Wealth Taxation: Lessons from History and Recent Developments

By Emmanuel Saez and Gabriel Zucman*

Since the late 2010s there has been renewed debate about the merits and demerits of progressive wealth taxation. This debate has largely been motivated by the increase in wealth concentration in recent decades. In the United States, the share of total household wealth owned by the 0.0001% wealthiest Americans—a group that includes 18 individuals with more than $50 billion in wealth in 2021—has been multiplied tenfold since *Forbes* started publishing data on the richest Americans in 1982. Wealth concentration has increased particularly fast during the Covid-19 pandemic (see Figure 1). All estimates show a dramatic increase in wealth concentration since the late 1970s (see Saez and Zucman, 2020 for a discussion of the data and reconciliation of the various estimates). Moreover, as wealth concentrated, the ratio of wealth to national income doubled from less than 3 in the late 1970s to over 6 in 2021. Top-end wealth is large relative to the economy, and therefore a sizable potential tax revenue source (Saez and Zucman, 2019).

To shed light on the practicality and desirability of taxing wealth, this paper studies the historical experience with wealth taxation in Europe. Using new research on the distribution of wealth over time in Europe, we show that the European wealth taxes had a narrow base, due to large exemptions, tax avoidance, and tax evasion. We explain why such exemptions were granted and how they undermined European wealth taxes, leading in many cases to their repeal.

* Saez: UC Berkeley, 530 Evans Hall #3880 Berkeley, CA 94720-3880, saez@econ.berkeley.edu. Zucman: UC Berkeley, 530 Evans Hall #3880 Berkeley, CA 94720-3880, zucman@berkeley.edu. We gratefully acknowledge support from the Stone foundation. We thank our discussant Laurent Bach for helpful comments and reactions.

Drawing lessons from this experience, we conclude by laying out the design and enforcement features that are required for a successful wealth tax in the 21st century. We compare this ideal wealth tax to proposals recently made in the United States.

I. European Taxes: A Narrow Base

We focus on progressive wealth taxes on households. Such a wealth tax is an annual tax on assets net of debts above an exemption threshold, often with graduated rates. Assets include both financial assets (such as stocks and bonds) and non-financial assets (such as housing). This is in contrast to more common property taxes, which only tax housing (with no deductions for debts) and exempt financial assets.

The European continent has a long experience with progressive wealth taxes on households. In 1985, according to statistics collected by the Organization for Economic Co-Operation and Development (OECD, 2018), 11 European countries has such a wealth tax, including Germany, France, Spain, Sweden, and Denmark. In most cases these were old taxes, first created in the late 19th and early 20th century. The taxes were based on self-reported wealth and applied above an exemption threshold often located around the 95th to 99th percentile of the wealth distribution, though some were broader (i.e., on the top 25% in Switzerland). Rates typically ranged from about 0.5%–1% above the exemption threshold to about 2%–3% for the largest fortunes.

In practice a large fraction of the wealth of taxable individuals was exempt or taxed at only a fraction of its market value. This was the case for equity in private businesses (a key source of wealth at the top of the wealth distribution) and for primary

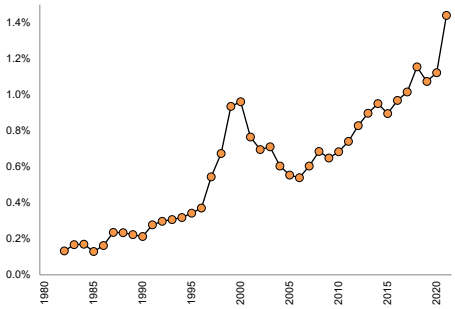

Figure 1. Top .00001% Wealth Share in the United States

Note: This figure shows the share of wealth owned by the top 0.00001% wealthiest tax units in the United States from 1982 to 2021. The top .00001% includes 18 tax units in 2021. Their wealth is from *Forbes*; the total household wealth denominator is from the Federal Reserve Financial Accounts. *Source:* Saez and Zucman (2020), updated.

homes (the main source of wealth just above the exemption threshold). Moreover, most countries had ceiling mechanisms, whereby the amount of wealth tax owed could not exceed a fraction of taxable income for the individual income tax; see Jakobsen et al. (2020) and Bach et al. (2022) for a description of these rules in the Danish and French contexts.

To quantify the fraction of wealth that was effectively taxed, we proceed in three steps. We start with the wealth distributions available on the World Inequality Database, WID.world. We then simulate the mechanical revenue of a wealth tax at a marginal rate of 1% on the top 1% wealthiest adults (that applies only above an exemption threshold equal to the 99th percentile of the wealth distribution). Finally we compare the theoretical revenues to the amounts effectively collected as reported by the OECD in its government revenue statistics (revenue code 4210, "individual recurrent taxes on net wealth"). The results are shown in Table 1.

The main finding is that the European wealth taxed collected little revenue relative to a simple 1% marginal tax on the top one percent. In Western Europe, the top 1% wealth share is typically around 25%. The average wealth above the 99-th percentile is typically around 3 times the 99-th percentile (corresponding to a Pareto parameter of 1.5). Therefore, a 1% wealth tax above the 99-th percentile collects about 2/3 of the top 1% wealth. Furthermore, the wealth to GDP ratio in Western Europe is pretty high around 5 or 6 in recent years. Hence, a 1% wealth tax above the top 1% threshold raises approximately 1 percent of GDP ($25 \times (2/3) \times 6 = 1$). In the US, the revenue potential is even higher as the top 1% wealth share is substantially higher at about 35%.

Consider the case of France. In 2016, about 351,000 tax units (with more than 1.3 million euros in net wealth) paid the wealth tax, or about 1% of all tax units. The top 1% owned about 25% of total household wealth or about 3 trillion euros, of which 2 trillion was taxable.[1] A one percent marginal tax rate on the wealth of the top 1% would thus have generated about 20 billion euros in revenues (0.8% of GDP). Yet that same year the wealth tax yielded only 5.1 billion euros (0.2% of GDP), i.e., four times less. Spain has a level of tax base erosion similar to France. Even countries such as Norway or Switzerland which tax a pretty large fraction of their populations (over 10%) fail to raise as much as our theoretical 1% tax on the top 1% implying that they also suffer from base erosion.

A recent study illuminates the reasons why the french wealth tax generated little revenue. By matching individual tax returns to business ownership and tax data, Bach et al. (2022) estimate the total

[1] As wealth is Pareto distributed, about a third of the wealth of the top 1% is below the exemption threshold and two-thirds (i.e., two trillion) above (see Saez and Zucman, 2019).

Table 1—Wealth tax revenues in Europe in 2016: actual vs. theoretical

	Fraction liable	Nominal marginal tax rates	Tax revenue (% GDP)	Revenue from 1% tax on top 1% (% GDP)
Spain	0.5%	1% to 2.5%	0.18%	0.96%
Norway	13%	0.85%	0.43%	0.86%
France	1%	0.5% to 1.5%	0.22%	0.83%
Switzerland	25%	0.2% to 0.5%	1.03%	1.36%

Note: This table reports statistics for four European countries that still imposed wealth taxes in 2016 (OECD 2018). Fraction liable reports the approximate fraction of households liable for the tax. Nominal marginal tax rates reports the range of graduated marginal tax rates that apply to the taxable base (there is regional variation in Spain and Switzerland so the most common ranges are reported in these cases). Tax revenue reports the wealth tax revenue as a percent of GDP (from OECD 2018). Revenue from 1% tax on top 1% reports the tax revenue potential (as a percent of GDP) of a wealth tax of 1% applied above an exemption threshold equal to the 99th percentile of the wealth distribution (individual adults with equal split for married couples). We assume that wealth is measured at market value for all assets with no exemption and no tax evasion. Data on the wealth distributions and wealth to GDP ratios are from the World Inequality Database.

amount of wealth owned by wealth-taxpayers, including the tax-exempt business assets of owner managers. They show that the exemption of owner-managers' equity wealth dramatically reduced the base of the tax. The effect is concentrated at the top of the wealth distribution. For the top 0.001% (the 370 wealthiest tax units), this exemption reduced the tax base by a factor of 10, reducing the effective wealth tax rate from the theoretical rate of 1.5% to about 0.15%.

The tax ceiling mechanism, which capped the total amount of wealth plus income tax owed at 75% of taxable income for the individual income tax, also played a major role in reducing effective tax rates. Bach et al. (2022) show that even if the equity wealth of owner-managers had been taxed, effective rate at the top would have have still been around 0.3% only, because the wealthiest taxpayers reported little taxable income on their individual income tax return (e.g., by retaining profits in the corporations they own, often using holding companies to do so). As a result, despite the wealth tax, the wealthiest taxpayers had low effective tax rate relative to their true economic income (i.e., income including profits retained in companies), of only 2%–3% when including individual income taxes and wealth taxes. As a result, the heaviest tax on the super-rich in France ends up being the corporate tax which taxes business profits at source with a flat rate.

In sum, European wealth taxes were all but comprehensive taxes on net wealth. In some cases such as France the law was written such that billionaires (including large shareholders of listed companies) were effectively exempt. It is as if the United States had had a wealth tax exempting Jeff Bezos, Elon Musk and Mark Zuckerberg.

II. Why Such a Narrow Base?

Three main reasons can explain the base erosion of European wealth taxes.

First, because the taxes started relatively low in the wealth distribution (typically below $1 million), they affected a fraction of the upper middle class, including taxpayers whose main source of wealth was housing. For these taxpayers the wealth tax was akin to a property tax. Property taxes are unpopular because they can create liquidity issues (e.g., Wong 2020). This led to a demand for exemption for primary homes and other assets that may not generate taxable income, such as artwork. Other taxpayers were able to use liquidity concerns to lobby for additional exemptions, such as reduced rates of owner managers and equity in private businesses. This process ended up benefitting the ultra-wealthy the most.[2]

A similar process has been at play in the United States with the estate tax. "Small family farms" were successfully used by opponents of the estate tax to advocate for its reduction and repeal in the early 2000s. The weakening of the estate tax dispropor-

[2]See, e.g., Alvaredo and Saez (2009) for the case of Spain which introduced such an exemption in 1994.

tionately benefitted large fortunes rather than small businesses, which are largely exempt from the tax due to its high exemption threshold.

Second, European Union countries never attempted to address the issue of tax competition whereby the wealthy can escape the wealth tax by moving abroad. While in the United States, citizens are taxable wherever they live, in other countries taxation is linked to residency. To avoid paying the wealth tax, rich Europeans could simply move abroad. The threat of expatriation was a major argument used to abolish the wealth tax in, e.g., Sweden and France.

In principle one could imagine a system where countries would keep taxing their expatriate after they leave, perhaps for a number of years that could depend on the number of years these expatriates have been tax resident in the first place. Tax competition is a policy choice, not a law of nature (Saez and Zucman, 2019b).

Last, there was a failure of tax enforcement. European wealth taxes were based on self-reported information, in contrast to income taxes which use extensive information reporting from employers, financial institutions, and other payers. Until 2017-2018, there was no automatic exchange of bank information between financial institutions in tax havens (e.g., Swiss banks) and European countries' tax authorities, making it easy for taxpayers to hide assets offshore. A recent study based on leaks from offshore banks (the "Swiss Leaks" from HSBC Switzerland and the Panama Papers) found that in 2007, the wealthiest Scandinavians evaded close to 20 percent of their taxes through hidden offshore accounts (Alstadsæter et al., 2019).

In sum, the reasons for the failure of European wealth taxes are political, not economic. Choices were made to largely exempt the wealthiest taxpayers; to allow tax competition; and to limit enforcement. While these choices were sometimes supported by economic arguments, there is no fundamental economic reason why billionaires should be exempted from wealth taxes, non-residents untaxed, and enforcement weak. Other choices could be made in the future.

III. Design of a Successful Wealth Tax

In light of this history, a number of ingredients appear helpful to make wealth taxes work in the 21st century.

First, focusing the tax on the ultra-wealthy can help deflect lobbying for base erosion. This can be achieved by choosing a high exemption threshold, thus focusing the tax on taxpayers which unambiguously have a high ability to pay and are wealthy enough to not face liquidity issues.

Second, comprehensive information reporting and pre-populated returns are critical to maximize tax compliance. A key lesson from the literature on tax evasion is that compliance is high when income is third-party reported and low when it is self-reported (e.g., Kleven et al., 2011). The same financial institutions that report income to the IRS could be asked to report account balances. Modern tax authorities have access to a wide range of information, including business balance sheets, allowing them to value large private businesses. Small private businesses can be valued using formulas (such as multiples of income and assets as done in Switzerland).

Last, in case there is disagreement in the valuation of private businesses, taxpayers could be allowed to pay in kind, with shares. The shares would then be auctioned off by the government, thus creating the missing market. Since corporate ownership is divisible in the form of shares, payments in-kind is always an option for owners of large businesses which are rarely owned by a single person, especially for the largest ones. This makes wealth taxes on corporate stock easier to administer than on real estate which is not as easily divisible.

Proposals made at the end of the 2010s in the United States generally follow these principles. In 2019, Senator Elizabeth Warren proposed a wealth tax at a rate of 2% above $50 million and 3% above $1 billion. Less than 0.1% of tax units in the United States would be liable for this tax (as opposed to about 1% in, e.g., the French wealth; see Table 1). In contrast to Euro-

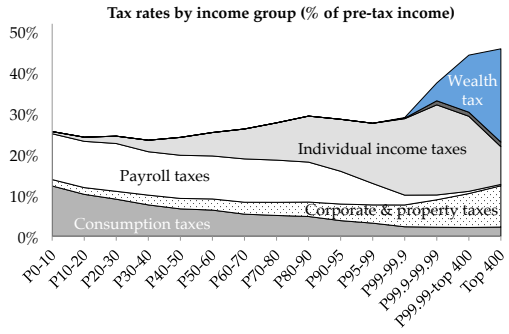

FIGURE 2. TAX RATES BY INCOME GROUP (% OF PRE-TAX INCOME).

Note: The figure shows effective tax rates in the United States expressed as a percent of pre-tax national income for the various groups of the pre-tax income distributions. Taxes at all levels of government (federal, state, and local) are included. The blue area shows the effect of a well-enforced wealth tax at rate of 2% above $50 million and 3% above $1 billion. *Source:* Saez and Zucman (2019b).

pean wealth taxes, such a tax would thus be focused on the ultra-wealthy. The proposal came with a large 40% tax on wealth upon citizenship renunciation, dramatically reducing the scope for tax competition. It was also accompanied by proposals to increase tax enforcement (with high audit rates at the top), drawing on the extensive information available to the IRS—including reports from foreign financial institutions since the passing of the Foreign Account Tax Compliance Act in 2010.

If well-enforced, such a tax would substantially increase the progressivity of the US tax system. As shown by Figure 2, it would increase the effective tax rate of the 400 wealthiest Americans from about 20%–25% in 2018 to about 45%. Despite involving less than 0.1% of the population, the revenue potential is significant: about 1% of GDP (Saez and Zucman, 2019).

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