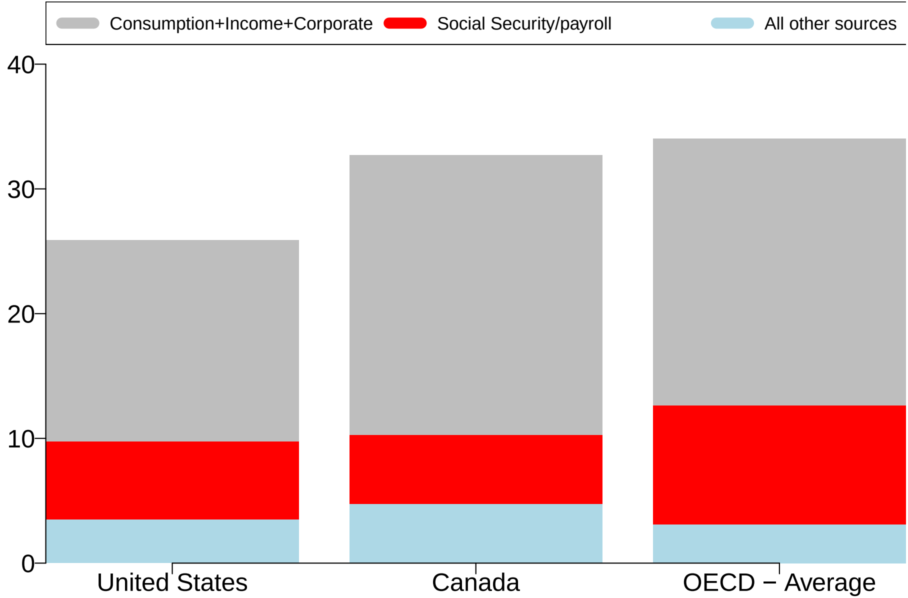
Revenue (%GDP) — VAT and excise



Revenue (%GDP) — income and corporate tax



Revenue (%GDP) — Social Security and payroll taxes



Revenue (%GDP) — estate/gift and wealth taxes