FABIAN POLICY REPORT

A UNIQUE CONTRIBUTION

Reducing budget deficits and tackling inequality with a one-off wealth tax, by Nick Donovan. Foreword by Dan Jarvis MP.

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ACKNOWLEDGEMENTS

I would like to thank Professor Sir Anthony Atkinson for pointing me towards the history of Labour's one-off taxes on unearned income; Dr Margit Schratzenstaller-Altzinger, Deputy director of the Austrian Institute of Economic Research for helpful comments on an earlier draft; Andrew Harrop and Ed Wallis of the Fabian Society, Ulrich Storck and Silke Breimaier of the Friedrich Ebert Stiftung, and Max Lawson and David Quentin for their invaluable help and advice. Any errors that remain in this report are mine alone.

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Designed by Soapbox, www.soapbox.co.uk

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First published in June 2016

ONLINE ANNEX

Worked examples of how the tax would operate in a practice for a range of (illustrative) taxpayers can be found at: www.fabians.org.uk/publications/a-unique-contribution

PREFACE

The Panama Papers have put questions of wealth, tax and inequality right back at the top of the political agenda. The unprecedented data leak provided perhaps the most vivid chapter yet in what has become one of the defining stories of our times: an untrammelled elite, whose extreme wealth allows them to play by a different set of rules to the rest of society.

And yet, it also highlighted the political conundrum which faces parties of the left across the European continent. While the gap between the rich and poor grows ever wider, and popular anger at rising inequality grows more visceral, social democrats still seem unable to profit politically. The 'progressive moment' that the financial crisis of 2007–8 was supposed to herald has in fact proved the opposite, with fiscal conservatism and political populism ruling the day. Social democrats now find themselves in a double bind. They seem unable to excite voters on the left, who seek proof that they will tackle rampant inequalities, and also unable to reassure the electorate as a whole that they will manage the economy well.

Centre left parties across Europe are looking for new ways to tackle inequality, and a progressive approach to taxation must be one means to achieve that goal. The Friedrich-Ebert-Stiftung and the Fabian Society opened the debate last year, with a collection of essays called *Tax for our Times: How the left can reinvent taxation*. We now build on this with a new proposal to enhance social justice through taxation.

The 'unique contribution' – a one-off levy on the passive wealth of the super-rich – is a pragmatic measure that can be used to reduce the deficit and build up resilience to future economic shocks. But it conveys radical intent by doing so in a way that socialises a share of the staggeringly unequal – and sometimes unearned – financial rewards that the super-rich are able to generate, not from their hard work but from wealth begetting wealth. To UK readers, the proposal will have historical echoes of the windfall tax on the utilities, introduced by Tony Blair. But the idea will attract interest across Europe.

Action on global wealth should be taken by countries working together in partnership, which is why we are so pleased that our two organisations are jointly publishing this report. We are keen to learn lessons and share ideas across borders, and this proposal for a one-off wealth levy draws explicitly from debates and research in Germany. But also, in a globalised world, policy co-ordination is crucial, when capital crosses borders and jurisdictions so easily. It is vital that social democrats work together to develop the right proposals to fit our own domestic economic and political contexts; but also co-ordinate internationally to present a united front in tackling tax avoidance and wealth inequality, so that we all play by the same rules.

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FOREWORD

By Dan Jarvis, Labour MP for Barnsley Central

Repairing our social fabric

Labour used the sense of national purpose that followed the second world war to build the national health service and the welfare state. These institutions joined universal education, juries and national service in bringing together individuals from all backgrounds. More recently Labour has laid the building blocks for universal childcare and as I have argued, for a renewal of national citizen service – a voluntary service for all our young people.

Today, powerful forces – which the Tories either condone or accelerate – are tearing at the ties that bind us together.

Inequality of wealth took off during the Thatcher years. Extreme inequality tempts some in our society to opt out of Britain's shared institutions: state schools, NHS hospitals, even taxes. This effect varies in its significance. Elite schooling turns inequality of outcome into inequality of opportunity – as the wealthy buy better outcomes for their children. Private hospitals insulated the wealthy from the shared experience of the shocking decline in the NHS during the Thatcher years. But nothing is more corrosive to the body politic than tax avoidance.

Most ordinary people – nurses, shop workers, soldiers – pay their taxes through PAYE. Small business owners are aware of every penny they send off to the taxman. It sticks in their craw that others, believing that taxes are 'just for the little people', arrange their affairs so that they can reduce their taxes through fictitious film schemes or Swiss bank accounts. The Panama Papers revelations feed the suspicion that there's one rule for them, and another for the rest of us.

This sense of unfairness has been exacerbated by austerity. In the aftermath of the global financial crash George Osborne has placed the burden for reducing the deficit on the narrowest shoulders. He's cut tax credits for those in work, attempted to cut disability benefits, downsized our military and starved the public sector.

What's worse is that none of those paying for the repercussions of the financial crisis had anything to do with causing it. Last year 2,274 pupils in my constituency were eligible for free school meals. More than half the children in Barnsley Central leave school without five good GCSEs. Not one of those kids owned a credit default swap or a collateralised debt obligation – the financial instruments that helped cause the banking crisis. Yet, according the Institute for Fiscal Studies, real school spending per pupil in England will fall by 8 per cent in this parliament, while spending on further education fell by 14 per cent over the last five years. This is both poor ethics and bad economics.

In place of cuts

The British public expect Labour to be a safe pair of hands with their money. Specifically, they expect the deficit to be reduced over the medium term – but for us to do so in a fair way. This is why the idea of a unique contribution is worthy of consideration – it opens up the possibility of a one-off response to a once in a lifetime financial crisis.

Rather than year after year of grinding cuts, or a heavier tax burden on income and earnings, a one-off levy on net wealth over £10 million could make a significant dent in the deficit. Moreover, it proposes to do so in a fair way: the threshold is so high that only those who are truly wealthy pay the levy, there are exemptions for earned income and assets used for trading, it is one-off so those who pay it aren't driven away, it exempts many difficult to value objects such as family heirlooms and it is largely non-intrusive except for those who may have dodged taxes in the past.

Indeed, for those who have avoided tax in the past, the unique contribution has a role in restoring the status quo. If the levy raised more revenue than expected the proceeds could be used to cut income taxes or national insurance contributions.

The proposal sits in a long Labour history of thinking about one-off taxes to repair public finances or damage to our social fabric. After the first world war, Labour proposed a one-off levy. After the second world war, Stafford Cripps imposed a 'special contribution' – a measure strongly supported by Roy Jenkins, who introduced his own version of the levy when chancellor in 1968. New Labour introduced the 'windfall tax' on the excess profits of privatised utilities to pay for the New Deal welfare-to-work scheme for the long term unemployed. Each proposal or measure was suited to its time.

A unique contribution would certainly have made sense instead of George Osborne's VAT rises and spending cuts he imposed in 2010. The economic and fiscal circumstances when Labour next comes to power will be different to those of 2010 or today – so the unique contribution might not be suitable then. However, this type of thinking is what Labour needs to be doing in opposition.

We must demonstrate that we are fiscally responsible and yet present a clear alternative to the Tories. When we do enter government again our job will be to rebuild our public services, invest in our economy and narrow inequalities. Our country is fracturing constitutionally and socially, our job will be to bring our country together again.

SUMMARY

THIS REPORT PROPOSES a one-off levy on the passive wealth of the super-rich, with a more stringent approach taken with those who have used tax havens or domestic tax avoidance schemes in the recent past. Revenue would be used to reduce the deficit, thereby easing pressure on spending cuts and taxes on income and earnings.

Importantly, it would also address inequality, which has become so extreme that a household at the top 1 per cent has wealth that is at least 228 times greater than a household in the bottom 10 per cent.

Much of the wealth of the super-rich is held as financial assets such as shares, bonds and derivatives. This generates passive income, which in turn begets passive wealth. Some of this wealth is routed through tax avoidance vehicles and offshore tax havens. Much of it would have been 'under-taxed'.

In the face of such inequality of wealth, citizens can never be truly equal participants in public life, and the super-rich can use their influence to shape the rules of the game to their advantage.

Other countries have annual wealth taxes which successfully raise small but significant sums. However, the recurrent nature of annual taxes might lead to several distortionary effects such as increased avoidance, emigration or a reduction in investment or entrepreneurial risk taking. These effects are often overstated but, even so, it is possible to avoid them with a one-off levy. The most detailed recent proposal for a one-off levy has been in Germany. Analysts at the Bundesbank and elsewhere have found that it produces few distortions which might inhibit growth, and could raise up to €100bn.

The unique contribution proposed in this report is a one-off levy on long-term residents of the UK with net passive wealth over £10 million, with a second, higher, rate charged on net wealth which exceeds a threshold of £20 million. 'High risk' taxpayers – those who have moved assets offshore or used domestic tax avoidance schemes, or who are non-doms who pay the remittance basis charge – would be required to undergo a full, stringent valuation exercise. However, 'low risk' taxpayers will have access to a streamlined assessment of their wealth based upon past declared unearned income, avoiding difficult assessments of family heirlooms. The simplicity of this calculation removes the objection that wealth taxes are necessarily intrusive. Unearned income would include all income except that from employment or trading.

It is not known how much revenue might be raised as the tax base – the wealth of the super-rich – is largely *terra incognita;* the unique contribution itself would be an exercise in map making. However, the proceeds would take a significant bite out of the current budget deficit. For example, the recent highly controversial tax credit cuts were costed at around £4bn per annum or about £20bn over the parliament. It should be possible for a one-off levy to raise sums in the same order of magnitude. If the levy raises more than is needed to reduce the deficit then proceeds could be used to reduce public debt (as a ratio of GDP) or perhaps to reduce income taxes on low to middle income earners.

The anger that the Panama Papers evokes stems from the sense that there is one rule for those that surfed the offshore waves of the financial bubble, and another for the rest of us. Worse still, much of the burden of deficit reduction has been placed on those who had no hand in the financial crisis – by those who pay their taxes by PAYE, or who depend on social security to get by. The Panama Papers and the Conservatives' post-crash fiscal choices reveal a society that has become unbalanced. The unique contribution is designed to be as unobtrusive as possible for the likes of JK Rowling or James Dyson, who earned their money and paid their taxes, while taking a strict approach to calculating the wealth of those who may have underpaid taxes in the past through the transfer of funds to tax havens or the use of avoidance schemes.

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A Unique Contribution

Reducing budget deficits and tackling inequality with a one-off wealth tax

by Nick Donovan

INTRODUCTION

THE REPERCUSSIONS OF the global financial crisis still shape European politics.

First, large public deficits developed as governments, in order to avoid a global depression, bailed out banks and propped up economies. This gave an opening to politicians on the right to place deficit reduction as the central economic task in the mind of the public – a place where it remains.

Second, as the need to raise revenue became acute, the public view of the world of tax-avoiding offshore finance swiftly moved from indifference to anger. Scandal after scandal – most recently the Panama Papers – have revealed how some of world's wealthiest have exploited gaps in the system to keep their wealth away from the tax authorities.

Third, public interest in the sheer scale of wealth inequality has partly multiplied because parties of the right have chosen to reduce the deficit largely through spending cuts – which disproportionately affect the poorest – rather than tax rises. It is difficult to imagine that Thomas Piketty's *Capital in the Twenty First Century*, a 700 page economics book containing equations, would have sold over 1.5 million copies in the years before the financial crisis.

And yet, conservatives and populists have proved more adept than the left in adapting to the changed political landscape. The cause of the global financial crisis was the build-up of over-leveraged credit in an under-regulated banking system in which the excesses of financial capitalism were too easily transmitted to the real economy. Yet, against the expectations of some, the left was not the beneficiary of the crisis. Similarly, while public anger at tax avoidance and concern over the vast scale of inequality is acute, there is no guarantee that voters will turn to the left for the answers. The challenge is to provide an authentically social democratic answer to the new politics of the financial crisis and ensuing public deficits – while appealing to the public as they are, not as we wish them to be.

> In the face of such inequality of wealth, citizens can never be truly equal participants in public life

It is in this spirit that this report proposes a 'unique contribution': a one-off levy on the passive wealth of the super-rich (those with net wealth over £10 million). The unique contribution takes a more stringent approach with those who have used tax havens or domestic avoidance schemes in the past. Revenue would be used to reduce the deficit, thereby easing pressure on spending cuts and taxes on income and earnings.*

It would also, at least temporarily, reduce inequality. Inequality of wealth is so extreme in the UK that a household at the top 1 per cent of the wealth distribution has wealth (£2.9 million or above) that is 228 times higher than a household just in the bottom 10 per cent of households (£12,550).[1] Estimates of the share of total wealth held by the top 1 per cent vary from 12.7 per cent to 23.3 per cent.[2] A rough comparison of the total £576 billion wealth owned by the top 1,000 shows that it is greater than the total wealth of the bottom 40 per cent of UK households (who own £496bn), is more than pension wealth of the bottom 60 per cent (£491 billion), and exceeds the "bottom" 90 per cent of UK households' (non-pension) financial wealth (£546 billion).[3]

Much of the wealth of the super-rich is held as financial assets such as shares, bonds and derivatives. This generates passive income, which in turn begets passive wealth. Some of this wealth is routed through tax avoidance vehicles and offshore tax havens. Some $140bn of UK households' wealth is held in Switzerland, with many tens of billions held in other secrecy jurisdictions.[4] Much of this wealth would have been 'under-taxed'.

In the face of such inequality of wealth, citizens can never be truly equal participants in public life, and the super-rich can use their influence to shape the rules of the game to their advantage. Inequality of outcome is then used to purchase inequality of opportunity for future generations.

It is for these and other more prosaic reasons, such as the need to raise revenue, that other countries such as Norway, France and Switzerland have annual wealth taxes which successfully raise small but significant sums. The recurrent nature of annual taxes might lead to several distortionary effects such as increased avoidance, emigration or a reduction in investment or entrepreneurial risk taking. These effects are often overstated but, even so, it is possible to avoid them – and associated political obstacles – with a one-off levy. This is an idea which has been proposed frequently when public debt has reached high levels – by David Ricardo after the Napoleonic wars, by Sidney Webb and Arthur Cecil Pigou

*This report should be read alongside a previous Fabian Society paper in which I proposed that Labour adopt a Financial Sector Revenue Stabilisation Account – a 'rainy day fund'. This is a type of sovereign wealth fund to be used in a future banking crisis. Our tax revenues – which collapsed in 2008 – are highly dependent on an unstable financial sector. Together, this 'rainy day fund' and a 'unique contribution' would form a visible yet responsible reply to the accusation that Labour doesn't 'fix the roof while the sun was shining'.

after the first world war and by J.M. Keynes and Friedrich von Hayek after the second world war. In Germany a one-off tax, the so-called *Lastenausgleich*, was actually levied after the war. Indeed the most detailed recent proposal for a one-off levy has been in Germany. Analysts at the Bundesbank and elsewhere have examined proposals and found that it produces few distortions which might inhibit growth, and could raise up to €100bn by taxing the top 0.6 per cent of the German adult population.

The unique contribution proposed in this report is a one-off levy on long-term residents of the UK with net passive wealth over £10 million, with a second, higher, rate charged on net wealth which exceeds a threshold of £20 million. 'High risk' taxpayers – those who have moved assets offshore or used domestic tax avoidance schemes, or who are non-doms who pay the remittance basis charge – would be required to undergo a full, stringent valuation exercise. However, 'low risk' taxpayers will have access to a streamlined valuation method. Their net wealth will be calculated by adding together the value of their main residence (minus any mortgage), their private pension wealth and their deemed investment wealth. Deemed investment wealth can be easily calculated by tax authorities using data on unearned income submitted on previous tax returns. Unearned income would include all income except that from employment or trading. Wealth which doesn't generate unearned income, such as jewellery and other family heirlooms, is excluded from the calculation. The simplicity of this method removes the objection that wealth taxes are necessarily intrusive.

Although some who have kept their undeclared wealth hidden offshore, refusing to participate in remarkably generous tax amnesties, might continue to so, they will still be taxed on their visible wealth. The failure to declare themselves as high risk will attract serious penalties if found out at a later date. In recent years, 'common reporting standards' have been agreed between countries, whereby both banking information and, sometimes, beneficial ownership details will be automatically exchanged across an increasing number of jurisdictions. This development, in addition to a variety of leaks about offshore finance, means many might consider coming clean. Now is a more auspicious time to launch such a levy than ever before.

The unique contribution tilts the tax system away from earned income towards unearned wealth

It is not known how much revenue might be raised as the tax base – the wealth of the super-rich – is largely *terra incognita;* the unique contribution itself would be an exercise in map making. This uncertainty is common when other taxes which deal with offshore finance have been introduced, such as the annual tax on enveloped dwellings and the UK-Swiss tax deal. However, the proceeds from this one-off levy would take a significant bite out of the current budget deficit. For example, the recent highly controversial tax credit cuts (which still persist in the future plans for universal credit) were costed at around £4bn per annum or about £20bn over the parliament. It should be possible for a one-off levy to raise sums in the same order of magnitude. If the levy raises more than is needed to reduce the deficit, then proceeds could be used to reduce public debt (as a ratio of GDP) or perhaps to reduce income taxes on low to middle income earners.

The unique contribution also has a restorative purpose. People do not begrudge the likes of JK Rowling or Sir James Dyson their wealth. For both author and entrepreneur earned their money through hard work, and then have proceeded to play the game fairly. Both have been clear about not using tax havens or avoidance schemes. The sense of unfairness that the Panama Papers evokes stems from the belief that there is one rule for those that surfed the offshore waves of the financial bubble, and another for the rest of us. Worse still, much of the burden of deficit reduction has been placed on those who had no hand in the financial crisis – by those who pay their taxes by PAYE, or who depend on social security to get by. The Panama Papers and the Conservatives' post-crash fiscal choices reveal a society that has become unbalanced. The one-off levy is designed to be as unobtrusive as possible for the likes of JK Rowling, while taking a strict approach to calculating the wealth of those who may have underpaid taxes in the past through the transfer of funds to tax havens or the use of avoidance schemes. The unique contribution is thus partly a conservative exercise in rebalancing: a return in the direction of the *status quo ante* – through increasing the contributions made by those who may have previously avoided paying their fair share.

The use of the word conservative is not just rhetoric. This is one of the most cautious proposals possible for taxing wealth, perhaps more so than taxing gifts or introducing regular annual wealth taxation. Even inheritance tax is more radical as it has a much lower threshold and a high 40 per cent tax rate, although it is avoided by many. The unique contribution is a one-off, with a high threshold, it tilts the tax system away from earned income towards unearned wealth, it exempts family heirlooms and its assessment method is intrusive only for those who may have underpaid tax in the past. It lies firmly within a moderate Labour tradition of similar measures: from Stafford Cripps' 'special contribution', to Roy Jenkins' 'special charge', to Tony Blair's windfall tax on the excess profits of the privatised utilities. While in opposition, the centre left needs to rejuvenate its thinking. The unique contribution is an attempt to respond to a British public who are as concerned about the deficit as they are about inequality.

1. THE SCALE OF THE FISCAL CHALLENGE

The legacy of the financial crisis has left us with much higher public debts…

Due to our dependence on the City of London, the UK was particularly badly hit by the global financial crisis. This economic shock was enormous. The UK suffered its first run on a bank in 150 years in 2007. Economic confidence and industrial output plummeted across the globe. At one point there was a real risk that several British banks would not open their doors on Monday morning. Labour's response to the global crisis was, entirely correctly, to prop up the economy and recapitalise the banks.

However, this has left a legacy of high public debt and annual deficits. The last Labour government adopted the 'sustainable investment' rule; this fiscal rule required the government to keep the public sector debt (net of its short-term financial assets) at a 'stable and prudent' level, defined as less than 40 per cent of national income (GDP). Public sector net debt was 40.9 per cent when Labour came to power in 1997 and remained between 30.9 per cent and 38.7 per cent, until the global financial crisis hit the UK in 2007–8.[5] Now, in 2015–16, public sector net debt is double the pre-crisis figure – 83.5 per cent – and is only projected to fall to 74.7 per cent by 2020–21.[6]

…there are good reasons to reduce public sector net debt interest over the medium term…

There are two underlying reasons for wanting to reduce public sector net debt over the medium term. The first is that, although the cost of borrowing is low at the moment (enabling the UK to sensibly borrow for infrastructure investment at historically low rates), eventually interest rates will rise, meaning that as bonds mature and the debt is refinanced, future generations will be spending more on debt interest, as opposed to, say, spending on education and the NHS. This shouldn't be a problem if the borrowing is for investment that creates assets (for example, workers with higher skills, useful infrastructure) which make us richer in the future. However, over the medium term an ageing population means that non-investment, 'day-to-day' spending on items such as social care and pensions, will rise. For instance, the recent NHS Five Year Forward View identified a £30bn a year gap in funding which needs filling by 2020–21.[7] These types of increases in demand are projected to rise far beyond 2020 by the Office for Budget Responsibility. Their central forecast has health spending rising from 6.4 per cent of GDP in 2018–19 to 8.5 per cent of GDP in 2063–64; state pension costs increasing from 5.5 per cent of GDP in 2018–19 to 7.9 per cent of GDP in 2063–64; and long-term social care costs rising from 1.2 per cent of GDP in 2018–19 to 2.3 per cent in 2063–64.[8] In this context, larger debt interest payments as a proportion of GDP mean future generations will find it harder to finance other forms of necessary expenditure.

The second is that, probably not imminently but at some point over the coming decades, another financial crisis on the scale of 1929 or 2008 is almost certain to occur. The UK, with a large financial sector relative to the size of our economy, is particularly vulnerable to systemic crises of this kind. To prepare for such an eventuality, in a previous Fabian Society report I proposed a 'rainy day fund' (a form of sovereign wealth fund to be used in a future banking crisis) and endorsed the Institute for Fiscal Studies (IFS) proposal of a 'sustainable commitments' rule – which targets the amount spent on debt interest and private finance initiative (PFI) payments instead of the debt to GDP ratio as a long term measure of intergenerational fairness.[9] Whichever fiscal rule is chosen, over the medium term it is better to have the fiscal headroom to respond, as we did in 2008, to any future crisis. This is particularly true if interest rates are close to the 'zero lower bound', reducing our ability to respond using conventional monetary policy such as lowering interest rates. Even in a crisis, the fiscal politics of moving from a debt to GDP ratio of 80 per cent to, say, 120 per cent are trickier than those of a move from 40 per cent to 80 per cent.

Finally, it is unclear whether paying for public spending through borrowing from the wealthy (who receive, traditionally at least, interest from lending to the state) has more progressive distributional outcomes, than taxing them.[10]

...but the Conservative approach unjustly targets those on low to middle incomes

To be clear this is not an argument in favour of George Osborne's permanent campaign to shrink the size of the state. The approach he has taken is wrong in its timing, and unjust in its effects on ordinary families.

There are many different political choices available in how to repair the UK's public finances. Decisions on the speed, timing over the business cycle, and the mix of tax and spending decisions dictate who bears the burden. The Conservative government has chosen to rely on cuts to social security and tax credit support to working families, coupled with large reductions in spending on certain public services.

First, during the 2015 election campaign, George Osborne repeated an oft-made promise to find £12bn of annual savings from the social security budget. While he may have suffered a temporary set-back following the furore surrounding the 2016 budget, many cuts have already been made. With most benefits for pensioners protected, this inevitably means that the axe has fallen on support to those of working age – particularly housing benefit and universal credit. So far this has meant changes to the design of tax credits and universal credit, which will affect the work incentives of low and middle income households, and a benefit cap which particularly affects those in receipt of housing benefit who live in expensive areas. A less noticeable change has been the freezing of the annual uprating of benefits. As inflation slowly erodes spending power, these amount to real terms cuts in the value of most benefits, with the exception of the basic state pension, which is uprated every year by the 'triple lock'.[11] One result of these measures is that the Institute for Fiscal Studies predicts that relative child poverty will increase dramatically by 7.8 percentage points: from 17.8 per cent in 2015–16 to 25.7 per cent in 2020–21.[12]

Second, government spending on public services is to be cut even further in this parliament, following five years of austerity under the coalition government. Certain budgets – the NHS, schools and overseas aid – are protected from real terms cuts, or have even seen their budgets increase. However, this makes the likely impact on unprotected areas of public services – job centres, the police, courts, business support, local government including social care, libraries, even more profound. In the 2016 Green Budget, the IFS calculated that the cumulative departmental cuts from 2010/11 to 2019/20 will be: Education (8.5 per cent), Business (40 per cent), Justice (45 per cent) and Home Office (25 per cent).[13] Here, the best analogy with the relentless effects of annual cuts on public services is to blood donation.[14] Most people can donate one or two pints of blood. However, if asked to donate more and more, then their vital functions quickly cease to work and the body starts to shut down.

In essence, working families and those dependent on social security and public services, are bearing the brunt of the burden for repairing public finances ravaged by a financial crisis they did not cause.

There is an alternative

Each choice reflects political priorities. The Conservatives have prioritised cutting inheritance tax, a tax paid by a vanishingly small number of wealthy households, corporation tax, and reducing the top rate of income tax on incomes over £150,000 per annum from 50p to 45p.

Alternatives, such as raising existing indirect taxes such as VAT, raise significant sums but hit those on low incomes hardest. Increases in income tax and national insurance contributions also have a detrimental effect on work incentives and jobs, particularly among those on low and middling wages.[15]

There is an alternative. Large public debts are accompanied by vast private wealth, disproportionately owned by the top 1 per cent. This reports sets out an alternative proposal for a new unique contribution – a one-off levy on the passive wealth held by the super-rich. The levy has an innovative valuation system which takes into account whether the taxpayer has previously used a tax haven (secrecy jurisdiction) or a domestic tax avoidance vehicle.

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2. WEALTH IN THE UK

Each year people receive an income, for example: earnings, benefits, rent, dividends and interest. Wealth represents the accumulation of that income. It is a measure of a stock not a flow. Think of a bath being filled: the amount of water in the bath is your wealth, the water flowing from the tap is your income.

Wealth in the UK is disproportionately owned by the top 1 per cent

The Office of National Statistics (ONS) estimate is that in 2012–14, the aggregate total wealth of all private households in Great Britain was £11.1tn.[16]

The ONS estimate that the top 10 per cent of households own 45 per cent of total aggregate wealth, while the bottom 50 per cent of households own 9 per cent. This data is derived from a survey and so comes with known shortcomings, such as lower response rates among the super-rich, and the failure to report wealth held offshore. In addition to hiding the real, higher level of UK households' wealth, these shortcomings also affect the reported distribution of that wealth. This makes it particularly problematic to use survey data for assessing the wealth of the top 1 per cent.

Other methods use inheritance tax data to infer the wealth of the very rich – although these also suffer from the weakness that inheritance tax is frequently avoided through estate planning. The result is that there are a wide range of estimates of wealth inequality. Estimates of the share of total wealth held by the top 1 per cent vary from 12.7 per cent (survey data) to 21 per cent (tax data).[17]

Finally, others use the *Sunday Times Rich List* data and combine it with the ONS data to make a rough comparison.[18] The top 1,000 in the 2016 UK rich list own £576bn wealth – a figure greater than the total wealth of the bottom 40 per cent of UK households (who own £496bn), is more than pension wealth of the bottom 60 per cent (£491bn), and exceeds the "bottom" 90 per cent of UK households' (non-pension) financial wealth (£546bn).[19]

Regardless of the source data, the general picture is clear: that the stock of wealth in the UK is large and distributed extremely unequally.[20]

The very rich own large amounts of financial wealth

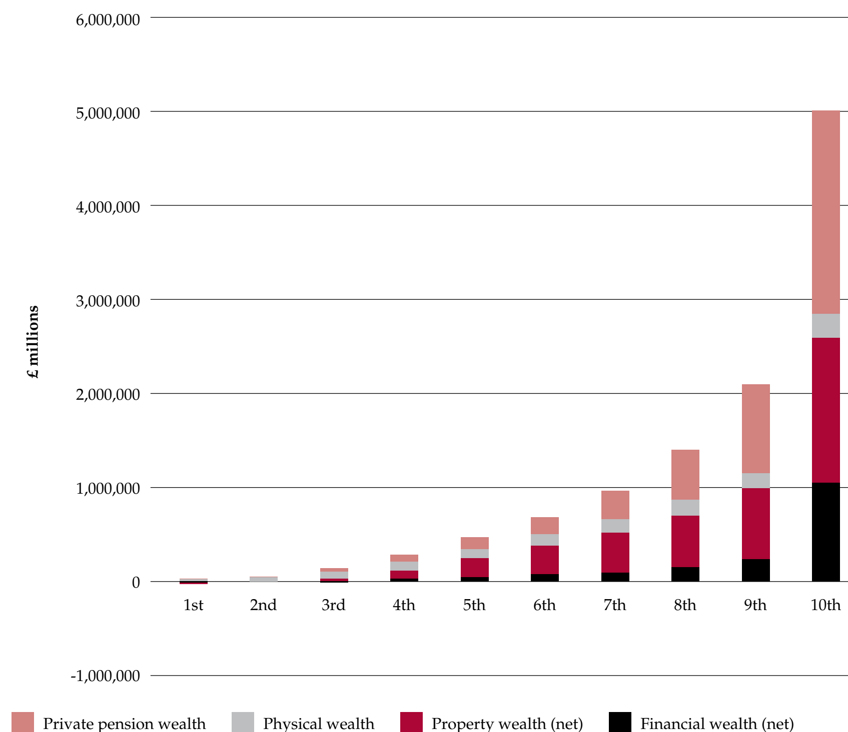
There are a wide variety of types of wealth. The ONS[21] estimate of £9.515tn aggregate total wealth is comprised of:

- Net property wealth (£3.9tn, 35 per cent of the total)
- Net financial wealth (£1.6tn, 14 per cent)
- Physical wealth (£1.1tn, 10 per cent)
- Private pension wealth (£4.4tn, 40 per cent)

Some in the bottom 10 per cent (under a threshold of £12,550) have no wealth apart from a few possessions, surviving day-to-day on their income. Others have negative net wealth, the result of personal indebtedness. As we start to move up the scale, more families hold some forms of property

FIGURE 1

Breakdown of aggregate total wealth, by deciles and components: GB, 2012/14[23]



wealth – principally their home, minus any mortgage – and some form of physical wealth – cars, jewellery, even personalised number plates. Others accumulate small amounts of financial wealth, usually small amounts of savings held in bank accounts and cash ISAs. The bottom 24 per cent of households own no private pension wealth.[22] But towards the top of the scale a much greater proportion of a household's wealth begins to be held as financial and private pension wealth.

The financial wealth of the very rich is different to that held by the rest of us

According to the ONS, the richest 10 per cent hold 43 per cent of their net wealth in pension rights, 31 per cent in property, 21 per cent as financial wealth and just 5 per cent in physical wealth.[24]

But what about the holdings of the top 1 per cent, or even the top 0.1 per cent?

Some of the wealth of the very rich is indeed held in their mansions, and perhaps status goods such as fine art and boats. This is the visible wealth we read about in the media. However, much is held in the form of financial assets – whether held in a private pension or not – that yield passive income and capital gains. Good household survey data about the assets held by the top 1 per cent doesn't exist. However, it is instructive to look at one prominent public example of an asset portfolio. In 2014 those managing the $36.4bn endowment fund for Harvard University invested 51 per cent of its assets in equity – shares of companies, including private equity (stakes in companies not traded on public stock exchanges), 11 per cent in natural resources such as timber and agricultural land, 12 per cent in property, 16 per cent in hedge funds who are able, among other roles, to 'short sell' stocks so that investors make money even when the stock market is falling, and 10 per cent in fixed income assets such as corporate and government bonds.[25] While the Harvard portfolio is unlike that of a typical wealthy household in that it does not hold any of its assets in cash, it does demonstrate the sheer range of income generating assets that can held by the very rich.

This is the key point: much of the wealth of the very rich produces further income, and their income accumulates to become wealth. This is *passive* income in that the very wealthy do not need to work to receive an income. The hard work is done by others – entrepreneurs and workers who mix the hard work and ideas needed to create wealth, but whose need for capital puts them in hock to others who, through the financial system, take stakes in their businesses or lend them money. Of course, entrepreneurial success often depends upon access to that capital. But these are not, in general, the entrepreneur-friendly tycoons of Dragon's Den. Their shares in businesses are not always long-term stakes accompanied by wise advice. Instead, those managing their share portfolios might hold stocks for seconds or minutes, frequently trading in order to exploit minute movements in 'momentum'. In time, passive income begets passive wealth. The super-rich do not even need to actively manage their passive wealth – their portfolio managers, private bankers and lawyers do that for them.

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These managers offer some or all of the following services:

- **Higher rates of return.** While you or I might receive a 1 or 2 per cent rate of interest on our savings account, the very rich have access to a wider variety of investments such as the services offered by hedge funds. These funds often have minimum thresholds for investment of millions or tens of millions of dollars. Through portfolio diversification, short selling, and complex financial instruments, rates of return can be higher than those available to other households. For the very rich the effects can be dramatic – and it is probable that the richer you are, the higher the rate of return you can achieve. Returning to the example of Harvard University, Piketty finds that the average real rate of return (after inflation and all administrative costs and fees) from 1980 to 2010 was 10.2 per cent for those with the largest endowments – Harvard, Yale and Princeton; 8.8 per cent for 60 colleges with endowments over $1bn; 7.8 per cent for those with endowments between $1bn and $500 million; 7.1 per cent for endowments from $500–100 million and 6.2 per cent for colleges starting with less than $100 million.[26]

- **Minimising taxes.** An integral part of the services offered by these managers are methods of reducing the amount of tax paid on both the wealth and any passive income. At its simplest, accountants will advise business owners on whether to take money as a salary or as a dividend, which attract different tax rates. Foundations and trusts can be established – these place distance between the legal owners and the beneficiaries of that wealth. This can be useful in, for example, minimising inheritance tax. Companies – sometimes under the ultimate control of just one person – can be established in tax havens where the rates of income and corporation tax are zero, and inter-company relationships can be established which, through transactions such as inter-company loans and abusive transfer pricing, can ensure that most profits are made where direct taxes are low or non-existent.

- **Secrecy.** Whereas in some countries such as Sweden, Norway and Finland, an individual's tax return is made public, and in the UK registries of the beneficial owners of companies are being established, many tax havens are also secrecy jurisdictions. They offer a chance to shield wealth from the prying eyes of disgruntled partners and, mostly, the tax authorities. Thus the real beneficiaries of a trust, foundation, company – and the assets owned or enjoyed by the real people behind those entities – can be kept secret.

In most cases wealth flows along the most 'tax efficient' paths in the same way that water flows down the steepest available gradient

None of the very rich have to avail themselves of the proffered chance to minimise taxes and hide their activities – but those who don't, such as the author of Harry Potter books, JK Rowling, are rare enough to be noteworthy in the media.[27] Compared with the majority of us however, whose earnings are subject to automatic taxation through PAYE, some of the wealth of the very rich has been under-taxed when compared with the original intent of democratically-elected governments of the countries in which the super-rich tend to live. In most cases wealth flows along the most 'tax efficient' paths in the same way that water flows down the steepest available gradient.

A significant amount of UK wealth is held offshore

As the Panama Papers revealed many of these tax efficient paths take geographically circuitous routes through a small number of secrecy jurisdictions such as the British Virgin Islands and Switzerland. How much of the UK's wealth might be found offshore?

By definition this is an impossible question to answer fully. However, despite the shortcomings in the data, some pioneering estimates of the global amount of offshore wealth have been made. These vary significantly according to the methodologies used, the breadth of forms of wealth measured, and the jurisdictions regarded as 'offshore'.[28] For example, the Boston Consulting Group, using estimates derived from interviews with wealth managers, estimate that some $11tn of financial wealth is held offshore – with $2.7tn held in Switzerland alone.[29]

An innovative methodology used by Professor Gabriel Zucman has used two techniques to estimate financial wealth. The first is analysis of data released by the Swiss central bank on assets held by foreigners in the Swiss banking system: $2.3tn (as at spring 2015).[30] Luxembourg has also recently released similar information, showing that foreign households have $370bn there. (Although this figure understates the true amount of offshore wealth in Luxembourg because it excludes some $350bn not directly held by households but through family offices and other intermediaries).[31] The second exploits cross border discrepancies in the statistics reported by share registries and banks:

> *"My own attempt relies on the anomalies in global investment statistics caused by offshore fortunes. Take the hypothetical case of Elizabeth, a UK resident who owns stock in Google through her Swiss account. In the United States, statisticians observe that a foreign investor owns US securities and record a liability. UK statisticians*

should record an asset held by a UK resident but they don't, because they have no way to observe Elizabeth's offshore holdings. Because Elizabeth's equity holdings are neither assets nor liabilities for Switzerland, over there nothing is recorded in the investment statistics. In the end, more liabilities than assets show up in global investment data. Strikingly, more than 20 per cent of the world's cross-border equities have no identifiable owner. By analysing these anomalies, I estimate that 8 per cent of the global financial wealth of households is held in tax havens, about $7.6tn at the end of 2013. … My method probably delivers a lower bound, in part because it only captures financial wealth and disregards real assets."[32]

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So how much of this wealth held offshore might be held by UK households? Unfortunately, Professor Zucman's technique doesn't allow for a precise estimate of wealth held by households in individual states. However, using the data from the Swiss National Bank Zucman estimates that about $140bn is held by UK households in Switzerland.[33] Recalling that Switzerland holds about one third of all offshore financial assets ($2.3tn of the total $7.6tn), it seems feasible that significant amounts might be held by UK households in other offshore jurisdictions. Further, these are just measures of financial wealth – physical assets and property (such as, say, a yacht held in the name of an offshore company but enjoyed by a particular family; or paintings held in a freeport) are not included in these estimates. It seems plausible to conclude that there are substantial amounts – at least in the order of magnitude of many tens of billions – of offshore wealth held or enjoyed by UK households.

Some of this wealth, and the passive income it earns, will have been declared to HMRC and other relevant tax authorities. Since 2005 any EU citizen who earns interest on their Swiss bank accounts has had a choice to declare their assets or to maintain secrecy but be charged a withholding tax of 35 per cent by the Swiss bank. Only 20 per cent of assets are voluntarily declared.[34] It is not known how much of the UK's offshore wealth is declared but it is fair to say that some of it will have been the product of past tax evasion and avoidance.

'ONSHORE' TAX AVOIDANCE

Of course, aggressive tax avoidance need not take place geographically offshore. For example, promoters of tax avoidance vehicles such as the "Working Wheels" scheme used by the DJ Chris Moyles set up highly contrived arrangements designed to create artificial losses which can be offset against other income in order to reduce one's tax bill.[35]

The promoters of such schemes are required to report their existence to HMRC under the disclosure of tax avoidance schemes (DOTAS) regime. HMRC then issue the scheme with a scheme reference number (SRN). The taxpayers who use such schemes must then declare the SRN on their tax return. Promoters (in practice, promoters are accountants, solicitors, banks and small firms called 'tax boutiques') are required to disclose the existence of a scheme if it fits certain 'hallmarks' such as confidentiality, premium fees, and schemes involving leasing and losses.

Some of these schemes are successfully challenged in the courts. Others succeed, at least until parliament then acts to close the loophole which has been exploited by the promoter. Through the establishment of the general anti avoidance rule, and the change in attitudes towards tax which has occurred since the financial crisis, these schemes have been declining in number. However, as with offshore wealth, some of today's onshore wealth which has been cycled through these schemes will have been under-taxed.

3. WEALTH TAXES

The main reason to tax wealth is to raise revenue. It is an attractive option because the sums are so vast, and its distribution so unequal. There are also other reasons to tax wealth:

- **Equality.** Wealth is far more unequally distributed than income. If you favour greater equality of outcome you need to influence the distribution of wealth, not only income. (As wealthy parents also do much to purchase a head start in life for their children, you should be interested in the distribution of wealth even if you only favour equality of opportunity, as that is intimately entwined with intergenerational equality of outcome.)

- **Power.** Wealth also brings with it a certain power. At its most innocuous this is the power to walk away from jobs. The power that wealth brings can also be desirable if it encourages or enables people to take entrepreneurial risks. Serial entrepreneur Stelios Haji-Ioannou, founder of EasyJet, was already rich through his inheritance of a Greek shipping fortune. However, of most concern is the power great wealth confers to shape the public realm. British citizens cannot be truly equal if, for example, a Russian banker resident in the UK who is married to a former Russian minister can purchase at auction the chance to play tennis with the prime minister and the mayor of London.[36] This, of course, is a crude example. More important is the 'agenda setting' power of the wealthy. This can be subtle, as in the campaign to reduce inheritance tax, or it can be obvious – such as when rich men, like the Barclay Brothers or Richard Desmond, purchase newspapers, and use them to campaign for pet causes such as withdrawal from the European Union. It is in this type of environment in which the rules of the game can be influenced to favour the wealthy elite.

We should aspire to lessen taxes on earned income wherever possible, particularly compared to passive income which arises to due to luck or inheritance

- **Merit and incentives.** Most people work hard for their income and deserve to keep as much of it as is consistent with the need to build a decent society for all our citizens. We should aspire to lessen taxes on earned income wherever possible, particularly compared to passive income which arises to due to luck or inheritance. Other things being equal, a tax on the stock of passive wealth is preferable to a tax on the income of the industrious and, furthermore, there should be fewer effects on work incentives.

The need to raise revenues, and a desire to curtail the power of the ultra-rich, has led to a long history of governments implementing wealth taxes. In a review of 'The Capital Levy in Theory and Practice', Barry Eichengreen notes that "the ancient Greeks used periodic capital taxes at rates varying from 1 to 4 per cent. It is said that these levies were phenomenally successful because property owners, out of vanity, overstated the value of their assets!"[37] This is not predicted to be the challenge any modern day wealth tax will face.

Annual wealth taxes can work well but have problems…

The history of modern annual wealth taxes is mixed. First and foremost, they exist and work well in several countries including Norway, some cantons in Switzerland, France, and Spain. Also the Netherlands has a capital income tax, described in more detail later in this report, which has some similarities to an annual tax on net wealth. The variety of problems that opponents speculate about – evasion, emigration, and the difficulties of valuing rarely traded assets – have been overcome in other economies. For example, the French *Impôt de solidarité sur la fortune* (ISF) raises around €4bn per annum.[38]

Nevertheless, many countries which had wealth taxes abandoned them in recent years: Austria abandoned its tax in 1994, Denmark and Germany in 1997, Finland, Iceland, Luxembourg, and Sweden in 2007 and Spain in 2008 (Spain and Iceland have since reintroduced their wealth taxes for the purposes of budget consolidation). Some of these moves are no doubt due to the ascent of centre-right political parties in those countries. However, other reasons are common to all annual wealth taxes. First, despite the extreme inequality of wealth, yields have always been low. For instance, those countries currently using wealth taxes raise only a relatively small amount of their revenue from them: France 0.6 per cent, Spain 0.36 per cent, Netherlands 1.59 per cent and Italy 1.45 per cent.[39] This is also true of those countries which abandoned their wealth taxes: revenue from the Swedish wealth tax typically varied from 0.5 to 1 per cent of total state tax revenue from the early 1970s until 2006.[40] Large personal allowances and exemptions of many types of assets combine with low annual rates to produce low

yields. Moreover, as the period of time that the tax has been in existence lengthens, political pressure tends to result in more assets being exempted and yields reducing still further.[41]

With ongoing, annual taxes there is always a temptation to engage in avoidance. Where certain assets (say, antiques, as in France) are exempt then one avoidance method could be to load up on debt to buy exempt assets; thus reducing assessed net wealth. Obviously, there is also a risk that an annual wealth tax would lead to greater offshore tax evasion and avoidance. This is one of the reasons why Piketty proposes an annual wealth tax only in the context of international co-ordination.[42]

An annual wealth tax in the UK, because of its ongoing nature, would in theory be more likely to encourage the emigration of the very wealthy. However, this effect is probably overstated as there are many reasons for moving to and from the UK. There is little data on the propensity of wealthy individuals to emigrate. When justifying the cut to the 50p tax rate in 2012, HMRC published 'The Exchequer effect of the 50 per cent additional rate of income tax'.[43] It cited a survey carried out for the Skandia life assurance company, in which "55.9 per cent of high net worth individuals would consider moving abroad under certain circumstances. High taxation was the most frequently cited reason for considering leaving the UK with 31 per cent of respondents." However, this was policy-based evidence making based upon a highly selective reading of the data. While 31 per cent cited high taxation as a motive to considering moving, 20 per cent cited a better standard of living in the destination country and 14.6 per cent cited the weather. Indeed, two of the top three possible emigration destinations are France and Spain – countries with wealth taxes and relatively high income tax rates.[44] The HMRC paper also cited evidence that 383 British citizens working in banking and financial services moved to Switzerland in 2010, an increase of 28 per cent on the previous year. It did not note that Swiss cantons too have an annual wealth taxes, with the rate charged by each canton varying from 0.2 per cent to 8 per cent.[45]

It is for these reasons, and those discussed below, that the Labour party before the 2015 election proposed a form of wealth taxation – on assets which couldn't physically move and whose value could easily be calculated – the so-called mansion tax. This was actually carefully designed, but was perceived by some to be unpopular. It was an annual levy on residential property worth over £2 million. The original £2 million threshold would rise in line with house price inflation at the upper end of the housing market rather than general consumer price inflation– so that owners of lower value homes wouldn't be dragged into the threshold by soaring house prices.[46] Labour also stated there would be protection for cash-poor but equity-rich owners – allowing them the option to pay

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the charge from their estate when they die. Despite these safeguards the tax was still regarded as a problem by about one in five voters in London who may have worried – in most cases wrongly – that their family home, which was a long way from being a 'mansion', might get caught in the net in future.[47]

… it is the macro-economic effects of annual wealth taxes that should attract most attention

Any annual wealth levy taxes not only inherited wealth but also wealth representing the individual's accumulated savings. Taxing the stock of accumulated savings is closely related to taxing the returns to savings (for instance, if you earn £2 interest per annum from savings of £100, then a 1 per cent annual wealth tax would raise £1, similar to a 50 per cent tax on savings interest.) Savings taxes affect both the total amount of savings in the economy and, probably more importantly, how those savings are allocated across different assets. This can directly affect the amount of capital invested and how efficiently it is invested.[48] Similar concerns within HM Treasury and the Labour party led to the abandonment of plans for an annual wealth tax in the 1974–79 government.[49] However, this effect on domestic savings might be lower in a globalised world where foreign investment can be attracted. Others argue that wealth taxes reduce risk taking, through lowering the net return. Conversely, others believe that a wealth tax might encourage investment in human capital and thereby positively affect economic growth.[50] Others state that wealth taxes might mean that the tax burden on labour income could be eased, which might be particularly important as technological change means that more returns might accrue to the owners of capital than those reliant on labour income.[51]

The effect of annual wealth taxes on growth have been tested empirically by Åsa Hansson, who examines the effect of wealth taxes on growth in a variety of European countries and finds that a 1 per cent increase in wealth tax does indeed reduce growth – but by a very small amount – between 0.02 and 0.04 percentage points.[52] Of course, other studies find that small increases in other taxes, including income tax[53], corporation tax[54], and VAT[55] all also adversely affect growth, typically by small amounts over time limited periods. This is because many models assume that long-term GDP growth is driven not by tax reform but by supply-side factors (technological progress, working age population growth, labour force participation rates and growth in the capital stock).

Any annual wealth levy taxes not only inherited wealth but also wealth representing the individual's accumulated savings

To summarise, while establishing an annual wealth tax is perfectly feasible, in practice they have not raised huge sums and the ongoing nature of annual taxes might lead to several undesirable distortionary effects such as increased avoidance, emigration, or a reduction in investment or entrepreneurial risk taking. While these have been generally overstated it is these long-term distortionary effects that a one-off wealth tax, as long as it is genuinely believed to be unique, largely avoids.

The most developed analyses of a one-off wealth tax can be found in Germany

Economists at the prestigious German Institute for Economic Research (DIW Berlin), latterly commissioned by the Friedrich-Ebert-Stiftung, have analysed the distributional and revenue raising potential for both one-off and annual wealth taxes in Germany.[56]

The DIW Berlin proposal analysed the tax rates needed to raise a target of €100bn through a one-off tax on very wealthy Germans:

> *"Since net wealth is strongly concentrated at the top of the distribution, a capital levy could raise substantial revenue even if relatively high personal allowances are granted, thus restricting the number of affected people to a very small share of all taxpayers. Assuming a personal allowance of €250,000, we estimate a tax base of €2,950bn, amounting to 118 per cent of GDP in 2010. A capital levy raising tax revenue of €100bn, or 4 per cent of GDP, would thus require a tax rate of 3.4 per cent. We also analyse alternative scenarios of a capital levy yielding the same tax revenue with a narrower tax base and a correspondingly higher tax rate. In the case of a personal allowance of €1 million, which would confine the capital levy to the richest 0.6 per cent of the population, the required tax rate would be 5.4 per cent."*

Much wealth in Germany is held in family-run businesses. Therefore the paper explores different options including providing exemptions and reliefs for such businesses, together with personal allowances including child allowances. The authors also allow for payment to be spread over 10 years. These measures reduce problems caused by liquidity constraints. They find that it is possible to raise €100bn through a tax design that includes a personal allowance of €1 million. In this scenario they estimate a tax base of €1,864bn (75 per cent of GDP) owned by 414,000 taxpayers – 0.6 per cent of the adult population. The extreme inequality of wealth means that the top 0.1 per cent wealthiest individuals account for 83 per cent of that tax base.

Finally, they include estimates of administration costs using data from inheritance and gift taxation. The higher the personal allowance, the lower the administration costs. A lower personal allowance

of €250,000 results in more taxpayers and increased administration costs of about 5 per cent of tax revenue. A higher personal allowance of €1 million reduces administration costs to less than 1 per cent of revenue.[57]

Similar proposals have been analysed by researchers from the German central bank, Deutsche Bundesbank.[58] The Bundesbank researchers who modelled a one-off wealth tax found that an annual wealth tax, in the long run, leads to lower growth and higher unemployment. However, they found that a one-off tax raises significant sums (€100bn) while causing few distortions which might hinder growth.[59]

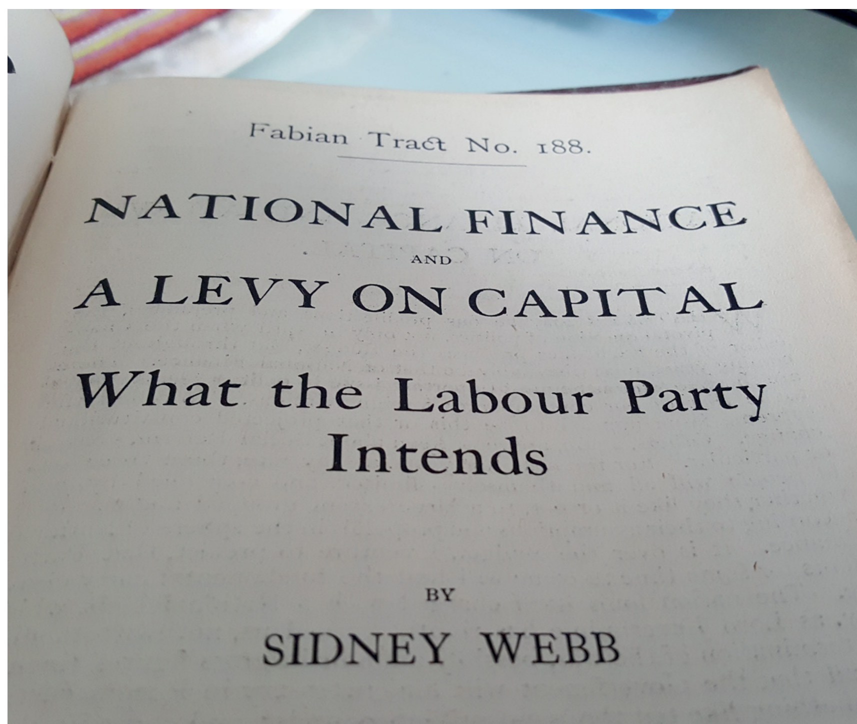
We should take the opportunity to learn from these German analyses and begin to seriously consider proposals for a unique contribution – a one-off levy on passive wealth in the UK.

Both the left and right have proposed one-off wealth taxes in the UK

Proposals for one-off wealth taxes, or capital levies, have a long pedigree in Britain and have originated from all sections of the political spectrum.[60] David Ricardo suggested a one-off capital levy to pay off public debt incurred during the Napoleonic wars.[61] In the period following the first world war public debt had again risen to problematic levels: interest payments as a share of budgetary receipts rose from less than 10 per cent in 1913–14 to 22 per cent in 1919–20.[62] Proposals for a capital levy were made by Sidney Webb, in a 1919 pamphlet for the Fabian Society which proposed a one-off levy on capital.[63] By 1920 a levy imposed solely on the additional wealth accumulated during the war had become part of the Labour party's official policy platform. The ruling Liberal Conservative government appointed a Parliamentary Select Committee on Increase of Wealth (War) which in 1920 submitted a plan for a levy, to be applied to the 1914–19 increment in property values. This plan was supported by the economist Arthur Cecil Pigou, in his book *A Capital Levy and a Levy on War Wealth* in 1920.[64]

As public debt soared again during the second world war interest in one-off levies increased. There was a one-off levy implemented in post-war Germany: the so-called *Lastenausgleich*. J.M. Keynes published his 1940 pamphlet, entitled *How to Pay for the War*, and included an idea for a capital levy suggested by an earlier reviewer – Friedrich vion Hayek. However, each made the proposal for different reasons. Keynes saw the one-off levy as necessary to retain the support of the Labour movement for his plan for compulsory savings, to be released after the war ended in order to counter the predicted slump. The levy would pay for the payments to all the workers who had deferred their income. Hayek meanwhile proposed the levy be used for the purposes of popular capitalism – to convert the workers' deferred pay into equity stakes in the 'industrial capital of the country' – through a trust fund or 'giant holding company'.[65]

In power, Labour has introduced two ad hoc levies, on capital *income* but structured so as to be not too dissimilar to a wealth tax. The first was Stafford Cripps' 1948 'special contribution', and the second was the 'special charge' introduced by Roy Jenkins in 1968. The special contribution was an ad hoc levy on investment income over £250, so long as the individual had a total income of over £2,000; while the special charge was a one-off retrospective tax on investment income in one year (1967–68). Roy Jenkins had always favoured some sort of one-off wealth tax – his maiden speech in parliament had been in favour of the 1948 special contribution and in 1951 he wrote a Tribune pamphlet arguing for a capital levy. When chancellor, he structured the special charge so that any investment income below a £3,000 threshold was exempt, but subsequent tranches were taxed at a steeply progressive scale: 10 per cent between £3–4,000, 15 per cent between £4–5,000, 30 per cent between £5–8,000 and at 45 per cent above £8,000.[66]



4. PROPOSAL FOR A ONE-OFF LEVY ON PASSIVE WEALTH

The rest of this chapter sets out a proposal for a one-off levy on passive (net) wealth. The levy is designed to take into account previous high risk behaviour, such as use of tax havens. The proposal borrows the language of the 1948 special contribution, terming the levy a 'unique contribution' – to emphasise that it is indeed a one-off tax.

The basic structure of the tax is set out below – which uses terms accessible to those familiar with British tax law. Where appropriate, grey text in italics gives additional commentary which explains key features of the unique contribution in simpler language, or using examples.

Description of structure of one-off levy

Introduction

1. The one-off tax on unearned wealth will be charged on all **long-term residents** of the UK. The amount of the charge will be a percentage (the **lower rate**) of each long-term resident's **chargeable wealth**, to the extent that the long-term resident's **chargeable wealth** exceeds a specified threshold (the **personal chargeable wealth** allowance). A **higher rat**e will be charged to the extent that the long-term resident's **chargeable wealth** exceeds a **higher rate chargeable wealth threshold**.

2. The 'personal chargeable wealth allowance' will be £[X], the 'lower rate' will be [A]%, the 'higher rate chargeable wealth threshold' will be £[Y], and the higher rate will be [B]%.

So, for example, the personal chargeable wealth allowance could be £10 million. The higher rate chargeable wealth threshold could be £20 million. The lower rate of, say, 1 per cent would therefore be charged on chargeable wealth between £10 million and £20 million, and the higher rate of, say, 2 per cent would be applied to chargeable wealth above the £20 million threshold.

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3. A key feature of the tax is certain exclusions which are referable to trading or employment activity. It is by reason of those exclusions that the tax is described as a tax on 'passive' wealth.

This disregard of employment and trading income is applicable whichever computation method is used. See paragraphs 7c) and 14a).

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4. Another key feature of the tax is that long-term residents who are not **high-risk taxpayers** will be permitted to elect to be taxed by reference to a streamlined computation mechanism which derives a **deemed chargeable wealth** figure from easily collected information. High-risk taxpayers are (broadly speaking) those who use or have used either aggressive tax avoidance or offshore financial services. In the case of long-term residents who are high-risk taxpayers, the chargeable wealth figure derives from a thorough assessment of the taxpayer's actual holdings of assets.

For the majority of taxpayers, who have not used offshore financial services or tax avoidance vehicles valuation of wealth will not be difficult: their financial wealth will be calculated by HMRC on their behalf (see paragraph 7b)) and they can value their main property. If they wish, however, all taxpayers can choose the full valuation exercise which high-risk taxpayers must undergo.

Meaning of "long-term resident"

5. A long-term resident is anyone resident in the UK on the date by reference to which the tax is charged (the **charging date**) who
   a) has been resident in the UK during at least four of the seven tax years preceding the year in which the charging date falls or,
   b) is unable to demonstrate that their residence in the UK is temporary by reference to (i) a projected departure date within four years of their date of arrival and (ii) the absence of long-term employment, business, property or family interests.

6. Long-term residents who are not **high-risk taxpayers** pay the tax in relation to their **deemed chargeable wealth**.

This is a new category which brings in potential taxpayers much quicker than the non-dom rules.

Meaning of "deemed chargeable wealth"

7. Deemed chargeable wealth comprises **untenanted property, deemed investment wealth, cash-valued assets** and **private pension fund wealth, minus deductible liabilities.**

A key feature of this levy is the exclusion of most wealth that does not generate a declarable income. This is due to the selection of declarable unearned income as a method of easily imputing financial wealth. So, for example, art, jewellery and personalised number plates would be excluded from both the calculation of chargeable wealth and deemed chargeable wealth.

a) 'Untenanted property' means real property, and high-value chattels for which a leasing market exists eg boats, insofar as such real property or chattels are not continuously let at an arm's length rent. A person's deemed chargeable wealth includes the market value (as at the charging date) of all such property where (i) the property belongs beneficially to that person (whether or not jointly with any other person or persons), or (ii) that person has continuous use of it, where such use arises by virtue of any property right held by that person or by any other person or persons, except to the extent a rent is paid for such use. Where multiple long-term UK residents have the value of such property falling to be included in their chargeable wealth by virtue of the foregoing, the value will be deemed to be included in the chargeable wealth of the person whose chargeable wealth is greatest, and excluded from the chargeable wealth of any other person.

A typical 'untenanted real property' would be the main family residence.

Property held in a trust would be covered by paragraph 7a)ii.

b) 'Deemed investment wealth' means a deemed amount of capital wealth derived from treating the highest amount of annual **unearned income** over the course of the four years of the taxpayer's UK residence prior to the charging date (inflation-indexed to the charging date) as representing the product of an **assumed average annual rate of return** of [Z]% on investment assets across all classes.

Examples of unearned income that would be included within the deemed investment wealth calculation include:

- *Rents from a buy-to-let empire;*
- *Dividends;*
- *Income from a UK based trust fund.*

Say the assumed average annual rate of return was 5 per cent. Unearned income of, say, £1m per annum would be divided by 5 per cent to infer a capital sum of £20m.

c) 'Unearned income' means all taxable income, or income which would be taxable but for relief in respect of foreign tax, with the following subtractions:
   i) income from employment,
   ii) trading income,
   iii) income from real property which is not continuously let at an arm's length rent, and
   iv) income from cash-valued assets

This income should have been declared to the HMRC and is therefore easily obtainable.

The effect of disregarding trading and employment income is to lessen the inferred capital sum.

Trading income is only earned income if the taxpayer his- or herself is trading, dividends are unearned income.

Real property which is not continuously let at an arm's length rent might be, for example, a holiday home which is sometimes let as holiday accommodation. This would be taken into account under paragraph 7a).

d) 'Cash-valued assets' means sterling cash, amounts in sterling-denominated bank accounts, and holdings of UK government debt. It also includes any asset subject to a cash valuation rather than inclusion within deemed investment wealth upon a claim to have it so treated by the taxpayer.

It is available to a taxpayer to make a claim for an asset to be valued rather than having its value estimated on the basis of the income it generates, to avoid a harsh outcome in circumstances where, for example, an asset yielded disproportionately high income in a single year.

e) 'Private pension fund wealth' means the market value (as at the charging date) of any assets held for the purposes of the taxpayer's rights under any registered pension scheme or qualifying overseas pension scheme.

This figure can be obtained easily from pension schemes.

f) 'Deductible liabilities' means any debt owed by the taxpayer on the charging date, or any other liability where the net present value of the liability as at the charging date can reasonably be computed, to the extent such debt or other liability was incurred on arm's length terms, and excluding debt where the interest is deductible against income used for the purposes of a deemed investment wealth computation. Deductible liabilities which are jointly owed shall be subject to apportionment.

The levy is charged on net *chargeable wealth so, for example, a mansion worth £20m with a mortgage of £5m remaining has that £5m debt deducted from the total chargeable wealth.*

8. It is by means of the foregoing method that taxpayers who are not **high-risk taxpayers** may elect to compute their chargeable wealth. For most taxpayers in this category, the only valuation exercise will be the valuation of any untenanted real property (ie generally-speaking, residential property for family use). Procuring such valuations should not be burdensome.

In the unlikely event that a taxpayer has recently liquidated and spent most of their financial wealth, then they can voluntarily choose to be assessed to have a full valuation of their wealth, using the same methods that high risk taxpayers must undergo, see below.

Meaning of 'high-risk taxpayer'

9. 'High-risk taxpayer' means a taxpayer who has during year in which the charging date falls or during the seven tax years preceding that year:
   a) made use of a scheme disclosable under the Disclosure of Tax Avoidance Schemes (DOTAS) regime, or
   b) entered into any arrangement designed to reduce or defer tax or otherwise obtain a tax advantage, where such arrangement (i) relied on a professional opinion as to its efficacy, and (ii) that opinion addressed or ought to have addressed the risk of the arrangement being found to fail on the basis of anti-avoidance legislation or jurisprudence (ie jurisprudence requiring that a realistic view of the transaction or purposive interpretation of the relevant legislation be adopted, or jurisprudence negativing the fiscal efficacy of circular transactions or transactions containing inserted steps with no commercial purpose) irrespective of whether such arrangement was subsequently found to succeed, or was subsequently found to fail on some other basis, or who has who has during year in which the charging date falls or during the twenty tax years preceding that year:
   c) transferred assets into a bank account in any secrecy jurisdiction,
   d) transferred assets otherwise than on arm's length terms to any company, trust, foundation or other asset-holding structure where any of the entities or arrangements in that structure is constituted by the laws of any secrecy jurisdiction or has a bank account in any secrecy jurisdiction, or procured such a transfer into such bank account or to such entity or arrangement (which shall include such transfer being made in connection with an employment relationship).

Under the DOTAS regime promoters are obliged to register schemes if they have certain 'hallmarks' such as confidentiality and schemes involving leasing and losses.

Paragraph 9b) is intended to capture "bespoke" tax avoidance in addition to the 'off the shelf' schemes caught through the DOTAS regime.

How the UK and other states may define secrecy jurisdictions is discussed elsewhere in this paper.

In paragraph 9d) for an offshore trust, for example, it is the settlor of the trust who is the high-risk taxpayer, rather than, necessarily, the beneficiary. If beneficiaries (who are not also high risk) are using property held in an offshore trust, or receiving income from it, that will be included in the calculation of their deemed chargeable wealth.

10. 'High-risk taxpayer' also includes any taxpayer who pays tax on the remittance basis.

This includes the small number of very wealthy non doms who elect to pay the annual flat rate fee known as the Remittance Basis Charge. For example, in 2012 nearly 5,000 of the 123,000 non doms chose to pay the Remittance Basis Charge rather than pay UK tax on their global income and gains.[67]

11. Some of the foregoing indicators require taxpayers to assess themselves to be 'high risk' since the relevant information will not in those instances be available to HMRC, and some will in practice require the taxpayer's advisers (or the taxpayer's employer's advisers) to notify taxpayers that they are 'high risk'. Provision will therefore have to be made to (i) penalise advisers who do not notify relevant taxpayers that they are 'high risk', and (ii) penalise high-risk taxpayers who do not notify their status to HMRC.

12. The chargeable wealth of high-risk taxpayers (and other taxpayers who do not elect to be taxed in accordance with their deemed chargeable wealth) is computed in accordance with the following.

The onus is on the taxpayer or adviser to declare their previous use of offshore finance. The increased use of automatic information exchange between tax jurisdictions (and occasional leaks of data from tax havens such as the Panama Papers) make continued obfuscation an unwise strategy.

Meaning of 'chargeable wealth'

13. Chargeable wealth is the aggregate market value (as at the charging date) of **relevant assets** which are **attributable** to the taxpayer, less deductible liabilities as defined above.

Here, rather than 'deeming' chargeable wealth from unearned income the market value of the taxpayer's net chargeable wealth is calculated through a valuation exercise.

14. 'Relevant assets' means any asset of whatsoever kind which is capable of generating income (including real property, and high-value chattels for which a leasing market exists eg boats whether or not such chattels are in fact being leased), except:
    a) contracts of employment and assets held for the purposes of a trade, and
    b) assets the value of which or income from which has already formed part of a deemed chargeable wealth computation.

Assets which are not capable of generating passive income, such vintage furniture or fine art, are excluded. The rationale is to keep the base of deemed chargeable wealth and chargeable wealth equivalent. High risk taxpayers are to be excluded from a simpler form of assessment not requiring substantial disclosure, rather than assessed on a wider tax base.

15. An asset is 'attributable' to a person if it belongs beneficially to that person (whether or not jointly with any other person or persons). An asset is also attributable to a person if:
    a) it is held for the purposes of that person's rights under any registered pension scheme or qualifying overseas pension scheme;
    b) that person has continuous use of it, where such use arises by virtue of any property right held by that person or by any other person or persons;
    c) it is held in any company, trust, foundation or other asset-holding structure any kind to which the person has contributed assets, where there exists any expectation that the person or any person connected to that person might receive any benefit from such structure, to the extent such asset is apportionable to the person by reference to respective contributions of assets to such structure by those who have contributed to it; or
    d) the person has received or has any expectation of receiving income from, the benefit of or continuous use of that asset in the future, where it is held in a company, trust, foundation or other asset-holding structure of any kind.

16. Further, where a person has received payments or other benefits from a company, trust, foundation or other asset-holding structure of any kind (except to the extent referable to employment by an entity or person in such structure or participation in such structure qua asset-holder), and no asset is attributable to the person to which such payment or benefit is referable, a **deemed asset** will be attributed to that person, the value of which is to be computed by treating the greatest annual amount of such payments or the greatest annual value of such benefit (inflation-indexed to the charging date) over the course of the four years prior to the charging date as representing the **assumed average annual rate of return** on the deemed asset.

Paragraph 15c) is largely focused on attributing assets to the settlor, and dealing with the possibility that a single settlement could have had multiple settlors – in those circumstances the assets in the settlement need to be apportioned.

17. Where an asset is attributable to more than one high-risk taxpayer, the value of that asset will be deemed to be included in the chargeable wealth of the high-risk taxpayer whose chargeable wealth is greatest, and not included in the chargeable wealth of any other high-risk taxpayer. Further, relief will be given to the extent that any asset included in the chargeable wealth of a high-risk taxpayer gives rise to taxable deemed chargeable wealth on the part of a low-risk taxpayer.

This paragraph is intended to avoid double counting of assets.

18. As with the initial identification of high-risk taxpayers, the assessment of their chargeable wealth will require their advisers to take a pro-active role, and serious penalties should apply in cases of non-disclosure by either advisors or taxpayers themselves.

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5. DISCUSSION

The following discussion seeks to address some of the questions that this proposal may provoke.

Should the levy be targeted at the top 1 per cent or 0.1 per cent?

One of the criticisms of the 'mansion tax' was that the £2 million threshold is so low that it captures properties that are not 'mansions' at all, but the normal dwellings of the middle class who happen to live in affluent areas. Should a one-off wealth tax be targeted at the top 10 per cent or top 1 per cent, or even higher? What do these percentages mean in practice?

To be in the top 10 per cent of wealthy households in the UK one must have assets worth about £1 million.[68] Therefore, a focus on the top 10 per cent would encounter some of the same political problems as the mansion tax and is therefore not recommended.

A household must have assets of just under £2.9 million to be in the top 1 per cent. However, the German wealth tax proposal analysed by DIW Berlin found that the extreme inequality of wealth meant that the top 0.1 per cent wealthiest individuals accounted for 83 per cent of the German tax base. Not much is known about inequality between the UK's top 1 per cent and the top 0.1 per cent (and therefore nor is the true threshold for being in the top 0.1 per cent known) but analysis which combines survey data with 'rich list' data implies that inequality of wealth at this very high level is also skewed in the UK.[69]

The evidence from Germany suggests that it might be possible to raise significant sums even with a high personal allowance of, say, £10 million. Setting of the threshold is, in the final analysis, a political judgment. It seems unlikely that many British swing voters would fear that they would be personally affected by a one-off tax on passive wealth of over £10 million. They may, of course, fear that the Labour party has set itself against 'aspiration', though again the fact the unique contribution is a one-off should be reassuring.

How much might the levy raise?

Her Majesty's Revenue and Customs (HMRC) hold some data which might be useful in making this calculation. For example, the UK Transfer of Assets Abroad rules are designed to require declarations and consequent payment of tax due in situations where a UK resident transfers assets to an offshore location in order to reduce their UK income tax liability. Between 9,000 to 13,000 individuals are affected by the rules each year – around 2,000 of whom are additional rate taxpayers (and around 1,400 of whom earn over £250,000 gross per annum).[70] Also HMRC should be able to make an estimate of the amount of deemed investment wealth, by examining data on declared capital income, and Land Registry data could be used to value UK property wealth.

However, the total tax base is difficult to estimate. As mentioned earlier, good quality household survey data for the very rich is absent, and tax data is largely derived from inheritance tax data, a tax which is frequently avoided by the wealthy. Considered alongside the large sums held offshore the wealth of the very rich is largely terra incognita for the UK authorities. The levying of the tax will itself be an exercise in mapmaking.

In short, therefore, we do not know, although we suspect the sums could be considerable. However, it is not uncommon for the amount of tax revenue raised or lost to be uncertain in any particular budget measure, or for estimates to change over time. For example, the annual tax on enveloped dwellings (ATED), a tax measure designed to counter the avoidance of stamp duty on sales of property held by offshore companies, raised five times the initial estimate made by HRMC.[71] Less happily, initial HMRC estimates of £5.1bn revenue (over 5 years) from the 2011 UK-Swiss tax deal were vastly over-optimistic.[72] We should not let uncertainty over the precise amounts which might by raised prevent action when we know the results could be significant.

Why would people who have been involved in dodging their taxes reveal their hidden wealth?

Some dedicated tax evaders – who have ignored many previous favourable amnesty deals – will no doubt remain on the wrong side of the law and their offshore wealth will remain out of sight. (However, their visible wealth can still be taxed, of course.)

There is an incentive to declare their past tax avoidance. Individual taxpayers or their advisers must assess themselves or their clients to be 'high risk' – for example that they have transferred assets to a bank account in a secrecy jurisdiction. Choosing not to identify themselves as high risk could carry serious penalties, perhaps including custodial sentences in egregious cases.

Moreover, the noose around the neck of tax evaders has tightened somewhat over recent years. There have been a succession of announcements between the UK and various other jurisdictions, including tax havens, which allow for automatic information exchange between HMRC and other authorities. Before these agreements, exchange of information, where agreements existed, was on an 'on request' basis: information is only passed over after a clear request is made, specifying the taxpayer concerned and various other bits of

information about him or her. In essence, you have to already know what you are looking for before you ask for it.[73]

Now, the devil is in the detail: some of the multi-lateral announcements of automatic information exchange will allow for the exchange of both banking information and beneficial ownership details – ie who really owns, controls or enjoys the fruits of a particular company, trust or asset. Some deals might be less useful. But such arrangements are becoming more common, and more jurisdictions, including certain tax havens, are participating. Further, as a succession of leaks ('Offshore leaks', 'Swiss leaks', and the 'Panama Papers') have shown, total secrecy can no longer be assured.

Someone who wishes not to declare themselves high risk is in effect saying that they are 100 per cent confident that their past tax-avoiding over the previous 20 years left no trace that can be discovered by future information exchange or a leak over the next 20 years. Those who might have a modicum of doubt might consider coming clean and registering themselves as 'high risk'.

What about the little old lady who is asset rich, income poor?

A criticism of the mansion tax plans was that the proverbial little old lady who may live in property which is valued at over the £2 million threshold may not have sufficient income to pay the annual charge. This criticism is overblown. ONS data reveal that only 1 per cent of UK households in the bottom 40 per cent of the income distribution have property wealth worth over £500,000.[74] Moreover there were plans to allow the mansion tax to be paid through a charge on your property, to be repaid once sold or on the death of the occupant, thereby allowing the elderly to remain in their own homes.

Similarly, if there are particular cases of individuals who have over, say, £10 million in assets – for example untenanted real property such as a main residence – but who also have low levels of income, then provision could be made to allow the tax to be paid over three years, or to allow a charge to be attached to a property. However, this should be considered carefully as, with a high personal allowance of £10 million, these cases will be vanishingly rare.

> There are other principles in taxation – such as progressivity – which should be given greater weight than that of avoiding double taxation

Would a wealth tax be taxing the same income twice?

Double taxation is a common objection to a wealth tax: some of the wealth that would be subject to the tax would indeed have been accumulated from post-tax income.[75] However, some would not be (for example, certain assets – in particular someone's main home – can gain in value and the capital gain remains untaxed). Former member of the Bank of England Monetary Policy Committee, economist Martin Weale notes that much of the increase in wealth over the last decades "has its origins in asset revaluations rather than resulting from past saving. In that sense taxes on wealth and on inheritance are not double taxation."[76] Finally, some of the wealth taxed through the unique contribution will have been 'undertaxed', particularly if the taxpayer has used offshore financial services or domestic tax avoidance vehicles.

The 'problem' of double taxation is endemic in our tax system and the distributional effect is proportionately greater for those on low and middle incomes. Most money raised through indirect taxes (such as VAT and tobacco duties) is also from individual's post-tax income – and these are regressive taxes on which the poor pay proportionately more of their income. There are other principles in taxation – such as progressivity – which should be given greater weight than that of avoiding double taxation.

How would HMRC calculate an assumed average rate of return?

One special feature of the unique contribution is the use of a streamlined wealth calculation method for low-risk taxpayers. This involves assuming declared unearned income to be the product of investment wealth, using a fixed assumed average rate of return. Say, for example, the assumed rate of return was 5 per cent. Therefore unearned income of say £1 million per annum from rents from a buy-to-let empire or dividends would be used to infer a capital sum of £20 million.

This use of an assumed average rate of return is not dissimilar to a special provision used in the Netherlands.[77] The Dutch Box 3 system taxes income from savings and investments in a special way. Actual rates of return from financial wealth – such as interest and dividends – are not relevant. Instead taxpayers' net wealth held in the form of savings and investment is calculated. The return on this wealth is assumed to be 4 per cent. This 4 per cent notional income is taxed at a rate of 30 per cent. Thus, effectively, 1.2 per cent of the taxpayer's net wealth is taxed annually.[78]

But what should the rate of return be? The super-rich can almost certainly earn higher rates of return. We have already noted how the average real rate of return (after inflation and all administrative costs and fees) from 1980 to 2010 varied from 10.2 per cent to 6.2 per cent for US college endowment funds, depending upon the size of their capital sum. This principle is also recognised in proposed reforms to the Dutch Box 3 system – in which the fixed yield will be reduced to 2.9 per cent for amounts up to € 100,000 but increased to 4.7 per cent for amounts between €100,000 and €1,000,000 and 5.5 per cent for sums over € 1,000,000.[79] This would be a matter for detailed analysis by HM Treasury. However, it seems likely

that UK assumed rates of return for those with net wealth over £10 million, should be 5 per cent or higher.

Is valuation of the assets of high risk taxpayers too difficult or intrusive?

The process is necessarily intrusive, which is why it is restricted only to high-risk taxpayers. However, the nature and level of intrusion will not be in a different category to that experienced by lower income families in receipt of social security benefits whose family, health, income, wealth and work situations are investigated regularly.

It is sometimes said that a wealth tax is too difficult to implement because of the difficulty of valuing rarely traded assets.[80] The unique contribution proposal outlined in this report however, only focuses on assets capable of producing an income, therefore exempting family heirlooms such as jewellery and art, for instance. In the UK professional valuers are well used to valuing estates, including assets held overseas, for the purpose of assessing liability for inheritance tax.

We also need not worry about taxpayers quickly moving their assets into exempt forms of wealth (such as art). The government can announce the measure under a constitutional convention known as the 'Rees rule' which governs retrospective application of new tax rules. The convention is that the government will announce, usually through a parliamentary answer or statement, the specific tax avoidance loophole which is intended to be closed. The relevant legislation, which might not be introduced until the next finance bill, is then backdated to begin on the date of that announcement.[81] In this case the measure could be announced on the day of the budget, or very shortly before. The date of the announcement can be used as the date of valuation of (taxable) relevant assets.

Aren't retroactive laws unlawful?

The unique contribution is not a retroactive tax – it is a tax on current, present-day wealth. Nevertheless, there are elements of retrospectivity in this proposal: in particular the use of past behaviour (use of tax havens and DOTAS registered tax avoidance schemes) to ascertain liability for the unique contribution.

Retroactive legislation is rightly frowned upon: however, it is not necessarily unlawful. While it is true that Article 7 of the European Convention on Human Rights (ECHR) forbids retroactive criminal law, taxes are not part of criminal law.[82] Indeed, there have been several examples of taxes with retrospective effect. In 1981 the Conservative government levied a one-off windfall tax of 2.5 per cent on banks' non-interest bearing current account deposits, raising £400 million. In 1991 the Conservative government introduced (with retrospective effect) regulations affecting the tax on interest paid by building societies. The Labour government's retroactive windfall tax on the utility companies in 1997 and 1998, raised £5.2bn.

In the realm of personal taxation retrospective legislation is used reasonably frequently as an anti-avoidance measure. This has been the case with partnerships dealing in commodity futures in 1978, bonuses in 2004, double taxation treaty abuse in 2008 and stamp duty land tax in 2012.

Court cases have tested these laws, where claimants state that Article 1 of Protocol 1 to the ECHR has been infringed. It is worth quoting in full the summary of case law given by a standard law textbook, and repeated by the House of Commons library.[83]

> *"Article 1 of Protocol No 1 to the European Convention guarantees, in substance, the right to property and, in effect, comprises three elements. The first contains the general principle of peaceful enjoyment of property; the second deals with deprivation of property and subjects that to certain conditions; the third recognises that contracting states are entitled to pass laws that they deem necessary to secure the payment of taxes. This was explained by the European Court of Human Rights in National and Provincial Building Society and Others v UK (1997) in the following terms:*
>
>> *"According to the Court's well-established case-law … an interference, including one resulting from a measure to secure the payment of taxes, must strike a "fair balance" between the demands of the general interest of the community and the requirements of the protection of the individual's fundamental rights. The concern to achieve this balance is reflected in the structure of Article 1 as a whole, including the second paragraph: there must therefore be a reasonable relationship of proportionality between the means employed and the aims pursued. Furthermore, in determining whether this requirement has been met, it is recognised that a Contracting State, not least when framing and implementing policies in the area of taxation, enjoys a wide margin of appreciation and the Court will respect the legislature's assessment in such matters unless it is devoid of reasonable foundation."*
>
> *"In the area of taxation, retrospective legislation is used most often as an anti-avoidance measure by plugging a loophole. Such legislation does not automatically infringe the European Convention, but it is certainly capable of challenge under Article 1 of Protocol No 1 since it undermines the rule of law and legal certainty. A claimant would have to show that the legislation in question was not objectively justifiable and was disproportionate."*[84]

If the government pursued the idea of a one-off levy, the detailed proposal would be expected to be robust to any challenge.

Will generating a list of secrecy jurisdictions be problematic?

Following the Panama Papers the UK has joined others in calling for an interna-

tional blacklist of tax havens.[85] However, governments are usually reluctant, for reasons of bilateral relations, to label other states as a 'tax haven'. An early attempt by the Organisation for Economic Cooperation and Development (OECD) listed several countries but intense pressure from those states, and revised, more lenient, listing rules, mean that currently no countries are listed as uncooperative tax havens by the OECD's Committee on Fiscal Affairs.

However, it is possible to take unilateral action. HM Treasury does in fact maintain a list of secrecy jurisdictions based upon their willingness and readiness to share data with HMRC, in order to set differential penalties for non-declaration of offshore income. Schedule 10 of the 2010 Finance Act empowers HM Treasury to classify territories in order to give higher financial penalties for tax evasion or avoidance where the scheme involves a secrecy jurisdiction:

> *"In considering how to classify a territory for the purposes of this paragraph, the Treasury must have regard to:*
>
> *a) the existence of any arrangements between the UK and that territory for the exchange of information for tax enforcement purposes,*
>
> *b) the quality of any such arrangements (in particular, whether they provide for information to be exchanged automatically or on request), and*
>
> *c) the benefit that the UK would be likely to obtain from receiving information from that territory, were such arrangements to exist with it."*

The current 'category three' territories include known secrecy jurisdictions such as Panama. However, the category three list doesn't include tax havens such as the Cayman Islands. The principles underpinning this list could therefore be amended to reflect a wider understanding of the common characteristics of secrecy jurisdictions including: the current and historical pattern of the bilateral exchange of information between the jurisdiction and the UK (whether automatic or only on request), the present and historical existence of registries which reveal true beneficial owners of entities (either to the public or to law enforcement authorities), and present (and historical) zero or low tax rates for income, capital gains and/or corporation tax. The emphasis on past characteristics is important. If a taxpayer settled funds in a secrecy jurisdiction which has recently cleaned up its act, the taxpayer should still be regarded as 'high risk'.

The emphasis on past characteristics is important. If a taxpayer settled funds in a secrecy jurisdiction which has recently cleaned up its act, the taxpayer should still be regarded as 'high risk'

The construction of such a list would also need to be robust to withstand challenges that may occur from the inclusion of secrecy jurisdictions which are in the European Union, such as Luxembourg. EU states do sometimes identify low tax jurisdictions, for example to construct controlled foreign company (CFC) rules. These rules, in a sense, define 'tax havens' in a way which the EU member state deems compatible with European law. CFC rules seek to discourage the shifting of income by a company to a (controlled) subsidiary in a low tax jurisdiction by taxing the parent company's income as if it included a proportionate share of the subsidiary's income (at the domestic, higher) tax rate. The low tax jurisdiction is either listed in a blacklist (or is absent from a 'whitelist') maintained by the EU state[86] or is defined by reference to a specific (lower) percentage[87] of domestic corporate tax – or a combination of the two.[88] For instance, Sweden effectively subjects the 'tax haven' subsidiary's profit to Swedish corporation tax if the subsidiary's profit is taxed at a rate lower than 55 per cent of the Swedish rate.

However, care will have to be taken that the inclusion of EU states within the list of secrecy jurisdictions is compliant with European law. Although direct taxation is not within the purview of the European Union in the same way as indirect taxes, for example, VAT, EU member states must nevertheless exercise their powers of direct taxation in a manner that is consistent with European law including the fundamental freedoms: free movement of capital (Article 63 of the Treaty of the Functioning of the European Union); freedom of establishment (Article 49) and possibly the freedom to provide cross border services (Article 56). Challenges at the European court of Justice to the CFC rules have resulted in reforms in the regimes operated by Germany,[89] Portugal,[90] Spain,[91] and Denmark.[92] However, there are a range of established justifications for restrictive tax measures – such as the need to ensure effective fiscal supervision, the prevention of tax evasion, the preservation of the cohesion of the national tax system, and the balanced allocation of taxing jurisdiction between member states.

As long as the tax is well designed and proportionate it should be robust to any challenge. After all, higher risk taxpayers who were users of secrecy jurisdictions are neither paying a higher rate of tax nor paying that levy on a wider tax base. They are merely excluded from one streamlined computation method. This is necessary and proportionate because their use of the offshore finance industry may make the calculation of their true wealth inaccurate when imputing a capital sum from (potentially under-declared) capital income.

CONCLUSION

The European social democratic model of marrying market dynamism with regulation to curb abuses, and progressive taxation to achieve greater equality and fund public services, is still very much alive. However, it needs defending. Centre-left parties in post-crash Europe have to navigate a narrow electoral path between the simplistic temptations of populism, and the dangers of being seen as indistinguishable from parties of the centre-right when faced with large public deficits.

A one-off 'unique contribution' might help Labour and other social democratic parties to navigate this path between populism and conservatism: it is an authentically left wing method of reducing deficits in an era of vast wealth inequality.

Nevertheless, presented in the wrong way, wealth taxes will worsen, not improve Labour's chances of winning future elections. The unique contribution is therefore carefully designed to address inequality whilst going with the grain of people's instincts around fiscal rigour and fairness: with a high threshold of £10 million, and a commitment to using the revenue to reduce the deficit, it sends a rather different signal than a perennial wealth tax with revenues allocated towards, say, housing benefit. A one-off levy also avoids any potential problems of emigration, avoidance, or investment mis-allocation that opponents of annual wealth taxes like to highlight. It is an easier political project than a permanent tax.

> A one-off 'unique contribution' might help Labour and other social democratic parties to navigate this path between populism and conservatism

The unique contribution, by easing taxes on earned income and work, is also a small step towards opening up a divide between Labour and the Conservatives around the treatment of unearned income.

The current tax system is skewed in favour of unearned income. To take two recent prominent examples: national insurance contributions aren't paid on unearned income such as the £46,000 that David Cameron earned from renting out one of his houses; and the £200,000 gift from his mother will almost certainly be taxed less heavily than the £140,000 salary he earns as prime minister. The merit of taxing the proceeds of hard work and enterprise less heavily than unearned income is hard to explain.[93]

This proposal (or others, such as the idea of re-introducing an earned income discount into income tax)[94] might be politically useful. The Conservatives are attempting to paint Labour as a party of 'skivers not strivers'. It might be possible to turn that accusation back on to the Tories if Labour looks seriously at differentiating between earned and unearned income. This is fruitful terrain. After all, the Labour party is a party of work.

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ENDNOTES

1. Comparing a household at 99th percentile, with one at the 10th percentile. Chapter 7 Extended Analyses (Figure 7.7 and table 7.7), Wealth in Great Britain 2012–14, Assets and Wealth Survey. Also see Danny Dorling, What Everyone Needs to Know About Wealth in the UK, New Left Project, 11 September 2014.

2. Facundo Alvaredo, Anthony Atkinson & Salvatore Morelli, The Challenging of Measuring UK Wealth Inequality in the 2000s, Fiscal Studies, vol 37, no 1, 2016.

3. Sunday Times Rich List 2016 p.28. ONS Wealth & Assets Survey Wave 4 (2012–14), Fig 2.3.

4. Gabriel Zucman, The Hidden Wealth of Nations, 2015

5. How public sector debt as a percentage of GDP has grown over the last 10 years, Office of National Statistics, 21 August 2013, available at: http://www.ons.gov.uk/ons/rel/psa/public-sector-finances/july-2013/sty-public-sector-debt.html

6. Public sector finances: March 2016, Office of National Statistics. Table 1.2 Economic and Fiscal Outlook, Office of Budget Responsibility, 2016, p.14.

7. NHS Five Year Forward View, 23 October 2014, available at: http://www.england.nhs.uk/wp-content/uploads/2014/10/5yfv-web.pdf

8. Fiscal sustainability report, Office of Budget Responsibility, July 2014, available at: http://cdn.budgetresponsibility.org.uk/41298-OBR-accessible.pdf

9. A Rainy Day Fund: Why Britain needs a financial sector revenue stabilisation account, with Victoria Barr, Fabian Society, 2012, available at: http://www.fabians.org.uk/wp-content/uploads/2012/12/A-Rainy-Day-Fund.pdf

10. I'm grateful to Dr Margit Schratzenstaller-Altzinger, Deputy director of the Austrian Institute of Economic Research, for this point. While some on low and middle incomes will benefit from gilts through their private pensions, the (roughly) quarter of the UK population with no private pension provision will not. See also Sandy Brian Hager's research on who owns US public debt, for example: Public Debt in an Unequal World, 2016, available at: https://www.city.ac.uk/__data/assets/pdf_file/0004/299974/CITYPERC-WPS-201601.pdf. However, a lot depends on other factors including prices – this under-explored area of economics is summarised briefly in Public Debt And Its Unequalizing Effects, 2014 PhD thesis by Victor Amoureux supervised by Thomas Piketty, available at: http://piketty.pse.ens.fr/files/Amoureux2014.pdf

11. Each year the basic state pension is uprated by the higher of the CPI inflation measure, average earnings or 2.5% – the so-called 'triple lock'.

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