



FISCAL AFFAIRS

Taxation of Capital, Wealth, and High Incomes

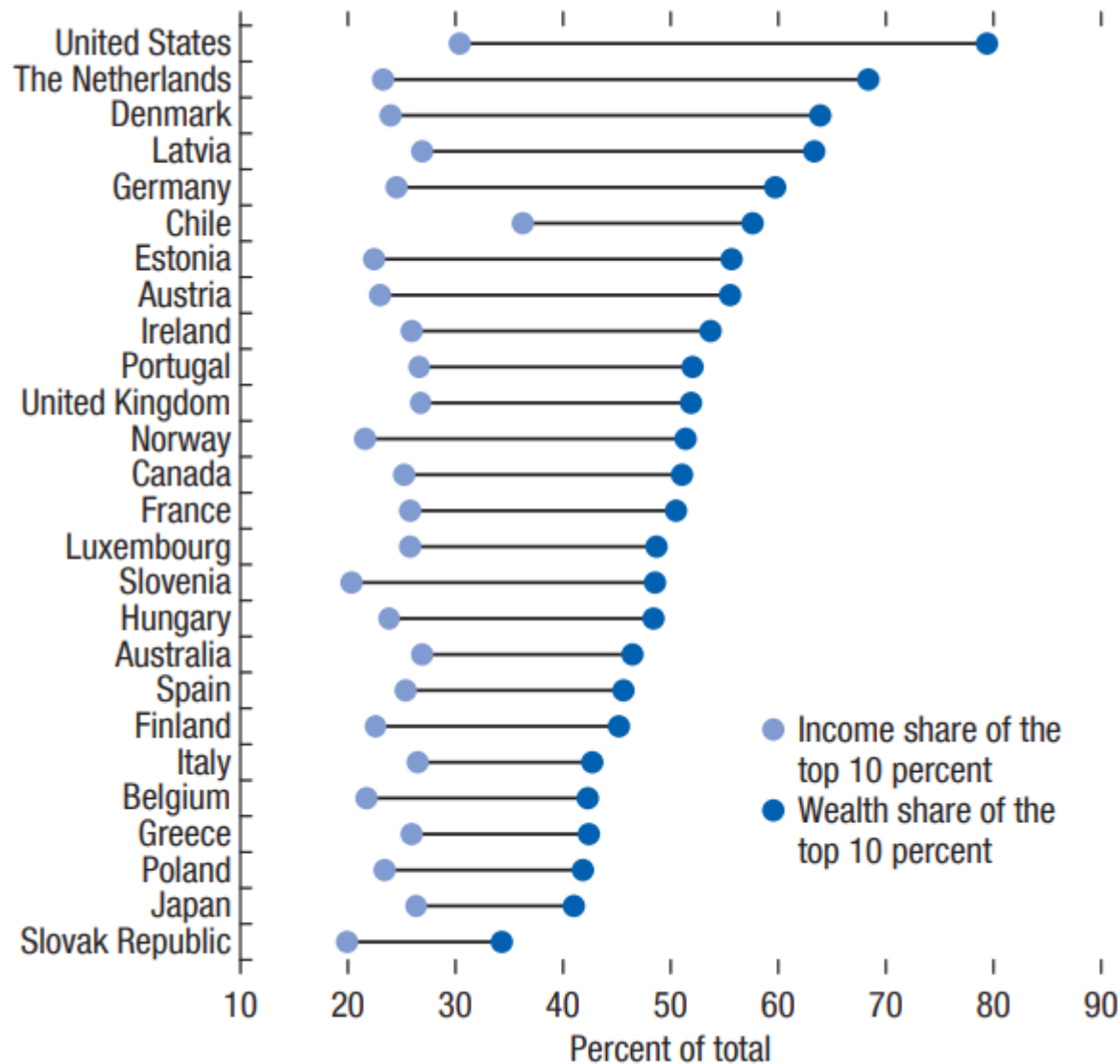
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Introduction

- High income inequality
- Even greater wealth inequality
- Tax is the most direct tool to address this
 - ▶ Spending policy can address poverty, but not inequality at top
 - ▶ Other important policies
 - ◆ Competition
 - ◆ Anti-corruption
 - ◆ Public procurement, concessions, etc.



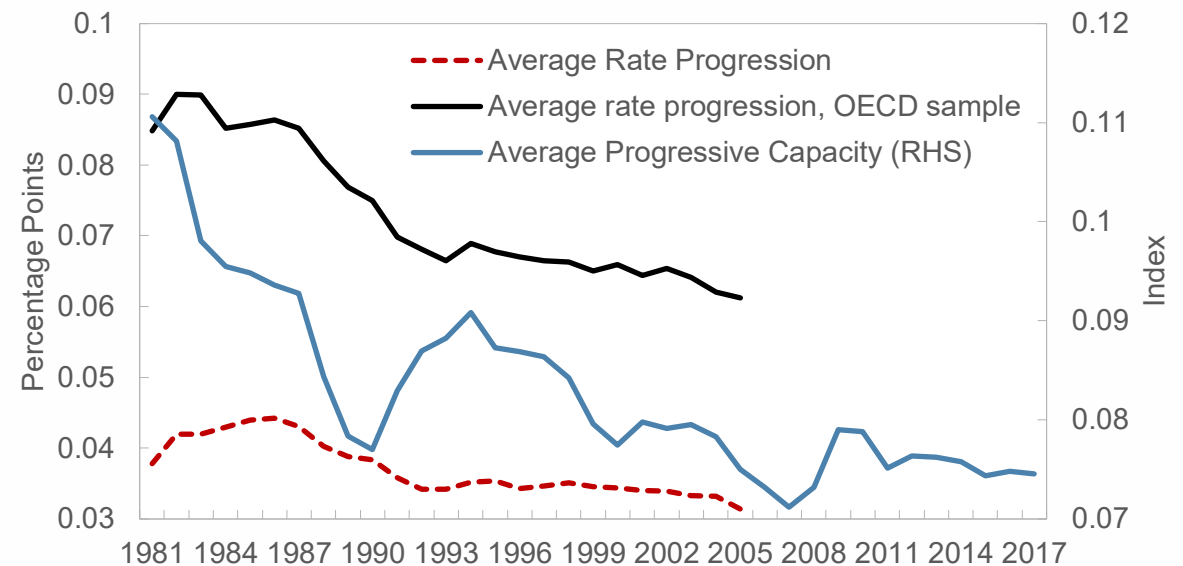
Source: Fiscal Monitor, April 2021; Data: OECD.

Challenges in the Taxation of Capital, Wealth, and High Incomes

- **Taxing Income**
- Taxing Wealth and Wealth Transfers
- Conclusions

Labor income is typically taxed progressively...

- Labor income taxes mostly progressive
 - ▶ Somewhat undone by social security
- Progressivity has declined over time
 - ▶ Even though progressivity does not appear to reduce growth

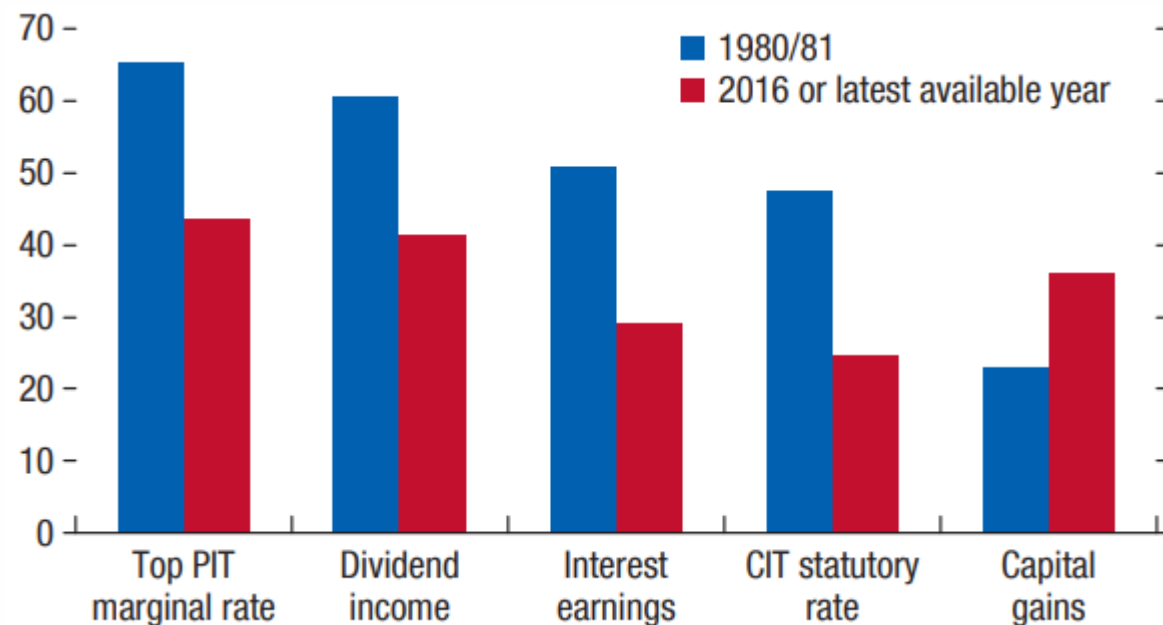


Source: Gerber, Klemm, Liu, Mylonas (2020)

...but capital income is taxed at lower rates...

- Most income of very rich is not in the form of labor income
 - ▶ E.g., US 2017: income of top 0.001% taxpayers
 - ◆ 8.7% wages
 - ◆ 56% capital gains
- Capital income often taxed at lower rates
 - ▶ Capital gains, interest
 - ▶ “Carried interest”
 - ▶ Dividends often taxed more highly (effectively double taxed)
 - ◆ Though: tax incentives/avoidance at corporate level

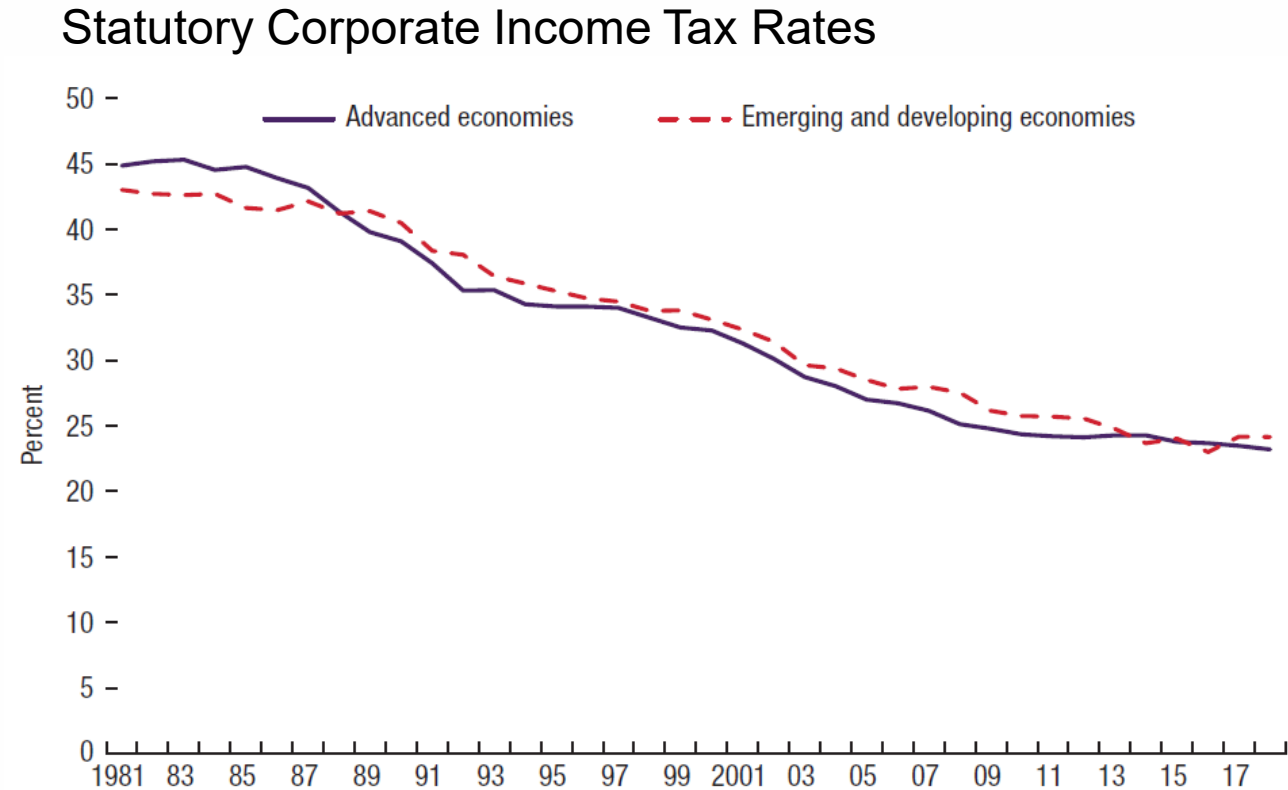
Top Income Tax Rates, OECD averages



Source: Fiscal Monitor, April 2021; Data: Carey, Chouraqui, and Hagemann (1993), Harding and Marten (2018).

...affected by declining corporate income taxes...

- Corporate income tax is important to enforce broader income tax
- Rates have been driven down
 - ▶ Tax competition
- Agreement on major international reform reached Oct. 8, 2021
 - ▶ 136 IF members signed
 - ▶ 15% minimum tax
 - ◆ Not yet implemented (foreseen 2023)
 - ◆ Thresholds, carveouts, exemptions

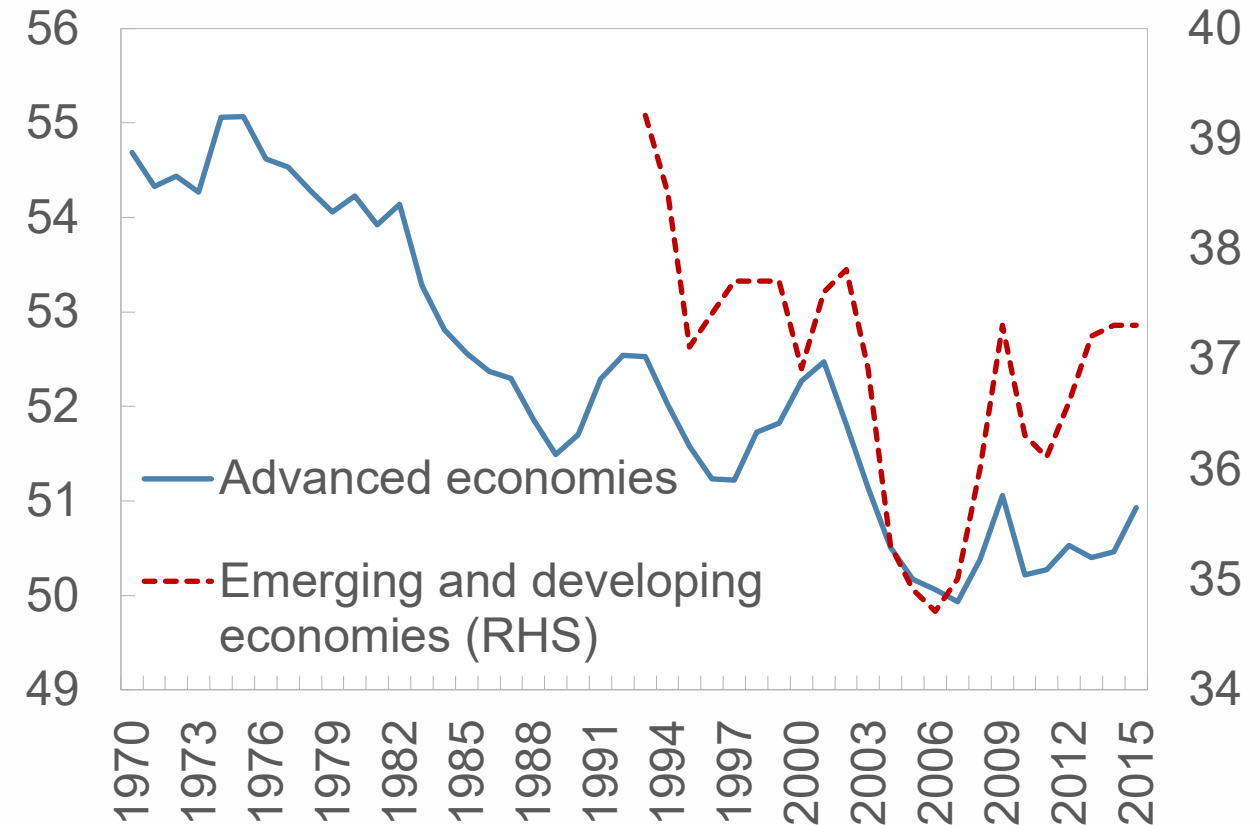


Source: De Mooij, Klemm, and Perry (2021)

...for reasons that may not hold anymore.

- Economic literature:
 - ▶ Classic results: taxing capital income distorts savings, optimal tax on normal return is zero
 - ▶ Recent papers: capital income tax can enhance equity and efficiency
- Moreover:
 - ▶ Rents
 - ▶ Endowments, tax avoidance
- Current and future trends:
 - ▶ Rising share of capital income
 - ▶ Automation, robot adoption, AI

Labor share of income (percent)



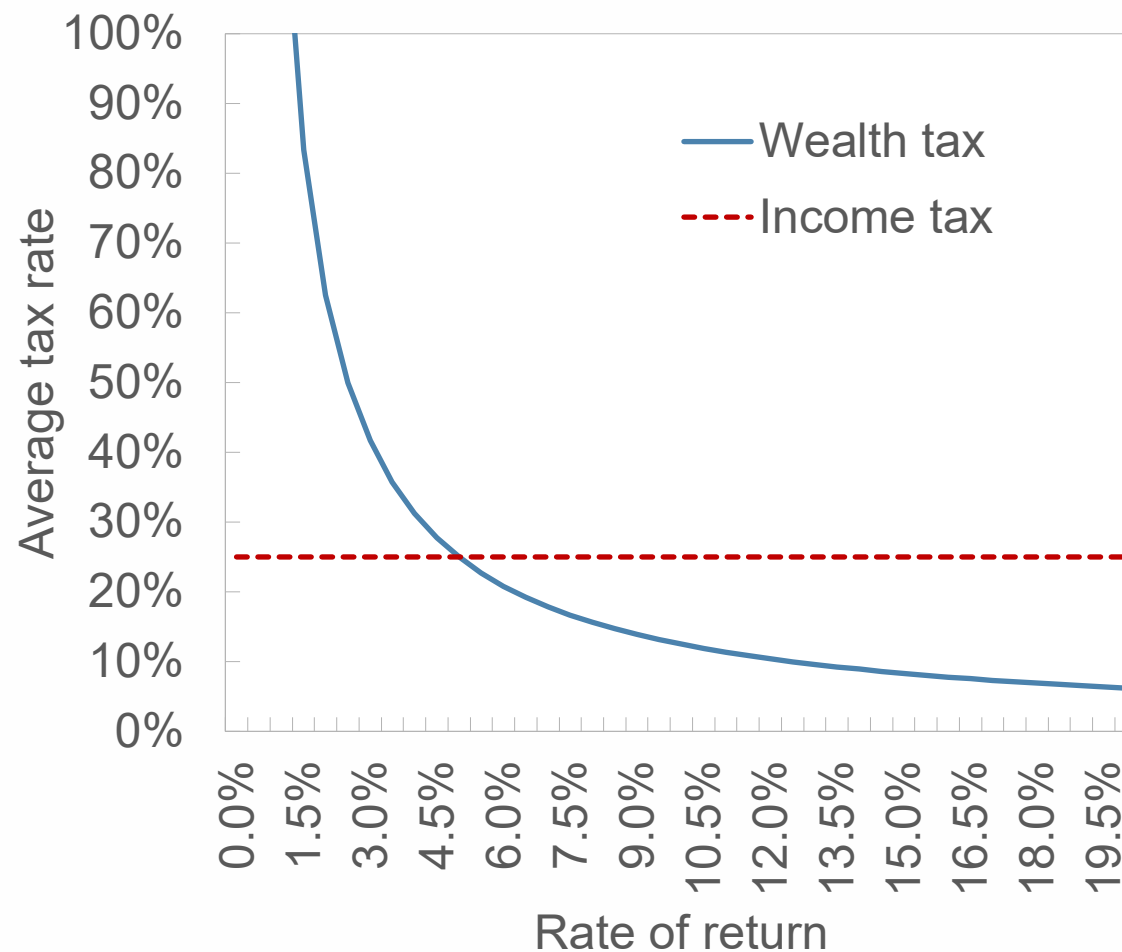
Source: IMF WEO, April 2017.

Challenges in the Taxation of Capital, Wealth, and High Incomes

- Taxing Income
- **Taxing Wealth and Wealth Transfers**
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Wealth taxes are another option...

- Income versus wealth tax
 - ▶ Flow versus stock
 - ◆ Wealth tax: Like taxing a fixed (normal) return
- Additional wealth tax
 - ▶ Recent proposals for high (wealth-reducing) taxes, with very high thresholds
- Avoidance, evasion, valuation difficulties
 - ▶ Experience over past decades
 - ▶ Renewed interest (helped by transparency initiatives)

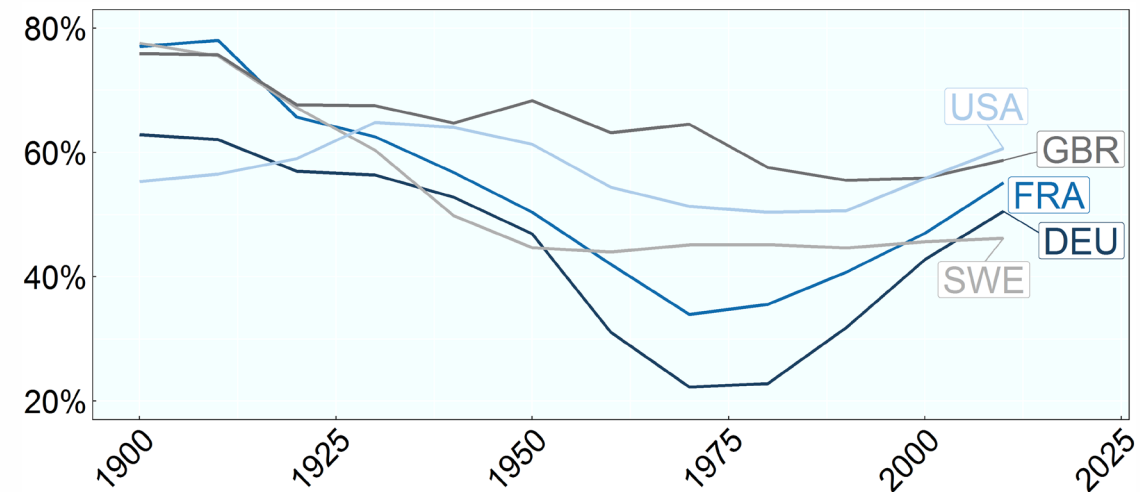


Assumptions: 25 percent capital income tax rate or 1.25 percent wealth tax

...or wealth transfer taxes.

- Inheritance versus estate tax
 - ▶ Former more aligned with future wealth distribution
- Need strong anti-avoidance
 - ▶ Gifts inter vivos
 - ▶ Trusts
 - ▶ Assets with favorable treatment (e.g., housing, companies)

Inherited wealth in percent of private wealth, 1990-2010



Source: OECD (2021), Inheritance Taxation in OECD Countries, OECD Tax Policy Studies, which lists as original source Alvaredo, Garbinti, and Piketty (2017), data for Sweden in Ohlsson, Roine, Waldenström (2020).

Challenges in the Taxation of Capital, Wealth, and High Incomes

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Conclusions

- Can raise progressivity of labor tax in many countries...
- ...but going after capital (or notionally capital) income more important
 - ▶ Includes domestic loopholes...
 - ▶ ...and international corporate income tax reforms
- Wealth taxes are not a good **alternative** to capital income taxation...
- ...but can be considered as an additional tax in some circumstances
- Wealth transfer taxes can reduce perpetuation of inequities over generations