Chapter 4. Net wealth tax design issues

This chapter examines practical tax design issues in countries that currently tax or have previously taxed individual net wealth. It largely draws upon countries' responses to the OECD Net Wealth Tax Questionnaire. This chapter highlights the differences in the ways that countries have implemented net wealth taxes in practice and identifies a number of good policy practices in the design of net wealth taxes.

This chapter is based on the tax rules that were in place as of 1 September 2017. Since then, France has replaced its net wealth tax ("*impôt de solidarité sur la fortune*") with a new real estate wealth tax ("*impôt sur la fortune immobilière*"), with effect from 1 January 2018.

This chapter provides an overview of net wealth tax design in countries that have or have had individual net wealth taxes. It draws upon countries' responses to the "OECD Net Wealth Tax Questionnaire" (see Annex A) and shows that countries that currently tax or have previously taxed net wealth have done so differently, with notable variations in tax design. Table 4.1 lists the countries that have responded to the questionnaire and whose net wealth taxes are discussed in this chapter. In addition to the four OECD countries that had individual net wealth taxes in 2017 (France, Norway, Spain and Switzerland), the chapter covers the net wealth taxes that were levied in Austria, Denmark, Germany, Ireland, Luxembourg, the Netherlands and Sweden. It should be mentioned as well that, in 2001, the Netherlands introduced a presumptive capital income tax that functions in practice like a net wealth tax (see Box 4.1). This chapter examines the different dimensions of net wealth tax design and compares how net wealth taxes have been designed and implemented across countries.

Table 4.1. Personal net wealth taxes covered in the chapter

	Countries	Name of the tax	Period of enforcement
Net wealth taxes in place in 2017	France[1]	*Impôt sur les grandes fortunes*, then renamed *Impôt de Solidarité sur la Fortune*	1982- Abolished in 1986 but re-introduced in 1989
	Norway	*Formuesskatt*	Introduced as a national tax in 1892
	Spain	*Impuesto sobre el Patrimonio*	1977 — 100% tax reduction introduced in 2008 but tax reinstated in 2011
	Switzerland	*Vermögenssteuer*	Gradual introduction by all cantons between 1840 and 1970
Historical net wealth taxes	Austria	*Vermögensteuer*	1954 - 1994
	Denmark	*Formueskat*	1903 - 1997
	Finland	*Varallisuusvero*	1919 - 2006
	Germany	*Vermögensteuergesetz*	1952 - 1997
	Ireland	Wealth Tax	1975 - 1978
	Luxembourg	Impôt sur la fortune (Net wealth tax)	1934 - 2006
	Netherlands	Vermogensbelasting	1965 - 2001
	Sweden	Förmögenhetsskatt (Wealth Tax)	1947, changed significantly in 1991, repealed in 2007

1. Chapter and table based on tax rules as of 1 September 2017. The French wealth tax has been replaced with a new real estate wealth tax since then.
Source: OECD Questionnaire on Current and Historical Net Wealth Taxes

Box 4.1. The capital income tax system in the Netherlands

The tax authorities in the Netherlands introduced the new Income Tax Act 2001 effective on January 1, 2001. The comprehensive personal income tax system that taxed both labour and capital income jointly at highly progressive rates was replaced with a schedular PIT system that taxed different types of income separately at different rates. The most significant component of the 2001 income tax reform was the introduction of the presumptive capital income tax (*vermogensrendementheffing*). In the Netherlands, the actual return on personally held wealth, in the form of dividends, interest or rental payments, is no longer taxed. Instead, a presumptive capital income tax on the value of the assets net of liabilities was introduced. The tax code assumes that all personally held assets – such as deposits, stocks, bonds and real estate (except owner-occupied property) – earn a presumptive rate of return, which is taxed at a proportional tax rate of 30%.

From 2001 until 2016, the presumptive rate of return was a uniform presumptive return of 4%. In 2017 some important new elements were introduced. First, a distinction was made between a presumptive rate of return on savings and a presumptive rate of return of investment (all other assets). Second, the introduction of three tax brackets with each bracket a presumptive mix of savings and other investment. The mix is based on the macro average portfolio mix per bracket. Third, the presumptive rates of return are yearly updated taking into account the actual return in the most recent year.

In the system that has been in force since 2017, the presumptive rate of return on savings in 2017 is following actual rates of return on savings by calculating a moving average over the last five years (1.63% for 2017). For investments, it is based on a long-term average annual return (5.50%). Each year the presumptive rate of return for investments is updated by 1/15th of the actual rate of return of the most recent year. Different portfolio allocations are then applied to different tax brackets, which result in progressive deemed returns.

Long-term average annual return on investments

	Return	Weight
Shares	8.25%	28%
Bonds	4.00%	12%
Real estate	4.25%	45%
Other assets	5.50%	15%
Average return	5.50%	100%

Deemed annual returns on savings and investments

	Deemed annual return
Savings	1.63%
Investments	5.50%

Deemed portfolio allocation and deemed return for the different tax brackets

Tax brackets	Deemed portfolio allocation		Deemed return
	Savings	Investments	
EUR 0 - EUR 25 000	Exempt		
EUR 25 000 - EUR 100 000	67%	33%	2.90%
EUR 100 000 - EUR 1 000 000	21%	79%	4.70%
Above EUR 1 000 000	0%	100%	5.50%

Although the presumptive capital income tax is an income tax (Stevens et al, 2006), it was equivalent to a net wealth tax of 1.2% between 2001 and 2016. Since 2017, deemed income increases with net wealth.

Government level

Net wealth taxes can be national level taxes, sub-central level taxes or a combination of both. In France, the wealth tax is a national level tax (replaced with a tax on real estate wealth as of 1 January 2018[1]). In Switzerland, wealth taxes are cantonal and municipal. Municipalities in most cantons apply the canton-level tax schedule but are free to choose the level of taxation by adding their own "multipliers" to the canton-level taxes (Brülhart et al, 2017). In Spain, the main structure of the wealth tax is regulated by the central government, but since the mid-1980s, along with the transfer of wealth tax revenues and the responsibility to administer net wealth taxes, regional governments have also been given limited legislative power to regulate the minimum threshold, tax rates and tax credits (Durán-Cabré et al. 2017). In Norway, the net wealth tax is split into a national and a local component. Among the countries that have historically had net wealth taxes, they were mostly national level taxes (Austria, Denmark, Finland, Ireland, Luxembourg, the Netherlands and Sweden), with the exception of Germany where the net wealth tax was levied by the federal states (Länder).

Tax unit

The practice has generally been to use the family as the tax unit in countries that currently have or previously had net wealth taxes. Family-based taxation implies that spouses and dependents are assessed and taxed jointly. Generally, the tax exemption threshold doubles for married couples but that is not always the case. In France, for instance, the tax exemption threshold and the tax schedule do not vary between single and married taxpayers, which implies that aggregating wealth increases the household's tax liability. Exceptions to family-based wealth taxes include Finland and Spain where the wealth tax was/is levied on an individual basis.

There are strong arguments for using the family as the tax unit. If spouses were to be taxed separately, it would be difficult to determine and split the ownership of household assets and to allocate the wealth of dependents to either one of the parents. In addition, in

the case of a wealth tax with progressive rates and exemptions and deductions, taxing spouses separately would require closely monitoring transfers of assets between spouses. These issues do not arise if spouses are taxed jointly. In addition, it seems appropriate to aggregate dependents' wealth – very often derived directly from parents – with that of their parents, as parents generally exert control over that wealth (Brown, 1991). Finally, the disadvantages of family-based taxation under the income tax in terms of reduced incentives for second earners to participate in the labour market and work long hours are less of a concern under a wealth tax.

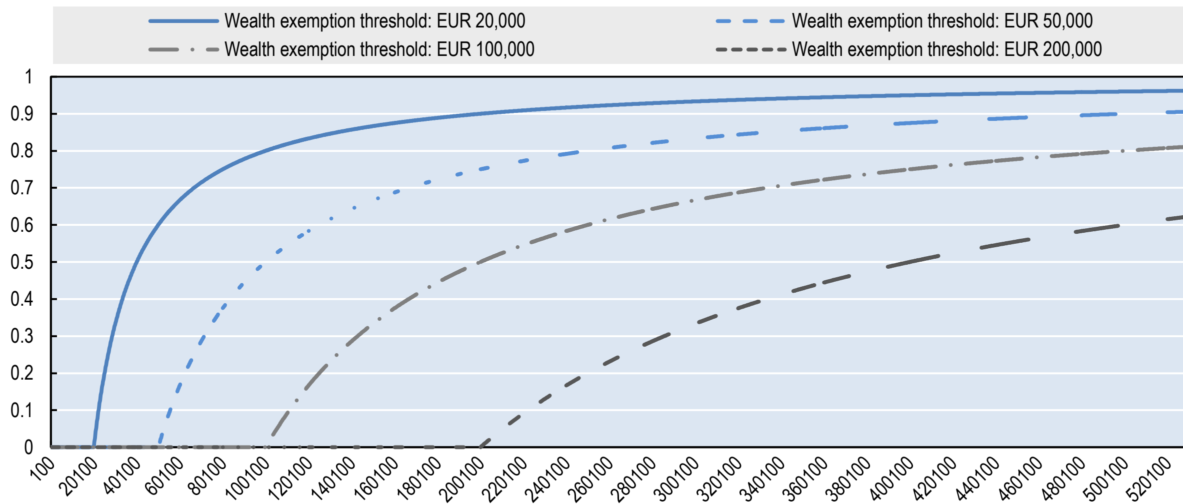
However, family-based taxation is not without problems. Joint taxation is usually only an option for married couples and not for other types of family structures (e.g. unmarried cohabitants) – a difference which is difficult to justify from the perspective of horizontal equity (but which might be explained by privacy arguments, as it is not the task of tax authorities to check if people live together or not). Moreover, it is not because couples are married that they actually share the ownership of their wealth. Finally, family-based wealth taxation may pose problems for countries that have elected individual-based income taxation.

The decision to double the tax exemption threshold for married couples or not involves a trade-off. If single wealth owners and married couples benefit from the same tax exemption threshold, couples may face a wealth tax-induced disincentive to get married. Alternatively, doubling the wealth tax exemption threshold gives a marriage bonus to households where both partners have very different levels of wealth.

Tax exemption thresholds

Net wealth taxes always exempt taxpayers under a certain level of net wealth to enhance equity. Figure 4.1, which models in a very simple way how the average effective wealth tax rate (i.e. wealth tax liability/net wealth) of a 1% net wealth tax evolves with net wealth, shows that an exemption threshold – and the level of that exemption threshold – has a strong effect on the progressivity of a wealth tax. By introducing an exemption threshold, the average effective wealth tax becomes a concave function. In fact, even with a flat tax rate, an exemption threshold can generate a lot of progressivity. A high exemption threshold also has the effect of lowering the average effective tax rates on the very wealthy.

Figure 4.1. Average effective wealth tax rate of a 1% net wealth tax



Source: Authors' calculations

Tax exemption thresholds have varied quite significantly across countries (Table 4.2). In some countries, the wealth tax only applies to the very wealthy, as is the case in France and Spain. In 2017, France had the highest exemption threshold, only taxing individuals and households with net wealth equal to or above EUR 1 300 000. In other countries, the wealth tax applies to a broader range of taxpayers. In Switzerland, for instance, despite variations across cantons, tax exemption thresholds are comparatively low: in 2014, they ranged from CHF 25 000 (USD 27 500) in the canton of Obwalden to CHF 200 000 (USD 220 000) in the canton of Ticino (Brülhart et al., 2017). Thus, net wealth taxes do not apply only to the wealthiest households but also affect a large portion of the middle class. Brülhart et al. (2017) report for instance that in the canton of Bern, 30% of all taxpayers and 41% of married households had a non-zero wealth tax liability over the 2001-2011 period. One of the explanations for these low tax exemption thresholds may be that Switzerland does not levy capital gains taxes and levies very limited recurrent taxes on immovable property (some cantons have them, others do not), and that net wealth taxes may partly replace these taxes.

Table 4.2. Net wealth tax exemptions thresholds in 2017 or in the latest year of operation, expressed in EUR

	Countries	Single taxpayer	Married couple
Net wealth taxes in place in 2017	France	1 300 000	1 300 000
	Norway	157 833	315 666
	Spain	700 000	1 400 000[2]
	Switzerland[2]	67 550	135 100
Historical net wealth taxes	Austria (1994)	No threshold[3]	No threshold[4]
	Finland (2006)	250 000	500 000[1]
	Germany (1997)	61 355	×
	Iceland (2015)	473 248	630 997
	Ireland (1978)	88 882	126 974
	Luxembourg (2006)	No threshold[4]	No threshold[4]
	Netherlands (2001)	90 756	113 445
	Sweden (2007)	166 214	221 619

Notes: For countries that abolished their wealth taxes before the introduction of the Euro, currency conversion rates on 1 January 2002 were used; for the other countries, currency conversion rates in the last year of operation of the wealth tax were used.

1. For Spain, each taxpayer is entitled to the EUR 700 000 allowance; in Finland, each taxpayer is taxed separately and entitled to the EUR 250 000 allowance.
2. Tax exemption thresholds in the Canton of Zurich used for Switzerland.
3. There was no specific threshold in Austria, but implicitly due to tax allowances persons with wealth below EUR 11 000 were exempt.
4. There was no absolute exemption threshold (in EUR) in Luxembourg but a relative threshold whereby only 50% of the “unitary value” of assets was taken into account for wealth tax purposes.

Source: OECD Questionnaire on Current and Historical Net Wealth Taxes

In recent years, tax exemption thresholds have generally been raised. The Norwegian tax exemption thresholds were NOK 750 000 for single taxpayers and NOK 1 500 000 for married couples in 2012. Since then, they have been increased progressively, respectively reaching NOK 1.48 million and NOK 2.96 million in 2017. In Spain, exemption thresholds were significantly raised when the net wealth tax was reintroduced in 2011. Prior to 2008, general exemption thresholds ranged from EUR 108 182 to EUR 150 000 depending on the region, while the central government threshold is now set at EUR 700 000. The exemption for the main residence was also almost doubled (Durán-Cabré et al., 2017). In France, the tax exemption threshold was raised in 2012 from EUR 800 000 to EUR 1 300 000. Increases in tax exemption thresholds were often motivated by the desire to avoid burdening the middle or upper-middle class, in particular as asset values – most notably housing prices – have increased. Such changes have significant effects on the incidence and equity effects of net wealth taxes.

Due in large part to differences in exemption thresholds, the share of taxpayers subject to the wealth tax has also varied quite substantially across countries. In France, only 351 152 tax households (“*foyers fiscaux*”), or slightly less than 1% of the total number of tax households, were subject to the net wealth tax in 2016. In Spain, there was a considerable decrease in the number of taxpayers subject to the wealth tax between 2007 and 2015, from 981 498 to 188 680, reflecting the significant increase in tax exemption thresholds (see above). In Norway, the share of taxpayers subject to the net wealth tax has been higher, estimated at about 11% of taxpayers in 2016. This share seems low given Norway’s comparatively low exemption threshold but may partly be the result of the very favourable valuation rules for primary residences (see below). It should be mentioned as

well that while the proportion of people paying net wealth tax in Norway has been reduced due to increases in the minimum allowance, the average amount of tax on the part of those who pay net wealth tax has increased in recent years (Norwegian Ministry of Finance, 2017). The highest number and share of total taxpayers subject to net wealth taxes by far is found in Switzerland, where a total of 5 150 529 taxpayers[2] were liable to net wealth taxes in 2016. Differences in numbers of taxpayers are to a large extent a consequence of variations in the levels of tax exemption thresholds, but also reflect the distribution of wealth in countries.

Differences in the levels of the exemption thresholds may in some cases – but not always – reflect differences in the range of taxed assets and in tax rates. For instance, in countries where tax rates are relatively high (e.g. Spain, France), exemption thresholds tend to be high as well. As shown in Figure 4.1, a high threshold implies that wealth above the threshold is taxed effectively at low average rates. High thresholds will therefore often be accompanied by high rates, otherwise tax revenues and ETRs will be low. However, this is not the case everywhere. For instance, the Norwegian wealth tax combines a low threshold and a relatively high tax rate, which makes it unusual and entails a much higher tax burden on the moderately wealthy compared to net wealth taxes in other countries (McDonnell, 2013; Schnellenbach, 2012).

In the discussion in Chapter 3, several arguments have been put forward to justify a high tax exemption threshold. The main justification for having a high exemption threshold is to support equity. Indeed, a high exemption threshold ensures that only the very wealthy pay the tax, prevents the taxation of lifecycle savings, and mitigates the issues related to taxing a presumptive return on assets (see Chapter 3), which end up penalising the holders of low-return assets. A high tax exemption threshold also has the benefit of limiting administrative and compliance costs. From a revenue raising perspective, since wealth is highly concentrated at the top of the wealth distribution, a net wealth tax should allow governments to raise significant revenues even if the exemption threshold is set at a high level (provided that the tax base is broad as recommended below). Ideally, the exemption threshold should also be revised annually or every few years to account for inflation.

Taxed assets, exemptions and reliefs

Under a net wealth tax, residents are typically taxed on their worldwide net assets, while non-residents are generally only taxed on their assets that are located within the taxing jurisdiction. Thus, net wealth taxes are a mix of source-based and residence-based taxation. A key reason for taxing a resident's worldwide net wealth is that it is the sum of taxpayers' assets, wherever they are located, that determines their ability to pay the wealth tax (IMF, 1996). In addition, a wealth tax imposed only on assets held domestically would encourage capital flight so a net wealth tax on worldwide assets of tax residents appears to be appropriate (Iara, 2015). With regard to non-residents, taxing assets that are located within the taxing jurisdiction (i.e. source-based taxation) might distort the international allocation of capital, although non-residents may be exempt from the wealth tax on financial investments made in the taxing jurisdiction (e.g. France). It is important to highlight that worldwide taxation for residents and source-based taxation for non-residents may lead to double taxation and therefore requires provisions preventing double taxation.

The scope of wealth taxes varies across countries. Both income and non-income generating assets are typically taxed under a net wealth tax. They can include land, real

estate, bank accounts, bonds, shares, investment funds, life insurance policies, vehicles, boats, aircraft, jewellery, art and antiques, intellectual or industrial property rights, although different countries apply different exemptions and reliefs (Table 4.3).

As discussed below, net wealth tax bases are often narrowed by numerous exemptions and reliefs motivated by different rationales, the most important being enhancing fairness (e.g. for primary residences) and addressing social concerns (e.g. pension assets), liquidity issues (e.g. farm assets which may not generate sufficient income to enable the owner to pay the wealth tax), supporting entrepreneurship and investment (e.g. for business assets), avoiding valuation and other administration difficulties (e.g. artwork, jewellery, shares in unlisted businesses), and preserving countries' cultural heritage (e.g. artwork, antiques).

Pension assets typically get full relief under net wealth taxes. Among the countries that provided information in response to the questionnaire, all reported net wealth tax exemptions for pension assets. Exemptions for pension assets are justified on social grounds, because of the social benefits that come from retirement income, but also because it difficult to justify both socially and politically taxing individuals on wealth that is not within their present control and from which they cannot withdraw funds to pay the tax (Brown, 1991). However, this creates inequities between different taxpayers, raises fairness concerns, and creates tax planning opportunities.

The exemption for business assets has been justified as a way to encourage entrepreneurship and investment in productive assets, but it has not been universal. The countries that reported exemptions for business assets include France, Spain and Sweden. For the business asset exemption to apply, rules typically require that real economic activities are being performed (possibly excluding activities such as the management of movable or fixed assets, e.g. Spain), that the taxpayer performs a managing role, that income derived from the activity is the main source of the taxpayer's revenue and/or that the taxpayer owns a minimum percentage of shares in the company (e.g. 25% in France and Sweden; 5% in Spain). Other countries generally tax business assets but often grant tax preferences in the form of preferential valuation rules, the exemption of a proportion of assets, the exclusion of certain assets or a lower tax rate (e.g. Germany, Norway, Luxembourg and Ireland).

Other assets that are often exempt from net wealth taxes include artwork and antiques on the basis that they are difficult to value and help protect national heritage. Indeed, five countries reported exemptions for artwork and/or antiques. Exemptions for furniture and jewellery are less common, although some countries do exempt these assets. An alternative to a full exemption for personal and household effects is an exemption for assets below a certain value, particularly for household items such as furniture which are often of limited value.

Other assets, in particular main residences, are often taxed preferentially under net wealth taxes. Tax relief for owner-occupied housing is justified as a way to avoid burdening the middle class whose wealth mainly consists of the primary residence (see Chapter 2) but also because owner-occupied housing does not generate the income needed to pay the tax. However, preferential wealth tax treatment for the primary residence might induce shifts in investments away from productive activities towards residential property, especially if homeownership is already encouraged by other provisions in the tax system (e.g. no capital gains tax for primary residences). Tax relief often takes the form of tax allowances or preferential valuation rules. France and Spain offer tax allowances on the value of main residences, equal to 30% in France and up to EUR 300 000 in Spain. In Switzerland,

as a general rule, housing is taxed at 60% of its market value. Norway offers a particularly favourable treatment for primary residences, which are valued at 25% of their estimated market value for net wealth tax purposes. In both Switzerland and Norway, these very favourable rules may be a way to compensate for the relatively low tax exemption thresholds, which imply that a portion of the middle or upper middle class are subject to net wealth taxes. Other assets also tend to benefit from a preferential tax treatment, including woods and forests, agricultural assets, small savings, life insurance policies, government bonds, charitable donations or investment in SMEs.

Table 4.3. Treatment of assets under net wealth taxes in 2017

Categories of assets	Assets	France	Norway	Spain	Switzerland	Austria (1994)	Germany (1997)	Finland (2006)	Ireland (1978)	Luxembourg (2006)	Netherlands (2001)	Sweden (2007)
Immovable property	Buildings	T	TP	T	TP	T	T	TP	T	T	T	T
	Main residence	TP	TP	TP	TP	T	×	TP	E	T	TP	T
	Woods and forests	TP	TP	TP	TP	T	T	TP	E	T	E	E
	Land	T	TP	T	TP	T	T	T	T	T	T	E
Movable property	Agricultural or rural assets	TP	TP	TP	TP	T	T	T	TP	T	T	E
	Furniture	T	TP	TP	E	T	×	E	T	T	E	E
	Artwork and antiques	E	TP	TP	TP	T	E	T	E	T	E	E
	Jewellery	T	TP	T	T	T	×	T	T	T	TP	E
	Vehicles	T	TP	T	TP	T	×	E	T	T	T	T
Financial assets	Shares	T	TP	TP	T	T	×	TP	T	TP	T	T
	Life insurance	T	E	T	T	T	×	E	×	T	E	T
	Bonds	T	T	T	T	T	×	E	T	T	T	T
	Liquidities	T	T	T	T	T	×	E	T	TP	T	T
	IP rights	T	E	E	T	T	E	E	×	E	T	E
	Pension savings	E	E	E	E	T	E	E	E	E	E	E
	Business assets	E	TP	E	TP	T	TP	T	TP	TP	TP	E

Note: T= fully taxed; E = full exemption; TP = tax preference; x: no information. No information for Denmark, Finland and Iceland.
Source: OECD Questionnaire on Current and Historical Net Wealth Taxes

In general, the tax base should be as broad as possible to avoid creating distortions in savings decisions as well as incentives and opportunities for tax avoidance. As mentioned in Chapter 3, tax exemptions and reliefs generate a number of issues: they reduce horizontal equity and create distortions in investment decisions; they tend to favour non-productive assets (e.g. housing, jewellery); they add to the system's complexity; they generate significant tax avoidance opportunities and ultimately work against the equity goals of wealth taxes as the wealthiest households are best able to shift the composition of their wealth towards untaxed assets. Exempting pension assets and household effects below a certain value may be justified, although if the overall tax exemption threshold is set at a sufficiently high level, many of these exemptions, in particular the ones aimed at addressing equity and social concerns, are not as necessary.

There is some justification for exempting business assets, but clear rules are needed to prevent abuse. As mentioned already, taxing business assets might deter investment in productive assets and generate valuation difficulties. However, exempting or providing significant relief for business assets creates tax avoidance opportunities, particularly at the very top of the wealth distribution, encouraging taxpayers to shelter their assets within their business. In fact, there is strong evidence that this mechanism is being used for tax avoidance purposes (see below). It is therefore critical to have clear criteria restricting the availability of this exemption, focusing on ensuring that real business activity is taking place and that assets are being directly used in the taxpayer's professional activity.

Debt deductibility

Net wealth taxes are levied on net assets, meaning that debts are deductible. As discussed in Chapter 3, from an equity perspective, it make sense to tax net wealth, as net wealth is a better reflection of taxpayers' ability to pay. However, debt deductibility provides incentives to borrow and can encourage tax avoidance. If the wealth tax base is narrow, taxpayers will have an incentive to avoid the tax by borrowing and investing in exempt assets or – if debt is only deductible when incurred to acquire taxable assets – taxpayers will have an incentive to invest part of their savings in tax-exempt assets and finance their savings in taxable assets through debt.

In practice, rules regarding debt deductibility have varied. Some countries have tried to limit tax avoidance opportunities by excluding debts incurred to acquire exempt assets from deductible liabilities (e.g. Austria, France, Germany, Spain and Sweden). For assets whose value is only partly included in the wealth tax base, rules have often been introduced to restrict the deductibility of debts incurred to acquire them. For instance, in France, only 25% of the debts incurred to acquire woods and forests, which are exempt from the net wealth tax for 75% of their value, are deductible.

Valuation rules

To ensure horizontal equity, valuation rules should be similar across assets and based on market values, but in practice valuation rules differ across assets and countries. Assets should ideally be assessed at their market value, defined as the price at which an asset would be traded in a competitive market. However, as mentioned in Chapter 3, one of the biggest practical difficulties with net wealth taxes is determining the value of infrequently traded assets. In some cases, these hard-to-value assets have been exempt. In addition, asset values need to be regularly updated which further increases administrative and compliance costs.

For housing property, market values are usually used. Most countries reported using estimated market values for immovable property. As discussed above, most countries provide tax relief in the form of discounted values for primary residences. In some cases, however, cadastral or fiscal values (i.e. valuation of properties in public registers used for tax purposes) may be used (e.g. Austria). In Spain, the tax base is calculated by taking the highest of three values: the cadastral value used as a basis for the recurrent tax on immovable property, the value assessed by tax authorities for the purpose of other taxes, or the purchase price. Importantly, there can be discrepancies between the housing values used for recurrent taxes on immovable property taxes and those used for net wealth taxes, in particular when the former are based on cadastral values while the latter are based on estimated market values. For instance, in France, while market value is used for net

wealth tax purposes, the recurrent tax on immovable property (*taxe foncière*) is based on cadastral rental values.

Regarding securities which are listed on a stock exchange, approaches are relatively similar. Countries typically use closing stock market values or the average trading price in the period preceding the end of the year (e.g. last 30 trading days in France, last quarter in Spain). In France, taxpayers can choose between the two options (i.e. last quoted price or average trading price in the last 30 trading days). Using average values may be a better option as they can take into account fluctuations.

Valuation is of course more difficult in the case of unlisted shares and approaches differ. Valuing unincorporated businesses and unquoted shares raises difficulties. An important consideration is whether goodwill should be included in the valuation of business assets, or alternatively, whether businesses should simply be valued on the aggregate value of their physical assets. Of course, merely taking the book value of assets substantially understates the value of a business (McDonnell, 2013; Rudnick and Gordon, 1996). There are also issues related to the estimation of a business' stock of physical assets. In practice, approaches have differed. In France, there are three methods for unlisted companies: the mathematical value after the revaluation of assets, the value of the return according to distributed profits, and the value of productivity. As a general rule, the valuation of the company will result from a combination of these different values. In Spain, the book value from the last audited balance sheet is used for the valuation of shares in unquoted companies. If the balance sheet has not been verified or has received a negative audit report, however, they are valued at the highest of: (i) the face value; (ii) the theoretical value resulting from the last balance sheet or (iii) the value resulting from capitalisation at 20% of the average profits of the three financial years before the tax becomes chargeable. Overall, irrespective of the methodology used, a uniform approach is needed for administrative purposes and taxpayer certainty (McDonnell, 2013).

As mentioned in Chapter 3, the date of valuation can also raise issues. If assets are valued on 1 January, then the net wealth tax is partly levied on wealth that will be consumed later in the year. This distorts the timing of consumption decisions as taxpayers will have an incentive to bring their consumption forward to the end of the previous year. This argument is less convincing, however, if the net wealth tax base is broad. A lot of consumption occurring at the top of the wealth distribution actually consists in buying assets that would be taxed under a broad-based net wealth tax (e.g. cars, jewellery, artwork). On the other hand, if assets are valued at the end of the year, taxpayers may be taxed on wealth that they have accumulated during the year which implies that savings would be taxed twice in the same year. In practice, valuation dates have varied, with some countries using as a general rule values on 1 January (e.g. France), and others using as a general rule values at the end of the year (e.g. Spain, Sweden, Switzerland).

In general, asset valuations should be based on market values, possibly at a slightly discounted rate, and valuation rules should be kept simple. While assets should be assessed at their market value, the tax base could be limited to a fixed percentage of that market value (e.g. 80-85%) to prevent valuation disputes but also to take into account certain costs that may be incurred to hold or maintain the assets. The rules should nevertheless be comparable across asset classes to avoid generating large distortions between assets. For assets that are infrequently traded and therefore hard-to-value, including artwork and high-value jewellery, insured values can be used instead of market values. There are also a number of ways to simplify asset valuations. In some cases, values for specific asset classes could be treated as fixed for a few years (e.g. France in

the case of furniture, where estimated value is valid for three years). Alternatively, the value of taxpayers' total net wealth could be treated as fixed for a few years before being re-assessed (McDonnell, 2013). As is often the case, valuation rules that are used for other taxes, in particular for taxes on residential property and inheritances, can be used for net wealth tax purposes as well. Finally, if values are assessed at a specific date, rules should be put in place to prevent abuse aiming at artificially lowering the value of assets just before the valuation date.

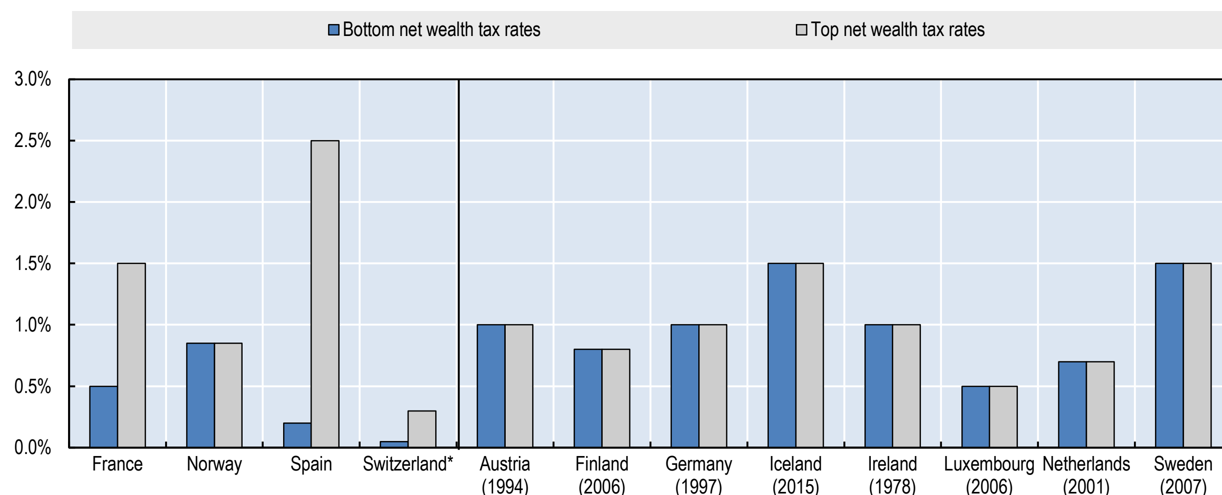
Tax rates

Net wealth tax rates and rate structures have varied across countries, but a majority of countries have applied flat tax rates. The lowest marginal tax rates have generally ranged between less than 0.2% and 1.5%, while the top marginal rates have generally varied between 0.5% and 2.5% (McDonnell, 2013). Spain has the highest top net wealth tax rate, at 2.5%, which applies to income above EUR 10 695 996. Tax rate structures have also varied across countries. Among the countries covered in this chapter, a majority of countries reported flat tax rates including Austria, Germany, Ireland, Luxembourg, the Netherlands, Norway and Sweden. On the other hand, France, Spain and a majority of Swiss cantons apply progressive tax rates that rise with total net wealth (Figure 4.2).

In countries where wealth taxes are local taxes, tax rates can vary quite significantly across municipalities or local governments. In Switzerland, there is considerable variation in wealth tax rates across cantons. In 2012, top wealth tax rates varied by a factor of almost 8, ranging from 0.13% to 1.0%, with the highest rates being levied in the Western French-speaking cantons and the lowest rates found in the small German-speaking cantons of central Switzerland (Brülhart et al., 2017). In Spain, there is a general tax rate schedule at the level of the central government, but the autonomous regions have room to determine their own tax scales. Top tax rates, for instance, vary across regions (e.g. 3.03% in Andalucía, 3% in Murcia, and 2.75% in Cataluña) (Durán-Cabré, 2017).

There has generally been a decrease in tax rates since the 2000s. In Switzerland, there has been a general downward trend in net wealth tax rates, but with wide variations across cantons. Tax cuts have been most significant in the central cantons, where tax competition was vigorous in the early 2000s; but other cantons have also significantly reduced their wealth tax rates. The high-tax western cantons, on the other hand, have not seen much change in their wealth tax rates (Brülhart et al., 2017). In France as well, the top tax rate in 2017 was lower than in the early 2000s. In 2011, the net wealth tax was reformed, with a simplification of the tax rate schedule and a reduction in the top tax rate from 1.80% to 0.50%. The following year, however, a new reform was introduced increasing the number of brackets and lifting the top tax rate to 1.50%. More recently, in Norway, the tax rate was lowered from 1.1% in 2013 to 0.85%, as part of a broader effort to reduce the wealth tax burden (accompanied by progressive increases in the tax exemption threshold and changes in the assessment rules) to promote Norwegian ownership and investment in business assets. In Spain, on the other hand, the Central government tax rate schedule has not changed since 2002.

Figure 4.2. Bottom and top net wealth tax rates in 2017 or in the latest year of operation



Note: * In Switzerland, tax rates in the canton of Zurich. No information for Denmark.
Source: OECD Questionnaire on Current and Historical Net Wealth Taxes

Overall, net wealth tax rates should be low, especially as this report also recommends maintaining a broad tax base. A low tax rate will limit the overall tax burden on capital, which tends to be particularly high when a wealth tax is imposed on top of taxes on capital income. Tax rates should also preferably be progressive to ensure greater equity, in particular given the fact that a flat net wealth tax would penalise the holders of low-return assets who tend to be less wealthy than the holders of high-return assets. Countries could also implement inflation-adjusted net wealth tax rates, which would mean that in high inflation environments, tax rates would be lower. The idea is that the tax would be as much as possible levied on real imputed returns, i.e. excluding the return that compensates for inflation.

Caps on total tax liability

Ceiling provisions or tax caps are common features of net wealth taxes. These often consist in setting a limit to the combined total of net wealth tax and personal income tax liability as a maximum share of income. They are used to prevent unreasonably high tax burdens and liquidity constraints requiring assets to be sold to pay the net wealth tax. In France, the wealth tax ceiling (often referred to as the "*bouclier fiscal*") limits total French and foreign taxes to 75% of taxpayers' total income. If the percentage is exceeded, the surplus is deducted from the wealth tax. In Spain, the aggregate burden of income tax and net wealth tax due by a resident taxpayer may not exceed 60% of their total taxable income. If it exceeds that amount, taxpayers may reduce their net wealth tax liability by the excess amount. However, Spain also has a floor provision requiring that a minimum of 20% of the net wealth tax liability, as originally calculated, be paid. In Switzerland, some but not all cantons have similar ceiling provisions. Indeed, seven (of the 26) cantons have limitation rules based either on the net rent of net wealth, a limit of wealth tax payments as a share of total taxable income or a limit of wealth tax payments as a share of total net wealth. Norway, on the other hand, does not have a tax cap.

In practice, these tax caps, in addition to lowering potential revenues from net wealth taxes, create significant opportunities for tax avoidance. These caps encourage taxpayers

to engage in tax planning to minimise their income, which then allows them to reduce their wealth tax burden through the tax cap. Safeguards should therefore be put in place to avoid tax planning through tax caps (see below).

Tax caps also have real effects that need to be taken into account. For taxpayers with a fixed income level whose tax liability is at or above the tax cap (e.g. total of their income and wealth tax liability equal to or above 75% of their income), owning more wealth does not result in more tax liability. For taxpayers with a fixed level of wealth whose tax liability is at or above the tax cap, however, an increase in income, which will raise the nominal amount of the tax cap, will not only cause an increase in the income tax liability but will also raise the wealth tax liability, thereby generating a strong disincentive to earn more income either through work or other income-generating activities.

Tax filing and payment procedures

Wealth tax filing is generally based on self-assessment. This means that each household is responsible for assessing whether or not they are liable to pay the tax. Tax authorities can of course decide to investigate and audit households to ensure compliance and where taxpayers have not properly self-assessed their tax liability collect tax arrears and/or apply penalties. Nevertheless, relying on self-assessment makes non-disclosure or underreporting – deliberate or not – more likely. This differs from withholding at source and third-party reporting which are well-developed for many forms of capital income taxation such as dividends and interest, although in theory the same tools could be put in place for the taxation of capital stocks (Keen, 2014). In addition to risks of non-disclosure and underreporting, self-assessment imposes a significant compliance burden on taxpayers (Brown, 1991).

Nevertheless, tax filing procedures differ across countries. In most countries, taxpayers have to file a separate wealth tax return (i.e. separate from the income tax return). However, wealth tax returns may be consolidated with income tax returns. In France, if net taxable assets are between EUR 1.3 and 2.57 million, taxpayers do not have to file a separate wealth tax return; assets have to be reported on the income tax return. Above EUR 2.57 million of total net wealth, taxpayers are required to file a separate wealth tax return. In Norway and Switzerland, the wealth tax return is also consolidated with the income tax return.

Regarding tax payment procedures, specific wealth tax provisions allowing payment deferral or payments in instalments are rare. As discussed in Chapter 3, liquidity issues are one of the biggest concerns related to net wealth taxes. Ways to address this issue include provisions allowing for payments to be made in instalments or for payment deferral until assets are sold. Such provisions are rare in practice, although some countries may have general tax rules (i.e. that do not apply specifically to wealth taxes) allowing tax payment deferral or payments in instalments (e.g. Spain).

A few good practices may help enhance tax filing accuracy as well as lower administrative and compliance costs. Concerning tax filing, even if the wealth and income tax returns are separate, it may be good to require both tax returns to be filed at the same time, which would allow wealth tax returns to be cross-checked with income tax returns to verify consistency and obtain information that may be relevant in auditing both taxes (Rudnick and Gordon, 1996). With regard to tax payments, measures allowing payment deferral until assets are sold could be envisaged, although they could generate lock-in effects. A better option would be to allow tax payments in instalments. This type

of relief – allowing taxes to be paid over multiple years at a very low interest rate – could be granted to specific categories of taxpayers (e.g. self-employed businesses, farms) or be based on the composition of taxpayers' assets (Rudnick and Gordon, 1996).

Anti-avoidance/evasion rules

A major concern with net wealth taxes is the ability of wealthier taxpayers to avoid or evade the tax. This has limited the potential of net wealth taxes to achieve their redistributive objectives and has contributed to perceptions of unfairness. This sub-section examines the most common forms of tax avoidance and evasion that countries have faced as well as measures that have been adopted to prevent them.

Different tax avoidance and evasion strategies have been widely used, some of them encouraged by the mobility of financial capital, others by some of the design features of net wealth taxes. The most common forms of avoidance and evasion reported by surveyed countries include using tax shelters available to the wealthiest such as vehicles to conceal the beneficial ownership of assets, avoidance through the exemption for business assets, avoidance through tax cap provisions, avoidance through other tax preferences provided under net wealth taxes, and finally simply holding assets abroad and not declaring them to tax authorities.

Avoidance/evasion through trusts

As discussed in Chapter 3, although they can be set up for perfectly legitimate reasons, trusts can also potentially be used to avoid taxes on net wealth and wealth transfers since they confer the benefits of wealth without transferring the legal ownership of the property. Indeed, they are often used to separate the entitlement to the income that property generates from the entitlement to the property itself (Adam et al., 2011). Thus, rules are needed to prevent tax avoidance through the use of trusts.

Trusts have been problematic in civil law countries which do not recognise them. Indeed, the fact that civil law countries do not recognise trusts has generated uncertainty regarding the taxation of assets held in trusts. In France, there was a significant change in 2011 regarding the wealth tax treatment of trust assets requiring that all assets and rights be included in the settlor's estate – unless the settlor is deceased, in which case the beneficiaries are subject to the tax on trust assets. Spain has adopted a similar approach, although it is not specified in the tax code. According to the Spanish tax authorities, it is also understood that settlors (or beneficiaries when the effective transfer is considered to occur, for example, upon the settlor's death) are subject to the wealth tax with respect to assets held in a trust. In that sense, trusts are disregarded and transactions carried out through trusts are considered as if they were direct transactions effected directly between settlors and beneficiaries, even if trustees have discretionary powers on the management and allocation of assets (Vidal Wagner and García-Perrote Forn, 2012).

Indeed, treating trusts as "see-through" entities seems appropriate. Following the approaches adopted in France and Spain, trusts can be treated as transparent or "see-through" in the sense that the trustee is legally obligated to identify the settlor or beneficiary/ies to tax authorities with the value of assets held in the trusts and then allocate these assets to the settlor or to the beneficiaries on a proportional basis to their assessable wealth (McDonnell, 2013).

Avoidance through the exemption for business assets

The exemption for business assets creates significant tax avoidance opportunities. In Spain, for instance, the government introduced a net wealth tax exemption for the shares of owner-managers in 1994. The exemption applied to business owners substantially involved in the management of their business, who individually owned at least 15% of the business (or with their families at least 20% of the business), and who received over 50% of their labour and business income from this activity. Looking at this exemption, Alvaredo and Saez (2009) showed that it progressively and substantially eroded the wealth tax base. Their empirical results reveal strong shifting effects whereby wealthy business owners re-organised their activities to take advantage of the exemption. In 2003, the rules of the exemption were modified, only requiring an individual stock ownership of 5%. Looking at the reintroduction of the Spanish wealth tax in 2011, Durán-Cabré et al. (2017) also find evidence that taxpayers who declared business ownership in 2011 were more responsive to wealth taxes. This suggests that taxpayers transfer part of their wealth in real estate, bank accounts and non-exempted business holdings to exempted business holdings, which is relatively easy once the business structure is set up (Durán-Cabré et al., 2017).

As mentioned already, there is some justification for the exemption of business assets, but clear rules are needed to prevent abuse. Given that there is strong evidence that this exemption is being used for tax avoidance purposes, it is critical to have clear criteria restricting the availability of this exemption. Requirements for the business asset exemption to apply should focus in particular on ensuring that real business activity is taking place and that assets are being used directly in the taxpayer's professional activity. Businesses whose main activity consists in managing movable or real assets could also be excluded to prevent abuse (e.g. Spain).

Avoidance through tax caps

Tax caps can be used as a tax avoidance mechanism. As discussed above, tax caps generally impose a limit on a taxpayer's total tax liability as a share of their income. There are various strategies that taxpayers can use to reduce their taxable income and thereby ultimately minimise their wealth tax liability. For instance, in France, taxpayers can reduce their income by investing in life insurance policies. If a taxpayer holds a large sum of cash on bank deposit accounts, the money will be included in the wealth tax calculation along with the value of other assets. The interest earned will also be considered as income and subject to PIT. If those savings are placed in an *assurance vie* and left there, however, the value of insurance policies will generally be taken into account in wealth tax calculations but savings will not be considered as generating income until withdrawal. This minimises income, which in turn can be used, through the tax cap, to lower the wealth tax bill. Another mechanism to reduce taxable income – and ultimately the wealth tax liability through the tax cap – is to capitalise cash in a financial holding entity. In the 2017 Budget Law, France sought to target this so called "cash box" practice by enabling tax authorities to capture artificially capitalised income for the computation of the wealth tax ceiling, provided that they can prove that this was done to avoid the wealth tax (PWC, 2017).

Tax caps may be justified to limit taxpayers' overall tax burdens as well as to address liquidity issues. Tax caps may be relevant for taxpayers facing liquidity constraints, as is likely to be the case for retirees, farmers or new businesses. As shown in Chapter 3, METRs including net wealth taxes can also reach very high levels, especially when the

rates of return from households' assets are low, which may also justify capping taxpayers' total tax liability as a share of their income. To limit tax avoidance and the wealth tax liability potentially being reduced to zero, however, tax caps could be accompanied by a floor provision which limits the amount of relief provided by the tax cap (McDonnell, 2013), as is the case in Spain. More generally, strategies to minimise income should be prevented in order to reduce tax avoidance through tax caps.

However, as discussed already, tax caps also have real effects that need to be taken into account and it may be argued that if net wealth taxes are properly designed, tax caps are not as necessary. First, if the exemption threshold is set at a sufficiently high level, liquidity issues become less significant, in particular as liquidity constraints are mostly related to real property. In addition, as mentioned already, instalment relief, allowing the tax to be paid over multiple years at a very low interest rate, could be provided to specific categories of taxpayers including self-employed businesses and farms to limit liquidity issues. Liquidity constraints may also be less problematic than often thought as there is evidence that retirees dis-save or sell their assets to consume (see Chapter 2).

Hiding assets abroad

The combination of increasing capital mobility and the lack of transparency has also encouraged tax evasion, with taxpayers holding assets abroad and not declaring them to tax authorities. The increasing mobility of financial assets as well as the rise of tax havens, combined with the development of information and communication technology and the elimination of barriers to cross-border capital transfers (such as capital controls), have allowed taxpayers to move their capital offshore without declaring it and made the enforcement of capital income taxes and wealth taxes much more difficult (Krenek and Schratzenstaller, 2017). In fact, capital mobility has been a major factor behind the reduction of taxes on capital in the last few decades.

Estimations of offshore wealth, although challenging to calculate, confirm the existence of widespread tax evasion. Recent estimates in the literature have varied from USD 6-7 trillion to USD 22 trillion (Alstadsaeter, Johannesen and Zucman, 2017). Alstadsaeter et al. (2017) estimate that globally the equivalent of about 10% of the world GDP is held offshore, but that this average masks significant heterogeneity—from limited levels in Scandinavia, to about 15% in Continental Europe, and more than 50% in Russia, some Latin American countries, and Gulf countries. The general order of magnitude of these estimates suggests that levying residence-based personal taxes is a considerable policy challenge.

The recent progress made on international tax transparency and the exchange of information is enhancing countries' capabilities to tax capital effectively. International cooperation on the exchange of information on request (EOIR) and on the automatic exchange of information (AEOI) as well as in areas like beneficial ownership will reduce opportunities for tax evasion and ultimately allow countries to tax both capital and capital income more effectively. However, such efforts need to take into account that high-wealth individuals can change their tax residence and even their citizenship in response to high taxes and that, by limiting opportunities for tax avoidance and evasion, the real effects of taxes on capital – in particular on savings and investment – may be stronger (see above).

There will also be challenges to ensure that information exchange is effectively implemented. It will be critical to ensure that a comprehensive EOI network develops amongst all relevant jurisdictions and that persons, assets, and institutions not covered

under existing EOI standards do not offer opportunities for continued tax evasion and thus frustrate the purpose of EOI. It is also important that peer review and technical support are ongoing, particularly for countries and jurisdictions with limited administrative capacity. The other challenge relates to coherently taxing capital income in a world where EOI is effectively implemented. First, the impact of EOI will be limited unless tax authorities have the means and methods to effectively use the information exchanged. Tax authorities should take advantage of new analytical tools and technological advances. The expansion and effectiveness of EOI may also induce taxpayers to shift their wealth towards assets that are not covered by the exchange of information, such as real property. This further stresses the importance of expanding the exchange of information to these assets.

Political economy considerations

The popularity of wealth taxes has varied across countries. Responses to the Net Wealth Tax Questionnaire reveal that wealth taxes were unpopular in a number of countries, which contributed to their repeal. However, experiences in other countries show that they have not been unpopular everywhere. In France, opinion polls have consistently shown a majority of respondents to be favourable to the net wealth tax. Recent evidence, based on online surveys in the United States, also reveals respondents' preference for positive wealth taxation (Fisman et al., 2017).

Differences in the popularity of wealth taxes may partly come from differences in awareness regarding capital income and wealth inequality. Bastani and Waldenström (forthcoming) explore whether information about capital inequality affects attitudes towards capital taxes through a survey sent to a representative sample of 12 000 Swedish adults in which they expose different parts of the target population to different information treatments regarding the distribution of capital income. One group receives special information about housing wealth, one receives special information about inherited fortunes, and the last group does not receive any special information at all. Because of the random assignment of individuals into these three groups, differences in attitudes between the different groups can be interpreted as a causal effect of this information. A similar argument may be made for inheritance taxes – i.e. addressing the lack of information on the inter-generational persistence of wealth gaps may help make these taxes more politically acceptable – although the unpopularity of inheritance taxes comes primarily from their salience and unfortunate timing.

In addition, the way wealth tax reforms are packaged is likely to affect how taxpayers view these taxes. If the introduction of a wealth tax or an increase in the existing wealth tax is part of a more comprehensive tax reform and goes hand-in-hand with a decrease in other taxes, especially in labour taxes which almost everyone is subject to, it may be more acceptable politically. Packaging a wealth tax reform as part of broader reform aiming at tax mix shifts as opposed to overall tax burden increases may increase the chances of the reform being adopted.

Box 4.2. Net wealth tax design recommendations

- Low tax rates, especially if the net wealth tax comes on top of capital income taxes;
- Progressive tax rates;
- Limited tax exemptions and reliefs;
- An exemption for business assets, with clear criteria restricting the availability of the exemption (ensuring that real business activity is taking place and that assets are directly being used in the taxpayer's professional activity)
- An exemption for personal and household effects up to a certain value;
- Determining the tax base based on asset market values; although the tax base could amount to a fixed percentage of that market value (e.g. 80-85%) to prevent valuation disputes and take into account costs that may be incurred to hold or maintain the assets
- Keeping the value of hard-to-value assets or the value of taxpayers' total net wealth constant for a few years to avoid yearly reassessments;
- Allowing debts to be deductible only if they have been incurred to acquire taxable assets – or, if the tax exemption threshold is high, consider further limiting debt deductibility;
- Measures allowing payments in instalments for taxpayers facing liquidity constraints;
- Ensuring transparency in the treatment of assets held in trusts;
- Continued efforts to enhance tax transparency and exchange information on the assets that residents hold in other jurisdictions;
- Developing third-party reporting;
- Establishing rules to prevent international double wealth taxation; and
- Regularly evaluating the effects of the wealth tax

Notes

[1] As mentioned, this chapter is based on the tax rules that were in place as of 1 September 2017. Since then, France has replaced its net wealth tax ("*impôt de solidarité sur la fortune*") with a new real estate wealth tax ("*impôt sur la fortune immobilière*"), with effect from 1 January 2018.

[2] The figure includes some double counting when taxpayers own wealth in more than one canton.

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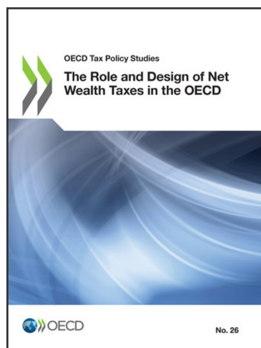

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