

CAN THE WEALTH TAX BE A REMEDY FOR PUBLIC FINANCE AND REDUCE WEALTH INEQUALITIES IN POLAND?

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Key message

Wealth tax proponents suggest that it should be introduced in order to reduce wealth inequalities and to gain additional tax revenues. In this paper, based on empirical data, I will attempt to prove that these objectives are hardly attainable through wealth tax.

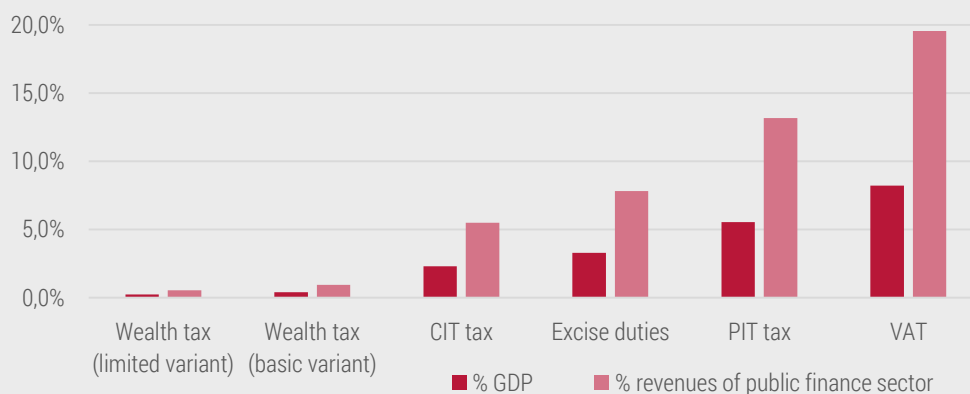
The impact of wealth tax on wealth inequalities would be rather low, as would any revenues resulting from its introduction. The tax would be paid by a relatively small number of taxpayers. Furthermore, the administrative requirements to collect it would be expensive and complicated. Therefore, since the benefit-cost ratio is unfavourable, the implementation of a wealth tax is an unfeasible solution.

Instead, the objectives behind the wealth tax may be attained more effectively through a more progressive tax system and the imposition of an inheritance tax.

Facts and figures

- **Nearly PLN 500,000:** the average household wealth in Poland (2016);
- **22%** of the total wealth value is held by the 1% most wealthy households in Poland;
- **40%** of potential wealth taxpayers receive a pension;
- **25%** of potential payers have an income below the average;
- **PLN 5-9 billion** (0.2–0.4% of GDP) is the potential value of revenues to be gained if the wealth tax is introduced.

Potential revenues from wealth tax in comparison with other taxes



1. Introduction

Wealth tax proponents advocate that this measure will reduce wealth inequalities and mobilise additional tax revenues. As a result of the substantial growth of the public debt due to the COVID-19 pandemic, some economists and politicians have proposed introducing a wealth tax in order to accelerate repayment of the debt. Due to an increase in wealth inequalities as observed over recent decades, there is a growing need to apply instruments which would limit or reverse this trend.

The idea of introducing a wealth tax is very popular. It played a considerable role in the U.S. presidential campaign. Among the political parties in the Polish Parliament, the Razem Party is demanding the introduction of a wealth tax. The International Monetary Fund also suggests that the option should be considered (IMF, 2020).

The research I have conducted helps estimate tax revenues and the extent to which inequalities may be reduced following the implementation of a wealth tax in Poland. Based on this research, it will be possible to discuss the wealth tax based on empirical arguments.

In Poland, a wealth tax would not be able to generate high tax revenues. In comparison with taxes constituting the main source of income for the public finance sector (CIT, PIT, excise duty, VAT), revenues from a wealth tax would be quite low. Such a tax would need to be collected for approximately 20 years in order to cover the fiscal costs of the aid programmes implemented after the COVID-19 pandemic.

Its impact on the level of wealth inequalities would also be minimal. Implementation of the tax would reduce the share of the wealthiest households in the total wealth of households, but without generating a substantial effect on the value of the Gini coefficient¹. The wealth tax might limit accumulation of the greatest fortunes, reducing the development of rich “dynasties”. However, this objective might be achieved more efficiently with the use of the inheritance tax.

The limited impact of a wealth tax on the level of wealth inequality and low tax revenues result from the relatively small size of the group of potential taxpayers. The relatively low wealth of the richest people in Poland is also of key importance. This is a natural consequence of the short period of free accumulation of wealth in Poland. 40% of potential payers receive a pension. 25% of potential payers have an income below the average rate.

To reduce economic inequalities and mobilise additional tax revenues are both worthy goals. However, these objectives may be achieved more efficiently through other reforms: a more progressive tax system and imposing an inheritance tax.

In the next section of this paper, I am going to present basic facts concerning wealth taxes in OECD countries. Next, I am going to discuss the advantages and disadvantages of wealth taxes. In the fourth section, I am going to present the results of empirical analyses of potential tax revenues and reduction of wealth inequalities following the implementation of a wealth tax in Poland. In the last section, I am going to present public policy conclusions.

¹ The Gini coefficient is a measure of inequality, including wealth inequality. Its value ranges from 0 to 1. A higher value of the coefficient represents a higher value of inequality.

2. Wealth taxes in EU and OECD countries

In this section, I will present the most important information concerning wealth taxes. First, I am going to describe their mechanism, and then the extent of their application in EU and OECD countries, including Poland. Next, I am going to discuss the tax revenues generated by wealth taxes in countries collecting such taxes.

In this paper, I am going to present the consequences of implementing a net wealth tax. I have assumed that net wealth worth is equal to the value of assets (including, but not limited to, real estate, savings, companies) reduced by the value of debts incurred. I have assumed that taxpayers would be individuals. There are also other forms of wealth taxes, including but not limited to: taxation of financial assets, real estate, inheritance tax. Table 1 shows basic information on the selected types of wealth taxes.

Table 1. Selected forms of wealth taxes

<u>Net wealth tax</u>	<u>Tax on the value of assets reduced by the value of liabilities.</u> <u>Currently collected in Spain, Norway and Switzerland. Collected in France until 2018.</u>
Tax on the value of financial assets	Taxation with a narrower scope than the net wealth worth tax. Collected in Belgium and Italy, among other countries.
Real estate tax	Applicable to real estate only, sometimes based on a different ratio than the value of the property. Collected in most OECD countries. Collected in Poland, but mainly paid by corporate bodies.
Inheritance and gifts tax	Collected at the time on inheriting assets/receiving a gift. Additional appraisals are not required. Collected in the vast majority of OECD countries, with varying practical significance. In Poland, tax revenues are limited due to immediate family members being exempt from inheritance and gift tax.
Capital gains tax ("Belka" tax)	The tax is not levied on the wealth itself, but on the revenues gained with it. Collected in the vast majority of OECD countries.

Source: own work based on OECD (2018).

The economic theory does not offer clear answers to the question about the optimal rate for capital tax. The theoretical models indicate 0%, however, they are currently under criticism due to the assumptions made. If some of the assumptions are changed, the resulting optimal rate for capital tax will be more than zero (OECD, 2018). We should also keep in mind that household wealth is not identical to capital.

Wealth taxes are often compared with capital gains taxes. If someone with a net worth of PLN 10 million makes capital gains of 4%, a 1.5% wealth tax corresponds to a 37.5% capital gains tax. Naturally, not all wealth components generate gains (e.g., real estate properties we live in do not generate direct gains).

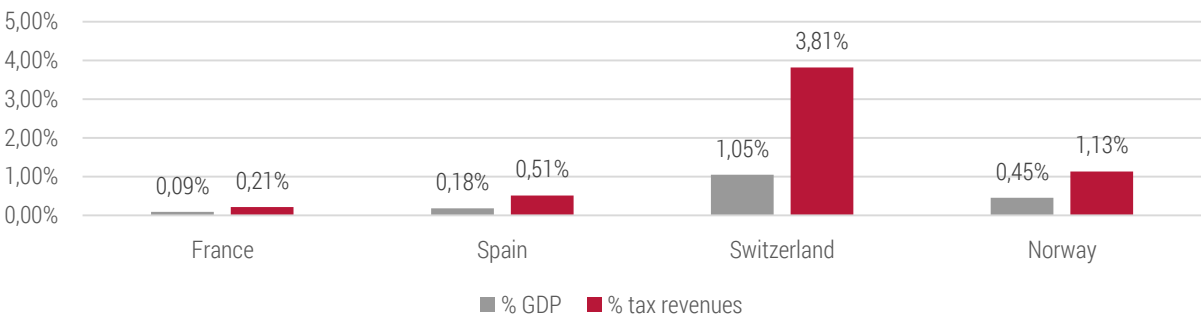
Wealth tax can also be compared with inheritance tax. Both are based on the value of property. If someone with a net worth of PLN 10 million pays a 1.5% wealth tax on an annual basis, the payment will correspond to a 45% inheritance tax after 30 years. However, the wealth tax does not fully substitute the inheritance tax.

The number of countries collecting wealth taxes is decreasing. In 1990, the tax was collected in twelve OECD countries, and now there are only three countries collecting the tax: Spain, Norway and Switzerland. The wealth tax was collected in France until 2018, but it has since been reformed; now, taxation is levied mainly on real estate. Italy and Belgium collect a wealth tax only on selected assets. In many countries, value-based real estate taxes are levied (OECD, 2018).

The discontinuation of wealth taxes was mainly due to the low revenues generated and high costs of collection. Wealth taxes are very complicated in terms of their administration. Valuing assets is difficult and may pose numerous problems. In the European countries, the ease in which individuals were able to avoid taxes through migrating/transferring their assets to another EU country a caused a considerable problem. Due to different treatments of various categories of assets (e.g., exemptions for corporate owners), the progressive nature of wealth taxes was frequently disturbed.

In countries collecting wealth taxes, their significance for the public finance system is low. Wealth tax revenues range from 0.09% of GDP in France to 1.05% of GDP in Switzerland (2018). The share of wealth tax revenues in the total tax revenues of the public finance sector ranges from 0.21% in France to 3.81% in Switzerland. Wealth tax revenues with reference to total GDP value and total tax revenues of the public finance sector are shown in Figure 1.

Figure 1. Wealth tax revenues with reference to the GDP value and tax revenues of the public finance sector



Source: own work based on the OECD Global Revenue Statistics Database.

Wealth taxes have often been used as an extraordinary measure in crisis situations. In Poland, an emergency wealth tax was introduced after World War I as part of a series of reforms implemented by Minister Grabski (see Box 1). Many countries introduced the tax after World Wars I and II. Emergency wealth taxes were also used to help mobilise revenue budgets after the 2008/2009 financial crisis in Ireland and Iceland. In 2020, Argentina introduced an emergency wealth tax in order to cover a part of the costs related to the COVID-19 pandemic.

In Poland, a net wealth tax is currently not applied. Taxes collected include real estate taxes as well as inheritance and gift taxes. The real estate tax constitutes an important source of income for municipalities. The fiscal significance of the inheritance and gifts tax is low due to immediate family members being exempt from the tax.

Box 1. Wealth tax in Poland in 1923 – hopes not fulfilled

On 11 August 1923, the Sejm adopted the Act implementing an emergency wealth tax. It was intended as a one-off tax payment to cover the budget deficit caused by expenditures needed for organisation of the armed forces and rebuilding following the war.

The wealth tax was highly complicated. There were as many as 33 progressive tax rates. During the period when the tax was collected, a range of regulations and circulars were issued, changing its rules of operation. The valuation of property was to be based on a range of complex tables. The total value of the property taxed was much lower than assumed, and the revenues collected represented only 40% of the anticipated amount.

Replacement of the emergency wealth tax with an annually collected tax was considered. The proposal did not take effect, but it shows the existing temptation. Development of infrastructure for collection of the (emergency) wealth tax reduces costs of implementation of a permanent solution.

3. Advantages and disadvantages of wealth taxes

In this section, I am going to present arguments for and against the introduction of a wealth tax. The most important argument in favour of the tax is the possibility to gain tax revenues while concurrently achieving a vital social objective, namely a reduction in wealth inequality. The most important arguments against the tax are numerous options available to avoid the taxation and administrative problems, particularly in terms of asset valuation. For a summary of the major arguments for and against introduction of a wealth tax, see Chart 1.

The taxation of wealth is supported by the clearly higher concentration of household wealth than of income. Inequality in the distribution of wealth is higher than inequality in the distribution of income. In many developed economies, a substantial growth in wealth inequality has been noted for the past several decades. Wealth taxes are able to reduce such inequalities and promote equal opportunities. In practice, however, their impact on wealth inequality is weak because the taxes are quite low and paid by few households. Nevertheless, they may substantially limit further growth of the greatest fortunes. Wealth taxes – if treated as a surcharge on income tax – considerably strengthen the progressivity in the tax system².

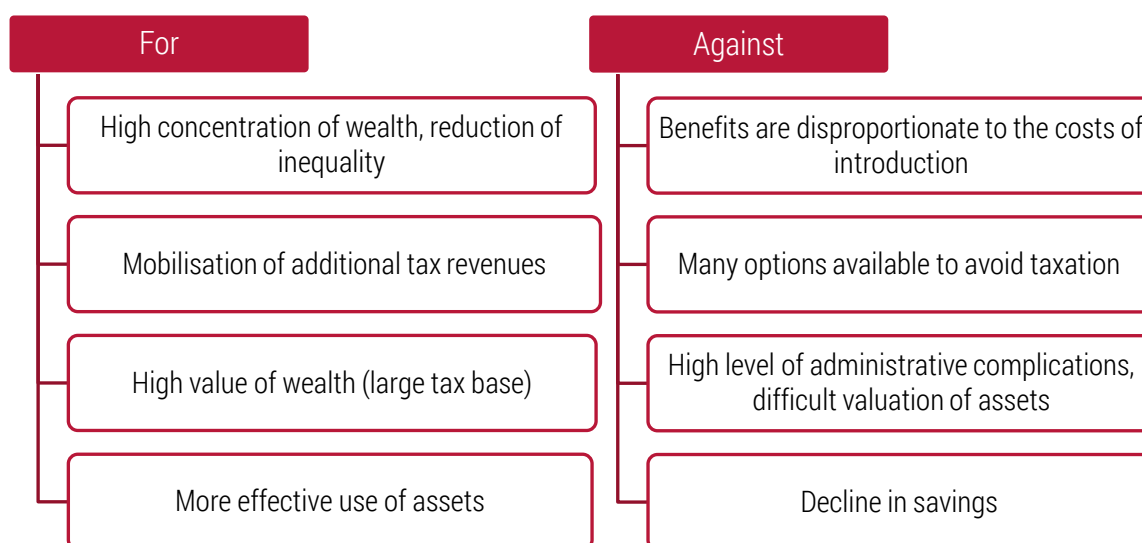
An argument supporting levying taxes on household wealth is the considerable growth of its value. In developed economies, the value of wealth has grown both in nominal terms and in proportion to GDP in developed economies for the past several decades. This way, the tax base is large and grows with time.

Wealth taxes may contribute to a more effective use of assets. Due to their introduction, taxpayers may change the structure of assets, reducing those not generating revenues. For example, implementing a wealth tax may

² Progressivity in a tax system is usually analysed by comparing the amount of paid income tax and social insurance contributions with income. If the amount of wealth tax is added to the analysis, the tax system becomes more progressive.

induce people to liquidate zero interest bank deposits and bond investments. It can also result in increasing investment in human capital, which is not taxed.

Chart 1. The most important arguments for and against the introduction of a wealth tax



Source: own work.

Implementation of a wealth tax may discourage some households to save and accumulate wealth. Empirical literature concerning the impact of wealth taxes on the savings rate is quite scarce; however, it usually mentions their statistically significant (although rather low), negative effect on the savings rate, value of property and changes in the structure of assets.

Correct valuation of assets poses a serious problem, hindering collection of the wealth tax. Valuation of unlisted companies is particularly complicated. Such companies represent a major part of the richest households' wealth. The valuation of listed companies can also be controversial. Listed companies with a higher valuation do not necessarily generate higher profits for their owners, since the valuation is affected not only by fundamental factors. Valuation of assets is also necessary when collecting inheritance tax. However, its advantage lies in the fact that the tax is collected when the valuation is nevertheless necessary. Therefore, its collection does not require an additional valuation.

Many wealthy households have a low income. Real estate properties which do not generate revenues constitute a substantial part of household wealth in Poland. Therefore, some of the households would not be able to pay the wealth tax. This problem may be solved through limiting the rate of the wealth tax to a certain part of the household's income. In the event of real estate property, it is also possible to accumulate unpaid wealth taxes through a mortgage and to have them paid upon death.

Free movement of capital and functioning of tax havens provide more options for avoiding taxes. The wealth accumulated in tax havens is equivalent to 10% of the world's GDP (Zucman, 2013). Due to the fact that the richest households are more capable of using tax havens, there is a risk that the wealth tax actually proves to be regressive – the effective tax rate for single-digit millionaires will be higher than the tax rate for multimillionaires. The value of assets owned by Polish citizens in foreign countries amounts to approx. 7.2% of GDP (Vellutini et. al., 2019).

Introduction of a wealth tax in Poland is difficult due to the free movement of capital within the EU. It is relatively easy to avoid a wealth tax introduced in one of the Member States. However, if the tax is introduced on an EU level, tax avoidance would be more difficult.

4. Wealth tax in Poland

In this section, I am going to present the results of estimations of tax revenues that may be acquired due to the implementation of a wealth tax. Next, I am going to discuss the impact of the wealth tax on the level of wealth inequality in Poland.

I have identified the taxpayers of two variants of the wealth tax and estimated the tax revenues generated upon implementation of each variant. In the basic variant, the tax will be paid by households with a net worth exceeding one million PLN; the limited variant will cover households with a net worth exceeding five million PLN. The value of wealth below the tax threshold is not subject to taxation. Both tax variants are progressive. This means that wealthier households pay higher taxes. The methodology of estimation is shown in Box 2.

Tax rates have been chosen under the assumption that its nature is not confiscatory. The purpose is to generate additional tax revenues and not to eliminate fortunes with a value exceeding the specified threshold. The application of progressive tax rates is justified by higher rates of return achieved by wealthier households. The existing literature on the subject suggests that the rate of return on capital grows together with the value of the property.

Table 2. Analysed variants of the wealth tax

Value of property	Tax rate
Less than PLN 1 million	0%
PLN 1-5 million	0.5% (basic variant) 0% (limited variant)
PLN 5-10 million	1%
PLN 10-50 million	1.5%
More than PLN 50 million	2%

Source: own work.

Box 2. Methodology of estimation

My estimations are based on survey data. For this purpose, I used data from the Eurosystem Household Finance and Consumption Survey (HFCS). The HFCS was conducted in Poland as the Household Wealth and Debt Survey (pl. *Badanie Zasobności Gospodarstw Domowych*) in 2016 by the National Bank of Poland and Statistics Poland.

I supplemented the survey data based on information published in the lists of the richest people. Due to the fact that rich people rarely take part in surveys, it is necessary to estimate the value of their wealth. The adjustment was based on the Forbes list of the richest people, published in March 2016 (Forbes, 2016). The method is generally applied in this kind of scientific research (Brzeziński et al. 2020).

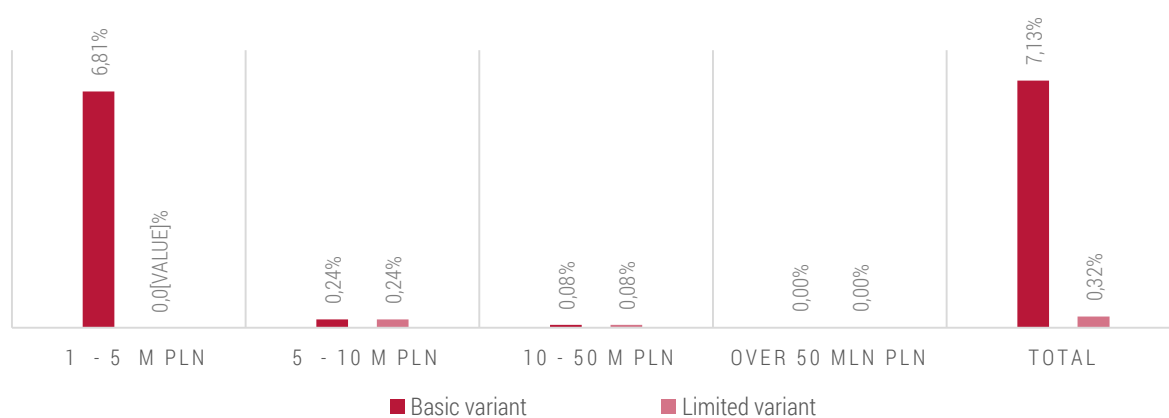
I have assumed that households are taxpayers. This is necessary due to the source of data. I have also assumed that households tend to avoid taxation. Actual wealth tax revenues collected are 25% lower than the amount due.

Revenues from a wealth tax introduced in accordance with the rules described in Table 2 would be relatively low. The wealth tax would be paid by less than 10% of households. For information on the revenues and number of taxpayers, see Fig. 2 and 3. For information on wealth taxpayers, see Box 3.

It is difficult to estimate administrative costs; however, the costs are higher than for most functioning taxes. These include, but are not limited to, the costs of property valuation, tax calculation and assessing the accuracy of the calculations. High costs of collection in relation to revenues generated by wealth taxes were one of the reasons for discontinuing the wealth tax in OECD countries. Collection of the wealth tax would also be complicated for taxpayers and would generate considerable costs (time, remuneration for accountants) on their part as well.

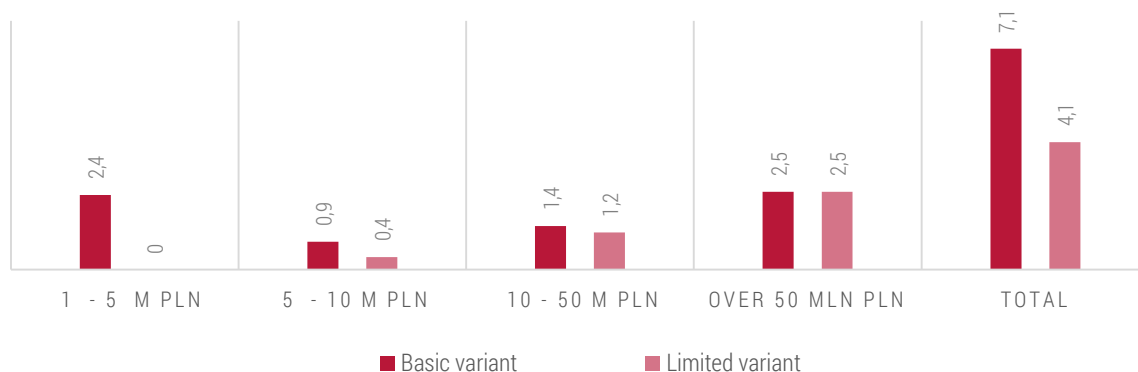
The highest revenues would be generated by households with a net worth exceeding PLN 50 million. The tax rates are sufficiently high to have those 500 households pay a higher amount of tax than nearly a million households with a wealth of PLN 1-5 million.

Figure 2. Percentage of households paying the wealth tax



Source: own work based on data from the Eurosystem Household Finance and Consumption Survey, adjusted by the wealth of the richest.

Figure 3. Revenues from wealth tax (in PLN billion)



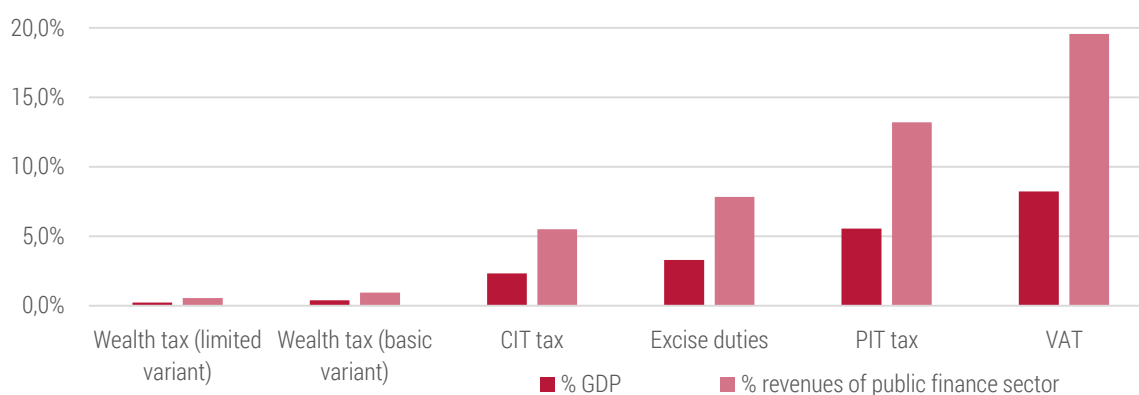
Source: own work based on data from the Eurosystem Household Finance and Consumption Survey, adjusted by the wealth of the richest.

The value of wealth tax revenues would be stable over time. The value of property in relation to GDP is changing slowly, so the assumption of constant revenues in relation to GDP is rather safe. In 2019, wealth tax revenues would reach PLN 5.1 and 8.8 billion respectively, which is a small amount in comparison to the most important taxes.

Potential revenues for the public finance sector due to implementation of the wealth tax are low. CIT, excise duty, PIT and VAT generate considerably higher revenues. To see how they compare with wealth tax revenues, see Figure 4.

The correlation between the wealth and income of households in Poland is relatively low. Nearly 40% of potential taxpayers in Poland receive a pension. One-quarter of potential taxpayers have an income below the average income of households in Poland. Therefore, collection of the wealth tax is difficult. Thus, it would be desirable for rich households to have a high income as well. Poland's situation (which is similar to other CEE countries) differs from this pattern. One of the contributing factors was the enfranchisement of real estate property after 1989.

Figure 4. Potential revenues from the wealth tax in comparison to other taxes



Source: own work based on data from the Eurosystem Household Finance and Consumption Survey and the Macroeconomic Data Bank of Statistics Poland.

Potential revenues from wealth tax collection in Poland are limited due to the relatively low wealth of the richest people in Poland in comparison with other countries. The total value of wealth of the 100 richest people in Poland amounts to less than 7% of GDP. In Hungary, the value amounts to 10%, in Germany to 15.3%, in France to 23%, and in Norway – nearly 30% of GDP. It is worth noting that all OECD countries collecting the wealth tax are countries where wealth has been accumulated for many generations.

The impact of the wealth tax on the level of wealth inequality would be low. The value of the Gini coefficient would fall almost imperceptibly. The 1% share of the richest households in the total wealth would change more considerably. For information on the impact of the wealth tax on the level of inequality, see Figure 5.

The wealth tax might limit growth of the greatest fortunes. The growth in the value of wealth owned by the 100 richest people in Poland (the Forbes list) would be approximately 20% slower. These calculations do not account for a change in strategy of property management, which would probably occur after the introduction of the wealth tax.

Box 3. Who are potential wealth taxpayers?

The overwhelming majority of wealth taxpayers would be households with a net worth of PLN 1-2 million. Nearly 80% of all potential taxpayers belong in this group. Their wealth constitutes nearly a half of the total wealth of the households which would be wealth taxpayers.

Real estate property represents a major part of the wealth of the wealth taxpayers. Practically all households belonging to the analysed group own a real estate property as their place of residence. On average, its value represents slightly more than half of their assets' value.

One-quarter of households with a wealth of PLN 1-2 million have an income below the average income in the population. The assumed wealth tax rate (0.5%) is probably the highest that could be levied on properties with this value. The potential taxpayers have income from self-employment more frequently than most households in Poland. However, many of them have already become economically inactive. Nearly 40% of potential payers receive a pension.

Figure 5. Short-term impact of wealth tax on wealth inequalities



Source: own work based on data of the Eurosystem Household Finance and Consumption Survey, adjusted by the wealth of the richest.

5. Summary and public policy conclusions

The introduction of a wealth tax would generate low tax revenues. Such revenues would be limited due to the low numbers of taxpayers and low wealth (in comparison with other countries) of the richest taxpayers.

The impact of the wealth tax on wealth inequality would be minimal. This is due to the fact that it would be paid by relatively few households. However, the tax may limit growth in the value of the greatest fortunes.

Collection of wealth taxes is expensive and complicated in terms of administration. Its calculation and control are more difficult than for most taxes. Valuing many assets is complicated, which hinders the functioning of the wealth tax. This problem applies in particular to corporate bodies. This is a very important point because companies constitute a major part of the wealth of the richest.

The introduction of a wealth tax would be difficult due to the relatively weak correlation between the value of wealth and the value of income gained by households. 40% of potential payers receive a pension. 25% of potential taxpayers have an income below the average income of households in Poland.

Implementation of the wealth tax in Poland as an EU Member State is difficult due to the free movement of capital. If the wealth tax was levied throughout the EU, tax avoidance would be less feasible.

In my opinion, it is impractical to implement a wealth tax in Poland because the costs would be too high and the benefits too insignificant. We should look for more effective solutions to help us achieve the same objectives.

One solution which is simpler than introducing a net wealth worth tax is to levy tax on selected categories of assets, mainly real estate and financial assets. Due to the fact that business enterprises constitute a major part of the richest households' wealth, there is a risk that the effective rate of tax for the richest will be lower than for slightly less wealthy households.

Strengthening the progressivity of the Polish tax system is currently a better option than introducing a wealth tax. In many cases, property income is subject to a flat tax. People with capital gains, irrespective of the amount, pay the 19% "Belka" tax. Similarly, business owners can pay the flat rate tax. There are also tax preferences available for those gaining rental income. Wealth income is often not covered by social insurance contributions or the contributions are lower than the ones paid in relation with income gained from employment. Progressive taxation on all categories of income (especially wealth income) and application of adequate social contributions should be considered. Such a solution is simpler than introduction of the wealth tax, and the same objectives can be achieved.

Fair taxation on inheritance currently constitutes a better solution than introducing a wealth tax. In Poland, the inheritance tax is practically of no significance because immediate family members are exempt from inheritance and gifts tax. Eliminating such preferences in the inheritance tax and increasing its rates would substantially increase the equality of chances. Thus reforming the inheritance tax is simpler than introducing a wealth tax, and the same objectives can be achieved.

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Additional information

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