

A Quantitative Assessment of the Net Wealth Tax: The Spanish Experience

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ABSTRACT

There is growing debate, both social and academic, about the possibility of levying an annual net wealth tax. Until a few years ago, such a proposal appeared difficult to both implement and control, but recent technological innovations, which could greatly facilitate the periodic valuation of wealth, combined with improvements in international tax information sharing could make a “modern wealth tax” possible. Nonetheless, a number of challenges regarding its design still need to be addressed. Taking advantage of the Spanish experience—the only EU country to levy a wealth tax—we undertake a quantitative analysis of various key legal elements of the current tax (exemptions and the common income and wealth tax ceiling) by means of a tax simulator we have developed; we also analyze its redistributive power. Our results show that the family business exemption and the common ceilings are highly regressive. We also assess the effectiveness of alternative reforms with more comprehensive tax bases.

Keywords: wealth tax, wealth distribution, redistribution, tax simulator, tax reform

1. Introduction

There is growing debate, both social and academic, concerning the possibility of levying an annual net wealth tax (henceforth, WT) ([Iara 2015](#)). This debate has been sparked as much by the large and increasing disparities in the concentration of wealth as by the technological improvements that could address some of the potential challenges of levying such a tax.

Concerns about inequality and low social mobility have become accentuated in recent years as the distribution of income and wealth has become more unequal, especially in the wake of the Great Recession¹. Over the last three decades, income inequality has grown in most OECD countries resulting in concern about the impact that growing differences between rich and poor might have on social cohesion. Some voices have even stressed the negative impact that inequality can have not just on society’s poorest but also on ensuring stable economic growth ([OECD 2015](#)). It has been argued that this negative effect results, in large part, from the limitations faced by the poorest segments of the population for investing in their education and skills. Likewise, the IMF has underlined the important association between less inequality and greater macroeconomic stability and more sustainable growth ([Lagarde 2012](#)). Although

no empirical studies to date allow us to affirm that greater inequality is the cause of lower growth, the importance of inclusive economic growth as an objective of economic policy has been recognized (Fuest et al. 2018).

Studies of inequality show that household wealth is much more unequally distributed than household income due to very high levels of wealth concentration at the top of the distribution (OECD 2015, Ch. 6). As Table 1 shows, wealth concentration is high everywhere in the world, but that there are marked differences between countries. The most obvious case is that of the USA, where the top 10% of households accumulate almost 80% of total household wealth. Yet, this high concentration has not always been the case (see, e.g. Piketty 2014, Ch. 10). After 1910, wealth concentration in Europe began to fall at a much faster rate than it did in the USA, so that by the 1960s, it was higher on the new continent. Moreover, an increasing trend in wealth concentration in the USA has apparently been documented since the beginning of the 1980s, although the actual outcomes crucially depend on the statistical technique employed to calculate concentration ratios (Kopczuk 2015). In Spain, wealth concentration is not especially high when compared to the ratios presented by most other OECD countries, but the Great Recession has had a significant impact: between 2005 and 2014, a 7 percentage-point rise was recorded for the top 1% (11 pp for the top 10%) (Anghel et al. 2018). All in all, not only is wealth inequality high, but recent trends seem to point to even greater levels of inequality or, at least, to a gap that is not being closed. It is for this reason that “the extent to which the well-off are going to rely on work versus rely on the returns to their wealth in the future is clearly important for assessing the extent to which a society will view itself as in some way a meritocracy” (Kopczuk 2015, p. 47).

Table 1. Concentration of Net Wealth (%). Selected OECD countries

	Australia	Denmark	France	Germany	Italy	Spain	USA	UK
Top 1%	15.00	23.62	18.65	23.66	11.69	16.32	42.48	20.05
Top 10%	46.47	63.98	50.59	59.76	42.78	45.58	79.47	52.50

Source: OECD Wealth Distribution Database; 2014 for all countries, except for Denmark (2015), Spain (2012) and the USA (2016).

To mitigate the negative impact of such a scenario, various authors have proposed the introduction of a WT. Piketty (2014, Ch. 15) proposed a ‘global capital tax’, since tax base mobility is a key constraint for maximizing the effectiveness of this tax at the national level². Atkinson (2015) identified a “re-examination of the case for an annual wealth tax and the prerequisites for its successful introduction” (p. 201) as an idea to pursue, although a few years earlier the Mirrlees Review had reported being contrary to such an option (Boadway et al. 2010). More recently, Saez and Zucman (2019a,b) have examined the case for the USA, including the prerequisites cited by Atkinson, and estimated its impact.

The aim of this article is to complement this literature with a simulation analysis of the WT based on the Spanish experience, the sole EU country with a WT. In particular, we quantitatively analyze the impact of key elements of the tax according to the national regulation. We are able to perform our simulation analysis thanks to the construction of a tax simulator (the so-called SIMPA) based on the Survey of Household Finances of the Bank of Spain (see, e.g. Bover et al. 2018)³. This survey, conducted every three years since 2002, contains information about 6120 households, with top households being overrepresented. We exploit the 2014 survey. These survey data allow us to consider all the details of the Spanish WT, enabling us to analyze the impact of the pertinent legal factors on redistribution. The Survey of Household Finances also allows us to compare the actual amount of tax revenue collected with the estimated amount that could potentially be collected. This should prove useful both for assessing the current role played by the tax and for guiding reforms in Spain and in other countries based on this experience.

According to our simulator, the current WT revenues collected account for just 44.6% of the estimated total that should be collected. In other words, potential revenues, €3692 M, are approximately 2.25 times greater than real revenues, which means the weight of the tax with respect to GDP could be raised from the current 0.18% to 0.46%. One reason for this sizable difference is that in the survey all assets are valued at market prices, but this is not always the case under the prevailing law for assets such as real property or closely held businesses, two assets that alone account for 75% of overall household wealth in Spain. A further reason for this large shortfall could be tax evasion. Based on

information contained in the 2014 universe of WT returns for Catalonia, [Durán-Cabré et al. \(2019b\)](#) estimated a “tax gap” of 44.34% for that Spanish region⁴.

The simulator also allows us to examine elements of its current design that might be undermining the redistributive impact of the tax: the ceiling on joint WT and personal income tax (PIT) liabilities and exemptions⁵. The WT could create liquidity constraints for taxpayers when their wealth is high but their income low. To avoid this, there is a ceiling on WT liability, which along with PIT liability cannot exceed a certain percentage of the taxpayer’s annual inflow of income. Legally speaking, the ceiling on WT and PIT liabilities is derived from the Spanish Constitution, which holds that the tax system cannot become confiscatory. Under WT rules, first dwellings, up to a maximum value, and family business assets are also exempt. Leaving aside the impact of these two elements on tax avoidance ([Durán-Cabré et al. 2019a](#)) and evasion ([Durán-Cabré et al. 2019b](#)), the combination of both benefits severely tames the redistributive power of the tax (i.e. these benefits are regressive with respect to wealth). These results should be of interest to those countries that are considering the introduction of a WT in their tax system.

According to our calculations, the tax ceiling and the exemptions cause a fall in potential revenues of €5,730 M, that is 1.55 times the potential revenue. Both kind of tax expenditures are mainly concentrated on richest households: the average rate for the top 1% (10%) decreases .364 (.149) percentage points. All in all, the negative impact of these elements needs to be taken seriously into account if the objective is to use this tax as a redistributive tool. We propose and simulate reforms with a comprehensive tax base in order to avoid such loopholes but, in general, we maintain the tax ceiling, given that the principle of non-confiscation is a legal requisite in the Spanish case.

From the survey data, we calculate that the top 1% (10%) holds 19.53% (51.86%) of total net wealth. And while the redistributive effect of the WT in the very short run is low, when a longer-run perspective is adopted the level of redistribution might increase notably, with concentration ratios falling to 19.23% (51.63%) after 5 years and to 18.14% (50.79%) after 25 years. We show the impact over such long periods of time in order to illustrate how difficult it is to achieve reductions in wealth concentration. Nevertheless, if assets are under-valued and evasion is high, revenues are much smaller and the redistributive impact of the tax becomes insignificant, even in the longer run.

The rest of the article is organized as follows. In Section 2, we briefly discuss the respective advantages and disadvantages of the WT and review the main legal elements that need to be considered in its design in order to maximize the tax’s positive impact. Traditional perspectives have to be reconsidered in the light of new technology advances, which usher in talk of a ‘modern wealth tax’. In this section, we also examine the aspects of the Spanish experience that can be informative for those countries considering the introduction of a WT. In Section 3, we summarize the main legal elements of Spain’s wealth tax and we present the tax simulator used to analyze the current operation of the Spanish tax. In Section 4, we quantitatively analyze specific elements of the current tax, and also assess several alternative reforms. Section 5 concludes the article.

2. The Wealth Tax: A Critical Appraisal

2.1 General review

One of the advantages of a WT is its potential role as a ‘self-checking mechanism’ ([Kaldor 1956](#)); that is, the information contained in a WT return should be useful for controlling capital income compliance in the PIT and even in the inheritance and gift tax or, at least, it should serve as a “self-reinforcing penalty system of taxes” ([Shoup 1969](#)). However, serious doubts have been raised about the effectiveness of this role. In fact, it may mean just the contrary: third-party reporting is key to ensuring WT compliance, as is already the case with current income taxes. For this reason, in the case of a ‘modern wealth tax’, third-party information should cover the widest set of assets and debts as possible (see [Saez and Zucman 2019a](#), section 4). Otherwise, tax evasion not only reduces potential WT revenues but also its redistributive power.

Wealth gives its owners an additional economic capacity—including greater security, status, or power—to that afforded by their income. This means that any tax on this wealth requires the periodic valuation of assets at their corresponding market value; however, this is far from straightforward because assets are being valued solely for tax purposes and not as part of a market transaction ([Sandford 1995](#)). This difficulty affects, in particular, such assets as real property, closely held businesses and works of art, and has traditionally been considered an important drawback for the levying of a WT. The accuracy of such valuations could only be achieved by incurring high administrative and

compliance costs. In determining the choice of valuation methods, the [Meade Committee \(1978\)](#) identifies the two major considerations to be borne in mind: i) the need to keep administrative and compliance costs as low as possible and ii) the need to employ methods that minimize uncertainty. And it concludes that ‘these considerations should on occasion take precedence over the desire to obtain a genuine open-market valuation’⁶. This is particularly relevant in the case of real estate values, as cadastral values are typically not up to date with market prices, which undermines the tax’s horizontal equity⁷. Yet, a ‘modern wealth tax’ should be able to take advantage of the latest computer and information technology in devising a better approach to valuation ([Gamage 2019](#)). Indeed, the technology for systematically obtaining reliable real property values exists and could be adopted by the tax administration ([Saez and Zucman 2019b](#)).

Additionally, tax base mobility (in those cases where the WT is based on the residence principle) and the existence of tax havens might make it difficult to enforce tax compliance. This would require a “global capital tax” ([Piketty 2014](#)) or some form of tax coordination ([Piketty et al. 2013](#)). Indeed, recent advances in information sharing between countries (FATCA, the Directive 2011/16/EU on administrative cooperation in the field of taxation, or the OECD Global Forum) constitute what [Iara \(2015\)](#) refers to as a ‘new paradigm’ insofar as it might facilitate tax compliance in a globalized world. Thus, there are reasons for the proponents of the wealth tax to be relatively optimistic.

While the market-based valuation of assets and the availability of third-party information at both national and international levels are important, there are other issues that need to be considered in relation to the tax base. Exemptions on certain assets can undermine the redistributive power of the WT⁸, as taxpayers (typically the super-wealthy) are likely to exploit them by building their wealth portfolios so as to minimize the tax bill. It is for this reason that [Saez and Zucman \(2019a,b\)](#) propose a comprehensive tax base that includes all asset classes, and which avoids behavioural responses that might erode the tax.

Another key design element concerns the potential liquidity constraints resulting from taxing a stock variable. To address this issue, some countries introduced a tax ceiling, whereby the sum of the income and wealth tax liabilities is not allowed to exceed a certain percentage of an individual’s income. However, as with exemptions, rich taxpayers are likely to devise ways of reducing their income to take advantage of this limit. A very large WT threshold would avoid this possibility, since *a priori* the very top taxpayers should not be affected by such liquidity constraints. Nevertheless, if taxpayers were to face this problem (e.g. a taxpayer whose wealth consists basically of assets from an early-stage business that is not yet profitable), [Gamage \(2019\)](#) proposes an alternative course of action: namely, offering the option of a limited deferral regime for certain kinds of assets in conjunction with deferral-interest charges⁹.

Although the WT can have a real impact (just as the capital income tax does)—among others, on capital stock, entrepreneurial innovation, top talent migration, charitable giving and even family structure (as reviewed by [Saez and Zucman 2019a](#), section 3)—it is claimed that the WT might play a complementary role to a PIT. That is, the two taxes are not fully interchangeable¹⁰. This is because a capital income tax is not able to tax full income, basically due to the existence of unrealized capital gains. This means the wealth portfolios of the super-rich are usually managed through a holding company (or other legal entity) in such a way that they receive a sufficient annual income flow to cover their private consumption ([Piketty et al. 2013](#)). And although they will eventually have to pay these taxes, deferral constitutes an advantage for them. Hence, a WT should contribute to the principle of fair taxation. On top of that, the simple possession of wealth (independently of financial profitability) might confer utility on taxpayers, which would justify the taxation of these assets in the WT, or alternatively the imputation of an annual rent in the PIT. On the whole, for the very rich, capital is a better indicator than income of their ‘contributive capacity’ ([Piketty 2014](#)). The recommendation made by the [Stiglitz-Sen-Fitoussi Commission \(2009\)](#) quoted at the beginning of this paper also goes in the direction of including wealth as a measure of living standards.

2.2 Spanish review

With the restoration of democracy in 1977, and the establishment of a modern tax system, Spain introduced an annual WT. At that time, it was intended as a transitory tax, but it continues in force today. The main reason for its adoption lays in its role as a “self-checking mechanism” (as described in the previous section), but it was also introduced due to its redistributive power and as a complement to the PIT.

Spain’s WT was actually abolished by the socialist government in 2008, on the grounds that it had failed to achieve its redistributive goals; but, by the end of 2011, due to the crisis of the public finances, it was reintroduced. The

surprising argument offered in justification by the left-wing central executive—surprising insofar as the 2011 tax had not been redesigned, and so the tax’s drawbacks remained—was that those with more resources should be made to contribute more to the economic recovery, and by so doing this would reinforce equity and allow a better redistribution of income and wealth.

As well as the obvious fraud risk associated with low rates of tax control (Durán-Cabré and Esteller-Moré 2010), many experts highlight the inefficiencies and inequities resulting from the design of this tax (i.e. assessment rules that differ from market prices, tax exemptions, etc.). Apart from giving rise to horizontal inequities between taxpayers with similar levels of net wealth but with different asset portfolios, the specific characteristics of the WT significantly distort its incidence and redistributive role given that it is primarily the richest taxpayers who benefit from them (see, e.g. Arcarons and Calonge 2007; Alvaredo and Saez 2009).

Recently, Durán-Cabré et al. (2019⁵) have estimated a 44.34% ‘tax gap’ for Catalonia, with underreporting constituting the main source of the gap (97.3% of the total gap). Specifically, underreported offshore financial assets (58% of the total gap due to underreporting) and the inappropriate application of the family business exemption (37%) are the main underreporting mechanisms. Furthermore, the tax gap is mostly concentrated among the richest taxpayers: richest decile’s gap accounts for almost 75% of the total gap.

Given the persuasive nature of these arguments, both Esteller-Moré (2013) and the White Report, the “Lagares Report” (2014, pp. 224–240) have advocated the definitive abolition of the tax. However, the conservative government, in office from the end of 2011 to mid-2018, and the subsequent socialist government maintained the tax. With the arrival of the COVID-19, Unidas Podemos, one of the parties of the left-wing coalition ruling the government, has recently advocated for increasing the importance of the tax such that the top marginal tax rate would be 3.5%.

3. A Simulator (SIMP) of the Spanish Net Wealth Tax

3.1 How the tax is currently designed

The tax works under a self-assessment system, whereby taxpayers have to report and evaluate all the assets they have on the 31st of December. In order to mitigate any tax avoidance incentives (e.g. in the case of bank accounts, withdrawing money on 30th of December) or to tame high valuation volatility (basically, that of publicly listed shares), the value of some assets is calculated as the average over the last quarter. Market price should be the common valuation criterion, but the law provides other specific valuation criteria for important assets, whose values however can be quite distinct from their market price. This applies particularly to real estates, where for tax purposes the highest value between the acquisition price and the cadastral value is taken. In the case of the shares of entities that are not publicly traded, their value is usually calculated in accordance with the company’s balance sheet, that is, applying accounting criteria. The unit of taxation is the individual (not firms or households), so family wealth has to be allocated among members of the family.

Taxable wealth is net wealth, that is, the monetary value of all non-exempt assets minus debts. Apart from the standard exemptions, such as public and private pension plans and human capital, other assets are exempt: those belonging to Spain’s historical heritage as well as works of art and antiques (as long as their value does not exceed a certain figure). However, the two main exemptions are that of the first dwelling—up to a maximum of €300,000 per taxpayer—and that of equity affected by economic activities and participations in certain entities, that is, the exemption of family-owned or closely-held businesses. In this latter case, to be eligible for the exemption certain criteria must be met: namely, that there is an economic activity, conducted by the owner of the assets or by a close relative; that, as a consequence of this activity, the individual obtains income that constitutes his main source of revenue; and, in the case of incorporated activities, that the owner, individually or with a close group of family members, holds a minimum participation in the capital of the entity.

The Spanish WT is only levied on taxable wealth exceeding a minimum threshold—currently fixed at €700,000. WT returns have to be submitted in two circumstances: (i) when taxpayers have a positive tax liability, or (ii) when, although their tax liability is zero because their net taxable wealth is below the threshold, their gross wealth (including both taxable and non-taxable assets) is above 2 million euros. Tax liability is obtained by applying progressive tax rates to the net tax base, that is taxable wealth minus the minimum threshold. The progressive tax schedule is shown in Table 2. Moreover, there is a limit on WT liability: the sum of PIT and WT liabilities cannot exceed 60% of the

PIT base. If it does, the WT due is reduced, although this reduction cannot exceed 80% of the original tax liability; in other words, at least 20% of the original WT due must be paid. Therefore, for taxpayers with very high wealth but low income the effective wealth tax rate is in fact 20% of the statutory rate. Likewise, when applying the ceiling a number of specific criteria apply: most important, long-term capital gains (i.e. greater than one year) are not taken into account, although they form part of the legal definition of taxable income. [Figure 1](#) [AQ5] shows a summary of the legal design.

Figure 1. Summary of the legal design.

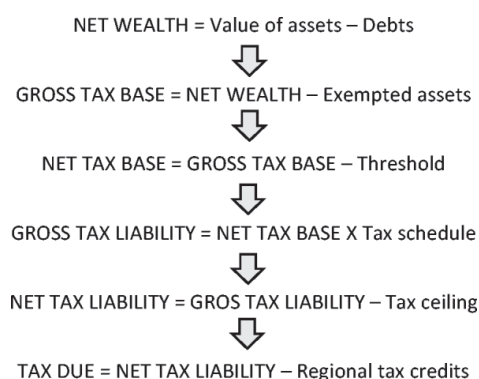


Table 2. Progressive tax schedule

Net tax base €	% Marginal rates
0.00–167,129.45	0.2
167,129.46–334,246.88	0.3
334,252.89–668,499.75	0.5
668,499.76–1,336,999.51	0.9
1,336,999.52–2,673,999.01	1.3
2,673,999.02–5,347,998.03	1.7
5,347,998.04–10,695,996.06	2.1
>10,695,996.06	2.5

The WT is a national tax regulated by a national law, but all revenues accrue to regional governments, which can also modify certain parameters: threshold, tax rates and tax credits. Tax credits are deducted from net tax liability. For instance, the Autonomous Community (AC) of Madrid has a 100% tax credit since 2011, which means its residents do not pay the tax. The ACs of the Basque Country and Navarre, which for historical reasons operate a different regional financing system, have full tax autonomy, although in broad terms the tax is similar in its application to the rest of Spain.

3.2 Simpa: the tax simulator

In order to analyze both the real and potential role of Spain's wealth tax, we have developed a tax simulator: SIM-PA (for details of its construction, see [Durán-Cabré and Esteller-Moré 2020](#)). The basic data are taken from the Bank

of Spain’s Survey of Household Finances for 2014¹¹, providing information about household wealth and income. Top households are clearly overrepresented (see Table 3), which is particularly relevant as the WT only levies richest individuals. Recall income data are critical for applying—when necessary—the WT tax ceiling. Here, we outline the six basic steps we take in the simulator:

Table 3. Survey of Household Finances 2014 (Bank of Spain): Basic statistics

Total number of observations		6120 households
Wealth tax filers of the sample vs. population		22% vs. 0.5%
Decile group	Observations	Oversampling rate ^a
90% to 95%	469	1.53
95% to 99%	813	3.32
100%	741	12.11

Source: Bover et al. (2018).

a Oversampling rate = number of observations actually in the sample to the number of observations if the sample was randomly drawn from the population.

1. We calculate net wealth and net income by household (i.e. the survey’s unit of response)¹².
 2. We transform these magnitudes to the taxpayer level using the fiscal concept of ‘splitting’, when the household comprises a married couple¹³.
 3. We apply, when the legal conditions hold, the exemptions in the WT return (first dwelling and family business) and, additionally, the deductions applicable to each tax base (contributions to private pension plans in the PIT; and the general threshold for the WT—amounting currently to 700,000 euros) to obtain the net taxable base.
 4. We apply, in the case of the PIT, the general and savings tax schedules to the taxable bases and the personal and family minimum deductions to obtain the gross tax liability (before tax credits), which we need to determine for the PIT-WT ceiling; and we apply the progressive tax schedule to the taxable wealth.
1. We verify if the WT tax liability needs to be reduced by the application of the tax ceiling.
 2. Finally, once we have the WT due at the taxpayer level, we transform it to the household level to calculate all the inequality indices.

3.3 The redistributive power of the tax

In the case of the WT, the tax due is a flow of income, while the tax base is a stock magnitude. This means effective tax rates calculated as a percentage of net wealth are low if we compare them, for example, with those of PIT. However, this is not a fair comparison because of the different nature of wealth versus that of income. In addition, as the accumulation of wealth is a process that occurs in the long term, we propose evaluating the redistributive capacity of the tax in the long term as well¹⁴. We will only analyze the current tax or alternative equal-revenue reforms; hence, the increase in the effective tax rate with respect to the current one would only be due to more compliance and better valuation of assets. Although Durán-Cabré et al. (2019a) have shown by means of an empirical analysis that in the short run there are no real responses, but avoidance, due to a higher level of taxation, we cannot disregard that enforcing compliance could provoke real responses in the medium-long run. That is why, our longer-term analysis might be considered as an upper bound, in particular, regarding the redistributive capacity of the tax. Next, we explain how we propose assessing this capacity in a longer term.

Specifically, for a given WT, we calculate the effective average tax rate to be paid in the first year. This we denominate as the “short-run” tax rate, $ATR_{s/r}$. From this, we calculate an effective long-run ATR as follows:

$$\text{Net Wealth in yeartwithout a WT (NW}_{w/o}) = \text{NW}_0 \times (1 + g)^t$$

$$\text{Net Wealth in yeartwith a WT (NW}_w) = \text{NW}_0 \times (1 + g)^t \times (1 - \text{ATR}_s/r)^t$$

NW_0 is the net wealth in the base year, which in the absence of a WT, would increase annually according to the factor, g , over t -years until $\text{NW}_{w/o}$ has been accumulated. The value of g depends on the capacity to generate annual savings, but it is also dependent on the evolution of asset values (e.g. stock indices or housing market)¹⁵. To just focus in a longer term on the impact of the tax, and acknowledging again the potential presence of general equilibrium effects in a longer perspective, we assume g is constant across the wealth distribution and over time. In the presence of a WT, given a constant ATR over time, which coincides with the effective tax rate of the base year, net wealth in the long run will diminish. Given these two scenarios (with and without WT), we can calculate the implicit long-run effective average WT rate as follows:

$$\text{ATR}_l/r = 1 - (\text{NW}_w/\text{NW}_{w/o}) = 1 - (1 - \text{ATR}_s/r)^t$$

Hence, in our simulations, we present the effective average tax rate in both the short and longer runs. To measure the capacity to collect tax revenues, we use the short run; however, for redistribution purposes, we introduce a longer-run perspective.

4. A Quantitative Assessment of the Wealth Tax under Current and Alternative Designs

4.1 The current tax

When applying the current WT rules (exemptions, threshold, national tax rates and common ceiling) to the taxpayers' wealth value at market prices (Survey of Household Finances), our results, calculated with SIMPA, show that the potential tax revenue for the base year is €3,692 M, that is, the current revenue only accounts for 44.6% of the potential one (panel A, Table 4)¹⁶. In other words, the potential revenue is approximately 2.25 greater than the actual revenue. Yet, despite these much higher revenues, the short-run effective tax rates are very low both before and after applying the tax ceiling, 0.005 and 0.0038%, respectively.

Table 4. SIMPA: inequality before and after the current tax

	Before WT	After potential WT
<i>A: Short run impact</i>		
Potential tax revenue (thousand €)	n.a.	3,691,969
		[915,485]
% (real tax revenue/potential)	n.a.	44.60%
Short run ATR (before/after tax ceiling)	n.a.	0.0050% [0.00091]/
		0.0038% [0.00075]
Short run ATR if tax due > 0 (after tax ceiling)	n.a.	0.1891% [0.0279]
% individuals with tax due > 0	n.a.	1.665%
		[1.0607]
% individuals with business exemption	n.a.	0.47255%
		[0.08277]
% individuals with first dwelling exemption	n.a.	1.6090% [1.0668]/
		1.0171 % [1.0656]: full exemption

	Before WT	After potential WT
% individuals with common ceiling	n.a.	0.2142%
		[0.0263]
<i>B: Long run impact (5 years)</i>		
Gini index	0.6294	0.6279
	[0.0102]	[0.0109]
Top 1%	19.53%	19.23%
	[2.2607]	[2.2106]
Top 10%	51.86%	51.63%
	[7.9206]	[7.9042]
Long run ATR (all/if tax due > 0)	n.a.	0.0187% [0.0037]/
		0.9264% [0.1369]
<i>C: Very long run impact (25 years)</i>		
Gini index	0.6294	0.6226
	[0.0102]	[0.0111]
Top 1%	19.53%	18.14%
	[2.2607]	[2.0365]
Top 10%	51.86%	50.79%
	[7.9206]	[7.8440]
Long run ATR (all/if tax due > 0)	n.a.	0.0890% [0.0173]/
		4.4190 % [0.6261]

Notes: n.a.: not applicable; in square brackets, we report bootstrapped standard errors; ~~we cannot calculate the bootstrapped standard errors of the ratio total revenue collected versus potential, as we do not know the real amount of revenue collected by taxpayer.~~

(*)a : In this ratio the only source of variation by unit is the potential amount of tax due per taxpayer, i.e., we do not know the real amount of revenue collected by taxpayer; thus, from the bootstrapped standard error of the variable in the denominator, we calculate the 95% confidence interval of the ratio: (0.3001 , 0.8677).

Only 1.67% of the adult population have to pay the tax. As Table 5 indicates, only individuals located at the very top of the wealth distribution are liable: that is, from the 94-percentile upwards. In fact, 92% of the total tax due should be paid by the top 1% of taxpayers. The huge disparity should also be noted within this 100% percentile, as the net wealth goes from €2 M to €524 M according to the survey data. Likewise, note that not everyone located in the top 1% of the wealth distribution becomes a taxpayer: this implies 11.69% of households would not have to pay the tax. This highly surprising result is attributable to the exemptions, which across the common ceiling PIT-WT, undoubtedly reduce the redistributive power of the WT, as the figures described below show. Close to 30% (i.e. 0.47/1.67) of taxpayers apply the business exemption and almost 97% (1.61/1.67) the first dwelling one, while the common ceiling only benefits about 13% (0.21/1.67) of taxpayers (panel A, Table 4).

Table 5. SIMPA: Potential distribution of taxpayers per household and percentile

Percentile	Average net wealth (€)	Minimum net wealth (€)	Maximum net wealth (€)	% Taxpayers within the percentile	% of total tax due
94	712,937	674,492	755,044	0.04	0.00009
95	803,292	755,063	855,800	8.81	0.00533
96	917,907	857,000	986,023	1.11	0.00692

Percentile	Average net wealth (€)	Minimum net wealth (€)	Maximum net wealth (€)	% Taxpayers within the percentile	% of total tax due
97	1,094,068	986,525	1,195,506	28.27	0.41
98	1,323,794	1,195,860	1,488,011	17.05	0.74
99	1,644,263	1,488,055	2,108,324	62.57	6.831
100	5,053,378	2,110,405	524,000,000	88.31	91.99

In Figure 2¹⁷, we show the evolution of the short-run average tax rate over net wealth, before (circle) and after (diamond) the application of the ceiling, while in Figure 3, we show the difference between these two average tax rates. In general, it is evident that the impact of the limit is regressive, as the difference in tax rates is increasing with net wealth. A good example of regressivity—clearly visible in Figure 2—is provided by a taxpayer whose net wealth is €152 M: here, the final tax rate falls from 2.43% to 0.49% when the ceiling is considered. This is as expected, given, as stressed in Section 2.1, the flow of income of the very rich does not match their level of wealth. In other words, the two magnitudes do not move monotonically. Paradoxically, this means that the tax itself tames its redistributive power. This suggests the need to define the ceiling in a different fashion, either by implicitly raising the general threshold or by changing the formula used to calculate the ceiling¹⁸. Failure to do so represents a lack of coherence with the tax’s original purpose¹⁹.

Figure 2. SIMPA: WT effective tax rate before and after the tax limit.

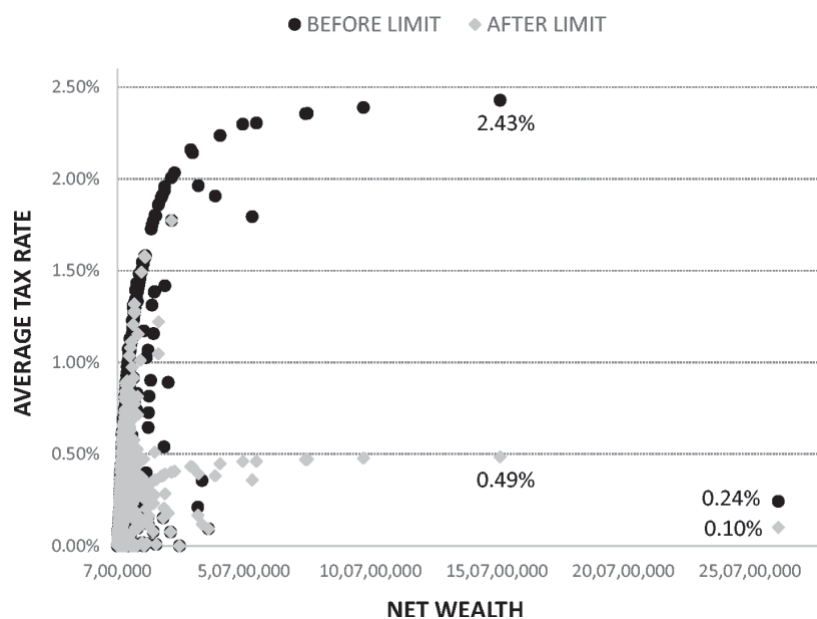


Figure 3. SIMPA: Reduction in the ATR attributable to the tax limit.

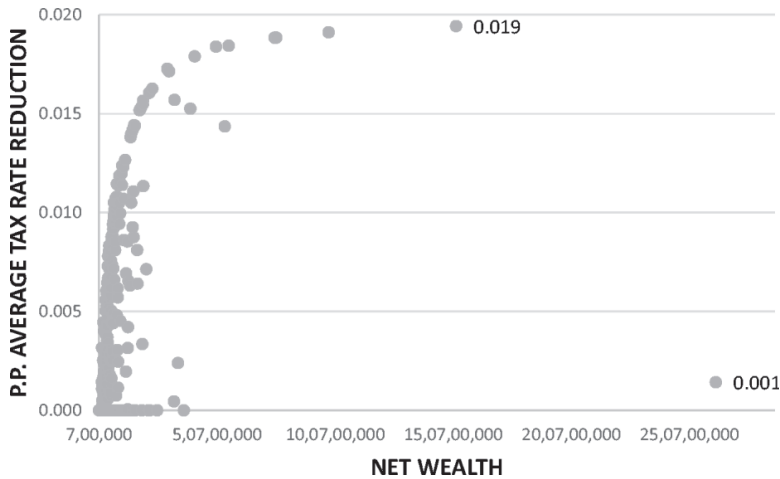
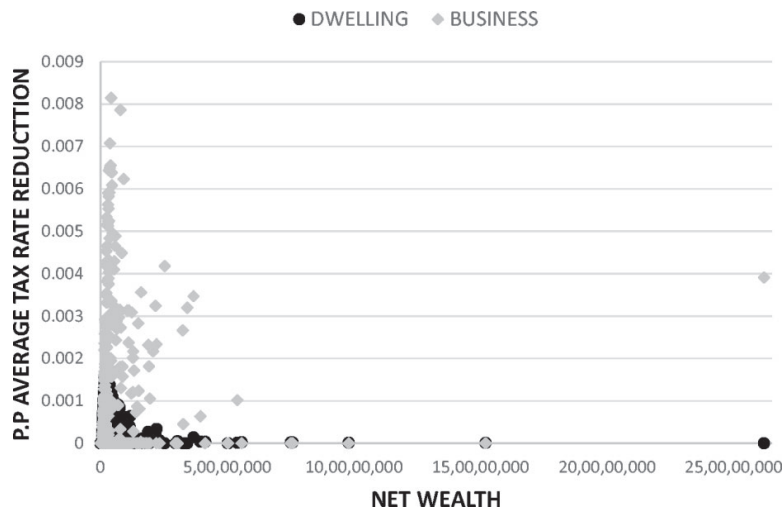


Figure 2 also highlights a further peculiarity: the average tax rates of the richest taxpayers of the survey (with €262 M of net wealth) are extremely low, both before (0.24%) and after (0.1%) the application of the ceiling. Therefore, the low short-run final rate is attributable primarily to the application of specific exemptions (first dwelling and family business) and not to the ceiling. This is what Figure 4 illustrates: average tax rates over wealth without (circle) and with (diamond) the specific exemptions, while Figure 5 shows the percentage point reductions for each exemption: first dwelling (circle) and family business (diamond). As expected, the importance of the first dwelling exemption (for which there is an absolute ceiling) is lower than that of the family business exemption (for which there is no absolute limit).

Figure 4. SIMPA: WT effective tax rate before and after the first dwelling and family business exemptions (in all cases, after the limit).



Figure 5. SIMPA: Reduction in the ATR for first dwelling and family business exemptions.



Thus, the results obtained with SIMPA suggest that both the exemptions and the common ceiling are regressive and so reduce the potential redistributive effect of the WT. This conclusion is confirmed in two additional figures that show the reduction in ATR per net wealth bracket; specifically, Figure 6 distinguishes the effect of the first dwelling and family business exemptions, while Figure 7 distinguishes the effect of both exemptions and the tax ceiling. In all figures, the scale of the vertical axis is the same across brackets, clearly illustrating where absolute reductions in the average tax rates concentrate most. If, for example, we compare the vertical axis of Figure 5 with that of Figure 3, it is evident that the percentage reductions for the specific exemptions are half those attributable to the ceiling.

Figure 6. SIMPA: Reduction of the ATR for first dwelling and family business exemptions per net wealth bracket.

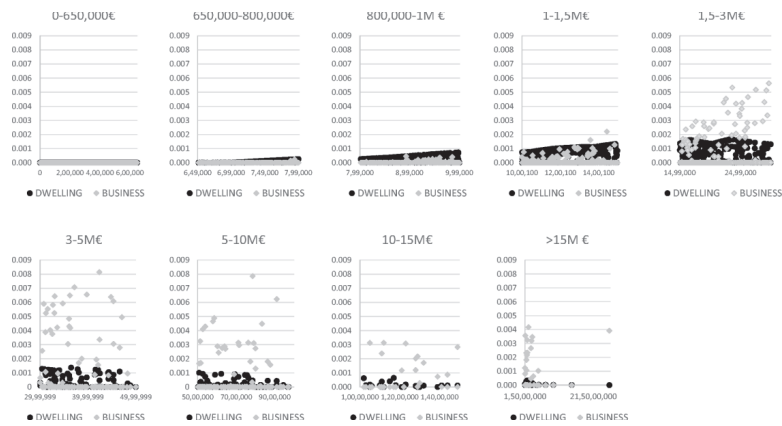
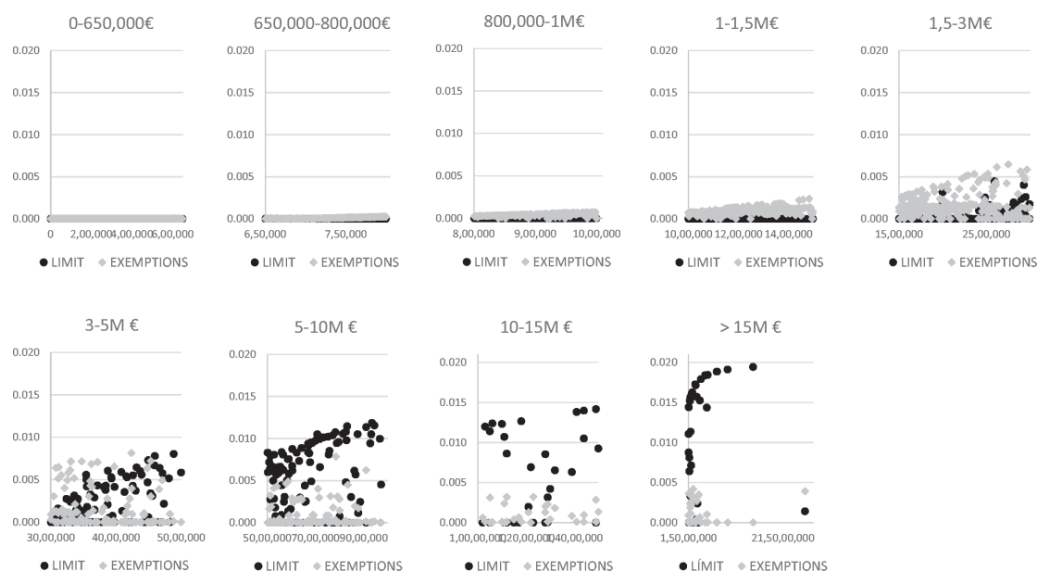


Figure 7. SIMPA: Reduction of the ATR for specific exemptions and tax limit per net wealth bracket.



In Table 6, we can observe the effect of the ceiling and the exemptions of the current tax. The highest fall in revenues is caused by the ceiling, more than €4,402 M, much more than the 715 M and 613 M of forgone revenues caused by the business and the dwelling exemptions, respectively. The top 1% ATR—who enjoys the largest percentage-point reduction in the ATR—halves thanks to the ceiling, and the impact of the business exemption is more than two-fold the impact of the dwelling exemption. In short, the exemptions and common ceiling reduce the tax’s progressivity, this reduction being most marked in the case of the ceiling, while of the two exemptions, the family business exemption is considerably more important in reducing progressivity than that of the first dwelling.

Table 6. SIMPA: The impact of exemptions and ceiling on the average tax rate and revenue

	ATR: no exemptions, no ceiling	ATR reduction due to “ceiling”	ATR reduction due to “family business” exemption	ATR reduction due to “first dwelling” exemption	ATR: current tax
Top 1%	0.597%	−0.299 pp	−0.045 pp	−0.02 pp	0.233%
Top 10%	0.245%	−0.114 pp	−0.019 pp	−0.016 pp	0.096%
Top quintile	0.186%	−0.087 pp	−0.014 pp	−0.012 pp	0.073%
Tax revenue thousand €	9,422,760	−4,402,564	−715,212	−613,015	3,691,969

There is also a notable shift in effective tax rates if we adopt a longer-run perspective (panels B and C, Table 4). The effective tax rates rise to 0.02% (0.93% for those with a positive tax due) after 5 years or to 0.09% (4.42%) after 25 years. Consequently, the redistributive effect, with all the caveats made clear before, might in fact be quite significant: ceteris paribus, the wealth concentration of the top 1% (10%) falls by 1.31 pp (0.84 pp) after 25 years.

4.2 Some alternative designs

In line with the conclusion that key elements of the current Spanish WT are regressive and undermine its redistributive effect²⁰, it is logical that we consider alternative designs that ensure the regulation is more coherent with its redistributive goal, in addition to reducing behavioural responses that might erode the tax. Our tax simulator, SIMPA, enables us to test the outcomes for a variety of reforms. In this section, we concentrate on three potential designs under the revenue equivalence assumption: that is that the total amount of revenue collected is equal to the potential amount of revenue collected under the current tax²¹. The exact nature of the three reforms is shown in Table 7. In Simulations 1 and 2, we do not consider any specific exemptions, while in Simulation 3 we consider solely the first dwelling exemption in line with its current legal configuration. Thus, based on redistributive grounds but also on the avoidance opportunities that it confers, we disregard the family business exemption in all three simulations. In Simulation 1, we do not contemplate any common PIT-WT ceiling; this, however, is included in the other two. The mar-

ginal tax rate remains constant in all cases at 1%, while the universal threshold is allowed to vary. As such, we propose a flat tax with a much higher general threshold, which introduces progressivity and, at least to a certain degree, avoids liquidity constraints, and a comprehensive tax base, which enhances the redistributive goal and reduces loopholes and behavioural responses.

Table 7. SIMPA: Alternative simulations under equal-revenue collected constraint

	Simulation 1	Simulation 2	Simulation 3
Exemptions	None	None	First dwelling
Tax ceiling	No	Yes	Yes
Threshold (€)	2,280,641	1,198,808.7	1,096,170
Tax rate	1%	1%	1%

As can be seen in Table 8, there are no great differences across the three simulations. Effective tax rates in the short run are quite low: in those with a positive tax due, it stands between just 0.002% and 0.005%. The tax would be paid by between just 0.36% and 1.34% of adult individuals. Figure 8 shows the evolution of the concentration ratio for the top 1%. Again, although there are no great differences across simulations, Simulation 1 achieves slightly greater levels of redistribution, which highlights once more the need to rethink the design of the limit. For example, after 25 years, the wealth concentration of the top 1% would be 17.95%, 18.18%, and 18.2% for Simulations 1, 2, and 3, respectively, where 19.53% is the starting point. Hence, in all cases, the reduction would be 1.33–1.58 pp. The elimination of all exemptions and the common ceiling, under the revenue neutral assumption, would slightly increase the redistributive impact of the tax, with 1% as a single marginal rate, much lower than the current top rates.

Figure 8. SIMPA: Evolution of the redistributive power of the WT over time: top 1% net wealth concentration.

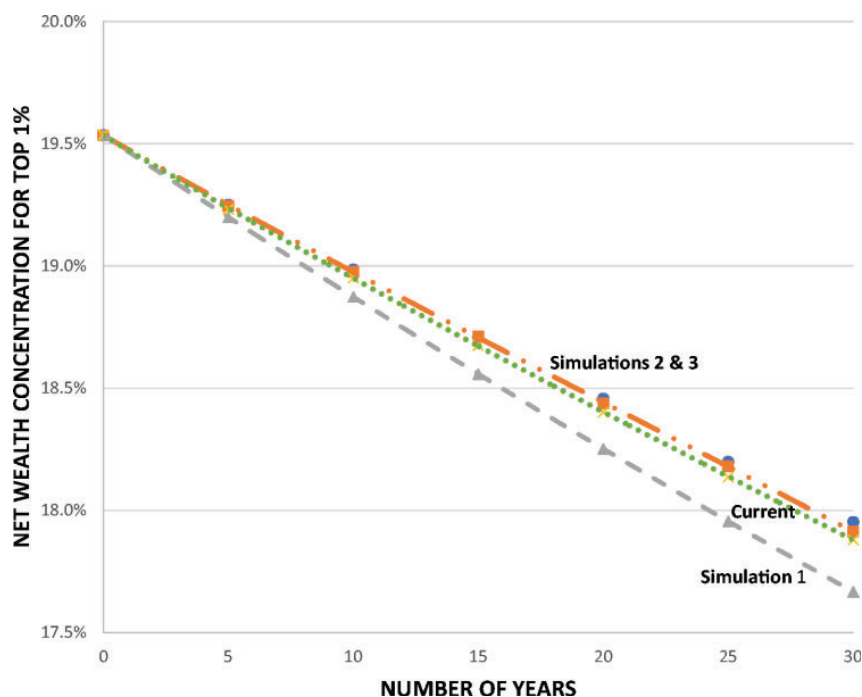


Table 8. SIMPA: Redistributive power of alternative equal-revenue simulations in the very long run (25 years)

	Potential current WT	Simulation 1	Simulation 2	Simulation 3
Gini Index	0.6226	0.6225	0.6224	0.6224

	Potential current WT	Simulation 1	Simulation 2	Simulation 3
	[0.0111]	[0.0101]	[0.0106]	[0.0100]
Top 1% wealth	18.14%	17.95%	18.18%	18.20%
	[2.0365]	[2.1072]	[2.0675]	[2.0539]
Top 10% wealth	50.79%	50.79%	50.77%	50.77%
	[7.8440]	[7.9263]	[7.7842]	[7.7282]
Short run ATR (before/ after tax ceiling)	0.0050% [0.00091]/	0.0019%[0.0004]/ 0.0019%[0.0004]	0.0054%[0.0009]/ 0.0044%[0.0008]	0.00541% [0.0010]/
	0.0038% [0.00075]			0.0045% [0.0009]
Very long run ATR (total/tax due > 0)	0.0890% [0.0173]/	0.0442%[0.0099]/	0.0851%[0.0193]/ 7.0850% [0.7040]	0.0885% [0.0220]/6.7624% [0.5890]
	4.4190 % [0.6261]	9.4833%[0.8899]		
% individuals with tax due > 0	1.6650%	0.3584%	1.1892%	1.3360%
	[1.0607]	[0.0629]	[1.0638]	[1.0653]

Note: In square brackets, we report bootstrapped standard errors.

5. Conclusions

Society is subject to constant change and nowhere is this more apparent than in the field of taxation. Technological innovations (e.g. as with respect to the valuation of assets) and advances in information sharing—specially at the international level—could well open the door to a ‘modern wealth tax’, which would be good news if wealth inequality continues to record such high levels and to pose a potential threat to social cohesion. However, as WT design has still to overcome a number of challenges, in this article, taking advantage of the Spanish experience, we have undertaken a quantitative analysis of various key legal elements of this tax (specifically, exemptions and the tax ceiling) and we have also analyzed its redistributive power. To do so, we have designed a tax simulator (the SIMPA).

In its current design, our simulator suggests that the reality of the Spanish tax is far from the potential one. For example, the weight of the WT over GDP should be 0.46%, that is 2.6 times its current weight. This discrepancy, we argue herein, is due to the existence of both tax avoidance and evasion as well as to the fiscal assessment criteria employed, which do not necessarily coincide with market values.

To address the sources of this discrepancy, the tax administration needs to take advantage of developing technologies to improve its valuation methods, while at the same time investing greater efforts in the fight against tax avoidance. In this latter instance, what is needed, as various authors have already stressed, is the elimination of existing loopholes. In this article, we have specifically illustrated the regressive effects of the ‘family business’ exemption, but also those of the common PIT-WT ceiling. While some kind of ceiling has to be left in place—to avoid the confiscatory tax system prohibited under the Spanish Constitution—its design needs to be rethought to avoid regressivity and its use as an avoidance tool (Durán-Cabré et al. 2019a). If these sources of discrepancy were to be rectified, the redistributive effect of the tax might increase notably, particularly when a longer-run perspective is adopted.

In short, the time is ripe to give serious consideration to the role a wealth tax might play in the tax system. While the current setting seems to welcome a ‘new paradigm’, recent experiences, such as that documented here for Spain, point to the fact that any flaws in its design can seriously undermine its redistributive role. If these flaws are not addressed, the tax will fail to achieve its basic goal: namely that of complementing the PIT by taxing the contributive capacity of the very wealthy. The Spanish experience might be useful to other countries currently discussing about the introduction of this tax.

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1. Although we cannot know the impact of COVID-19 yet, a recent poll among outstanding economists found that the vast majority are concerned that COVID-19 will raise inequality (IGM 2020). Landais et al. (2020) propose a European progressive net WT to finance the extraordinary deficits the pandemic is generating.

2. Note this is not necessarily the case for the USA, as the personal tax system is not based on the residence principle, but on nationality.

3. https://www.bde.es/bde/en/areas/estadis/estadisticas-por/encuestas-hogar/relacionados/Encuesta_Financi/

4. It might be tempting to conclude that the difference in the two tax gaps (i.e. 55.4–44.3%) is attributable to the assessment criteria employed, which indeed have been shown to be quite important: in order to obtain market values, Agrawal et al. (2020) and Durán-Cabré and Esteller-Moré (2010) use a correction factor for real estates that ranges between 2.5 and 3. However, although Kopczuk (2015, p. 50) claims that survey data may not be affected by evasion, we cannot be sure, particularly with regard to offshore accounts. Thus, our results could be considered as a lower bound of the real potentiality of the tax.

5. While Saez and Zucman (2019b) have discussed in detail some of these shortcomings, including references for the Spanish case, here we offer precise quantifications of their impact.

6. For example, in 1974, a Labour Government came to power in the United Kingdom committed to introducing a WT. The idea, however, was criticized by scholars otherwise sympathetic to some kind of redistribution of wealth, including Atkinson and Sandford, because the administrative costs and the difficulty of assessing wealth annually for tax purposes made it impractical (Glennester2012).

7. In 1995, the German Constitutional Court declared the WT unconstitutional, because the law gave unequal treatment to different types of wealth: some assets were valued according to their market value; others were assessed using values that were well removed from their market price. For example, real property valuations dated from 1964 (Wendt1997).

8. For instance, in the French annual WT, eliminated in 2018, the tax base did not include certain financial assets and some business assets. In fact, the base represented just half of the wealth held by WT taxpayers (Boadway and Pestieau 2018).

9. This is in line with Glogower’s (2016) proposal for taxing capital as an alternative to the realization rule.

10. When rates of returns on capital across individuals differ, wealth taxation and capital income taxation are not equivalent and have different implications for both efficiency and equity. Guvenen et al. (2019) show that a WT leads to a more efficient allocation of capital than a capital income tax, as entrepreneurs that are more productive pay similar taxes regardless of their productivity, which shifts the tax burden toward unproductive entrepreneurs.

11. Alternatives are available, including the capitalization of capital income from the PIT returns or the inheritance multiplier. However, they both have their drawbacks. In the case of the former, too many assumptions are made (e.g. profitability is assumed to be the same across the income distribution, while unrealized capital gains cannot be capitalized), while the latter is simply not available for all the ACs as the inheritance and gift tax is decentralized. Another alternative would be to use data from the WT records provided by the Spanish Tax Agency, but then wealth would be under-valued, evasion could not be considered and there would be a lack of data for the region of Madrid, where most taxpayers do not have to fill in the WT return and the foral regions (Navarre and the Basque Country). In addition, as Table 3 shows and we said before, the overrepresentation of wealthy households is particularly useful regarding the WT. According to the comparative analysis carried out by Martínez-Toledano (2017), the Survey of Household Finances is extremely useful for analysing inequality dynamics at the top (p. 28).

12. As we want to calculate its potentiality for Spain as a whole, we apply to all regions the state legislation, that is, the legislation that would apply in absence of legal adjustments by the regions. This should be interpreted as the role the tax could play if it were harmonized all over the country, and so the negative effects of mobility within the national territory would be overcome.

13. This assumption matches well with the most common matrimonial property regime in Spain, the community of property.

14. We are well aware of the potential existence of general equilibrium effects in the long run, but still believe it is also illustrative to show the potential redistribution impact adopting a longer time span.
15. For the USA, according to available empirical evidence, the increase in wealth accumulation at the top has been driven by a rise in asset prices rather than by capital accumulation (Saez and Zucman 2019b).
16. As Madrid has a 100% tax credit, in order to make a homogenous comparison, we add the money it would have collected had the AC applied the WT to the real revenue raised by the other ACs. We take the actual revenue raised by Madrid in 2007, the last year the WT was applied before its transitional abolition between 2008 and 2010 and assume it would have evolved in line with the revenue collected in Catalonia up to 2014. The two are Spain's richest regions.
17. In the figures, each dot is a survey response. In SIMPA, each response is elevated to the factor provided by the survey for transforming individual data into the national aggregate.
18. This negative assessment of the ceiling does not take into account the fact that it creates margins of avoidance response (by redesigning the wealth portfolio not to take into consideration general annual flows of income, but rather capital gains) as shown by Durán-Cabré et al. (2019a).
19. In the Spanish case recall that the Constitution, Art. 31.1, holds that the tax system should be progressive but without becoming confiscatory. Although the Constitutional Court in Spain has not ruled on the practical consequences of this non-confiscatory principle, the suggestion is that some kind of joint limit between PIT and WT needs to be considered.
20. Furthermore, although not specifically examined here, there is fairly strong evidence that these elements enhance the avoidance responses that effectively erode the tax (Alvaredo and Saez 2009; Durán-Cabré et al. 2019).
21. The results of other reforms are shown in Durán-Cabré and Esteller-Moré (2019a).

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