MARCH 2020
TAX REFORM

A European Tax for a new Europe

Thomas Piketty elaborates his ideas for a new Europe in his new book Capital and Ideology. The Treaty of Europe needs to be renewed and four new European taxes are introduced, in addition to national taxes. It is daring, innovative, but it does not appeal to the imagination. An alternative.

HET MENSELIJK VERMOGEN

Why the European Taxes of Thomas Piketty will fail !

The alternative: A Progressive Tax on growth of wealth

Innovative and Effective

Easy to Implement

Restores Solidarity and social cohesion

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Guide into the March 2020 Issue

The first issue of "The human capacity" - magazine for imagination - delves into the new book by Thomas Piketty "Capital and ideology" that was published in Dutch this month. In the last chapter, the writer gives a political outline of the innovations needed to reduce inequality in Europe. The contours of this sketch are further elaborated in a manifesto co-written by Thomas Piketty and published on the website www.tdem.eu. More than 100,000 people have now expressed their support by signing the manifesto. It is unclear whether this manifesto will also be continued in the form of a new social movement or a political party.

The manifesto consists of two parts: a new treaty of Europe and a new budget and taxes for Europe. The new treaty states that the participating countries of Europe, not necessarily all EU Member States, will form a new European Assembly, alongside the European Parliament, which will include national parliamentarians. The meeting will receive a new budget obtained from 4 new European taxes that are additional to the national tax systems. Spending the budget is aimed at reducing inequalities in Europe, in particular stimulating education. The four new taxes are a progressive income tax and a progressive wealth tax for individuals and a CO2 tax for companies and an additional tax for large companies. The ideas are daring, innovative and stimulating, but they also seem to be inspired to dovetail well with the reality of European practice. Partly because of this, they lack the power of imagination. And partly because of this, they also carry the seed for failure. More is needed to truly renew Europe. A vision that goes deeper into the structures of our societies; that give new hope and inspiration. In the coming numbers I will "amend" his ideas. The first amendment "the tax on growth of wealth" will be the subject of this first issue.

Johannes WH Janssen

AMENDMENT ON TDEM'S 'A BUDGET FOR EUROPE'

Preface

Piketty and others wrote in 2018 on www.tdem.eu a manifest to transform the EU. It contains two key items: a new Treaty between European states called 'Treaty on the democratization of the economic and social government of the Union' (TDEM), and a 'budget for Europe' that will be spent by this new Assembly. The 'budget for Europe', consists, according to the manifest out of 4 taxes: a tax on the profits of large companies, a progressive income tax, a progressive wealth tax and a CO2 tax. These taxes already exist in individual Member States of Europe. It makes sense to "copy" them to an European scale. But the problem is, these taxes are no longer suitable for the 21st century. They have some major flaws. It would be sensible for a new Assembly to design new taxes, which on the one hand should improve relations between European citizens, government and the economy, on the other should hand give Europe its own identity and strengthens the debate within a European political space. In this (first) amendment, I propose to merge tax on income and wealth (the total value of property of a person) into one new type of tax: a tax on growth of wealth[1] that can effectively fight inequality.

Criticism

National states have three taxes for individuals to direct redistribution of income and wealth and to finance a part of the public tasks: a (progressive) income tax, wealth tax and inheritance tax. The income tax is aimed at the current cash flow of a private person that can fluctuate widely, the tax on wealth, is aimed at the wealth accumulated during life. The inheritance tax is taxed on the transfer of that wealth to a next generation.

All three are due for replacement. They no longer function in the 21st century. Income tax puts a heavy burden on the labor-factor of production. Because capital and nature, the other two factors of production, were hardly taxed for centuries (read: "free"), our productivity has grown strongly, but at the expense of labor and nature. We are now

[1] In my second amendment, I will introduce a new type of tax for companies, which will replace the tax for large companies and the CO2 tax. It also ensures a firm basic income. In my third amendment I will propose an alternative Assembly based on a new concept of state: liquid states which are states of different scale each with their own citizens that penetrate each other. In my fourth amendment I will design a liquid democracy that combines direct and representative democracy.

standing at a turning point. We have reached a point where greater productivity threatens humans (makes them unhealthy and unemployed) and destroys Earth. In order to survive, we will have to transform the economy into a circular economy. As a consequence, the three production factors will have to be taxed differently. The present income tax is a blockade. It destroys labor by preferring capital over labor, burdens the labor relationship with an unprecedented bureaucracy and blocks the transition from material to immaterial ‘consumption’ such as education, care, art and culture, politics and democracy. Costs of labor in these sectors have increased enormously because these sectors cannot (easily) adjust to the productivity demands of capitalism.

Wealth tax on wealth is avoided due to the concerns of capital flight. Many fear that taxing wealth will affect technological innovation. They fear capital will look for other ways that yield more returns. In other words, it is an "open-ended" tax and is therefore completely unsuitable for promoting a stable society and social cohesion.

Finally, the inheritance tax has a very bad name. It is considered unjust because the state is taking part of someone’s accumulated wealth. The tax has received this bad name because, more than with the wealth tax (which mainly affects the really rich), it also affects small wealth. The tax also penetrates into close family ties and sensitive matters such as the selection of heirs. Finally, perhaps the biggest problem, the tax clashes hard with the keynote of our capitalist society: we all want to get rich.

It is noteworthy that hardly anyone in the world is surprised by the existence of millionaires, multi-millionaires and billionaires. It seems to be a fact of life. Lotteries that let people become a millionaire in one fell swoop, underline this fact. If we want to tackle inequality seriously, we will have to address the question if these forms of wealth are desirable. The central, usually hidden motive of our actions "getting rich" must be counterbalanced. We will have to frame "property" and "wealth" differently!

That is not easy. For example, in his new book ‘Capital and Ideology’ Piketty proposes to circulate property by giving all 25-year-olds a starting capital of 125,000 euros. This proposal sends a completely wrong signal to society. By giving unrestricted capital to young people, the idea that property is desirable is strongly propagated. Everyone can and will get rich and if can be done in your lifetime. It strengthens egoism in society and dismantles a sense of community.

The new tax system that I propose does not focus on actively circulating income and wealth, but on creating a **bounded space** within which income and wealth can move freely. The system is simple, transparent and feasible. Every citizen "gets it". You don't need a tax advisor.

Amendment: a Progressive Tax on Growth of Wealth

We have to maximize the accumulation of personal wealth. I propose a European Progressive Tax on Growth of Wealth for individuals. This tax can replace both tax on income and tax on estates (like property and financial assets). The tax is levied on the *growth* of your wealth. A persons individual wealth is the sum of the (book) value of all personal estates within Europe, movable and immovable, like houses, boats, cars, jewelry, paintings and all financial assets, shares, savings accounts, etc. etc. with a value greater than 5000 €. Debts are deducted. The growth of wealth is the difference of wealth between moment A and moment A + 1 year. The tax *rate* depends on the current wealth, not on the growth of wealth.

This is an example of what a Progressive Tax on Growth of Wealth could look like:

- a 0% tax-rate for all changes in the total value of your estates below € 100.000,-
- If the value of your possessions increases in a calendar year, to an amount between € 100.000,- and € 200.000,- then 1% tax must be paid on the excess above € 100.000,-.
- If your personal wealth rises the next calendar year again, but remains within the graduated scale (between € 100.000, - and € 200.000,-), 1% tax must be paid on the growth within the graduated scale.
- If the wealth rises in the next calendar year to an amount between € 200.000,- and € 300.000,-, 1% tax must be paid on growth up to € 200.000,- and 2% tax must be paid on the excess above € 200.000,-.
- Etc. Etc.
- The highest tier has a rate of 95%. If the property exceeds 9.5 million euro (M€), a 95% tax must be paid on the capital growth in a calendar year
- If the induvial capital remains the same or descends, *no* tax needs to be paid.
- An inheritance is growth of wealth for the heir and falls under this progressive Tax on Growth of Wealth.
- *Only* assets located within Europe are taken into account for the calculation of private wealth.

Explanation

The tax on growth of wealth is therefore levied on the positive fluctuations of capital. It has a crucial effect. The tax-load dampens these fluctuations. Large fluctuations in the value of assets will disappear because they can have immediately major tax consequences. The explosive housing market, but also the stock market or the foreign exchange market will become "calmer". I will explain this further in the examples below.

Tax on growth of wealth expresses a new form of justice. She acknowledges that wealth is possible and allowed. But she also says: 10 million is enough for an individual. That amount is more than enough to lead a carefree life as a private individual. If the maximum wealth has a upper bound, then the human motive will gradually shifts from 'obtaining individual wealth' to the question how to act socially: 'what will I do for society when I have reached my maximum?' A new frame of "social interest" is emerging that is a solid core for a society and that brings much needed social cohesion back into society.

The tax on growth of wealth is therefore aimed at *maximizing* wealth, not at circulation of wealth. That maximum does not affect the existing capital of rich people. Billionaires and multi-millionaires keep their wealth during their life-time. And they don't have to pay taxes if their assets don't grow. But if it does grow, the largest part (95%) of the growth will come to the (European) state through a tax assessment.

A progressive tax on growth of wealth is not a capital gains tax or a capital return tax. With a capital gains tax, not the capital, but the growth of capital is divided into progressive tiers. Return tax is based on a notional return on capital (e.g. 4%) on which tax must be paid. In our case, the tax on growth of wealth, is based on the real value of the property which is measured as accurately as possible.

How do we calculate a private individual's capital for tax on growth of wealth? All European assets, movable and immovable assets, houses, boats, cars, jewelry, paintings with a value greater than 5000 € and all financial assets, shares, savings accounts, etc. are added at their current book value. Debts are deducted.

The tax on growth of wealth is settled annually. The simplest calculation is of growth of wealth is the difference of the total wealth within Europe on January 1 of year X + 1 minus the total wealth on January 1 of year X. If the difference is positive, we call that growth of wealth and tax is due. In reality, the calculation is much more complex, because within a year large fluctuations in wealth can be included into the calculation (see example 6).

Tax on Growth of Wealth is an *implicit* progressive income tax. Income that is added to the private capital is taxed as growth of wealth. If a person has a large wealth, the income that is added to the wealth will also be subject to a higher tax-rate (up to a maximum of 95%). So it makes no sense for the wealthy to have high salaries, because they have to give it to the tax authorities for the most part. High salaries will not be taxed if the income is *spent* on non-capital consumption and labor services, such as the gardener, the tax advisor or a donation to charity. The optimal wage requirement is a salary that is just enough to cover the costs of living.

Only assets within the borders of Europe are counted. Capital flight is therefore taken into account. Suppose a private individual has shares of a European company that doubles in value, the private individual is entitled to sell half of his shares and put the money in a savings account on the Bahamas. His wealth within Europe has not increased and he does not have to pay tax. There is of course a "catch" to this. The money on the Bahamas can never be used again in Europe, for example to buy a house, because at that moment the wealth increases within the European borders and therefore a tax has to be paid.

Incorporating a territorial boundary for wealth calculation is *essential*. With it, we transform capital flight into a form of international development aid. Because the capital will not flow back to Europe, it will play a role outside Europe in building the economy. In short, tax avoidance is being transformed into a policy tool to organize an effective redistribution of wealth around the world.

Moreover, I do not expect that tax on growth of wealth will cause a large capital flight. This tax system[2] will create a very stable European society. Stability and justice are strong attractors of capital. Capital will flow in!

Finally, this tax on growth of wealth is easy to implement. We don't need fraud departments or investigative officers. All necessary registrations for the tax on growth of wealth are present in Europe. Banks are already required to report large money transactions. All it takes is an European tax office that connects the data flows. A process that is already in full swing.

Examples

I would like to conclude with a number of calculation examples that illustrate the operation of the tax on growth of wealth:

Example 1. A multimillionaire has 200 M€ of capital consisting of 1000 houses with a value of 200 K€ per house. His income consists of rental income: 1000 x 10 K€ = 10 M€ per year. After deduction of the cost of living and maintenance of the houses, 4 M€ remains. This is added to his wealth in Europe i.e. 3.8 M€ tax (95%) must be paid. So there is 200 K€ left. His net return on his assets is 2% before tax (rather modest for a capitalist!), and only 0.1% after tax. The higher the individual wealth, the lower the return.

Example 2. A multimillionaire has 200 M€ of capital consisting of 1000 houses with a value of 200 K€ per house. His houses increase in value by 10% in 1 year. His new assets are 220 M€. He therefore has to pay 19 M€ in tax on growth of wealth. That is

[2] Together with the innovative tools of my second amendment: profile tax, basic income, labor rights.

almost twice as much as the total rental income from his houses. The multi-millionaire will have to sell 10 houses to pay the tax. Because all multimillionaires with houses must sell houses, it will affect the market counter wise. It will have a depressing effect on growth of value. In other words, the capital gains tax has a negative feedback on the increase in value and leads to a redistribution of capital goods over more people. Fluctuations in the asset markets are strongly dampened.

Example 3. A multimillionaire has 200 M€ of capital consisting of 1000 houses with a value of 200 K€ per house. His houses decrease in value by 10% in 1 year. His new wealth at the end of the calendar year is 180 M€. He can now add the profit from rent (4 M€) to his own capital without paying taxes. The capital becomes 184 M€. Millionaires will not receive big tax bills if they keep their assets from growing.

Example 4. A multimillionaire has 200 M€ of capital consisting of 1000 houses of 200 K€ value per house and still has 100 M€ in a South American bank account. His houses decrease in value by 10% in 1 year. The value of his assets at the end of the calendar year is 180 M€. He decides to "import" 20 M€ to Europe and therefore buys new homes. He does not have to pay taxes because his wealth does not increase, but his action has negative feedback on the housing market. The price of housing will change due to its action. So it is possible that the decline will turn into an increase next year. Again fluctuations in the asset markets are strongly dampened.

Example 5. A multimillionaire has 200 M€ of capital consisting of 1000 houses with a value of 200 K€ per house. He has 1 son and heir. He realizes that if he dies his son inherits 200 M€ and that the tax authorities impose an assessment of approximately 185 M€ on his son. His real estate empire has to be sold to pay the bill. He tries to servive his empire by making a will. His capital will revert to a company with shareholders. His son becomes director of the company. He receives a share worth 10 M€. The tenants are offered to also become shareholders in the company. Through these shares, they thus become part owners of their own homes. A tax on growth of wealth will ultimately lead to effective redistribution of large assets. Individual wealth will be converted into companies and corporations.

Example 6. A millionaire has a capital of 5 M€. He still has 600 K€ in an account on the Bahamas that do not count in the wealth calculation for his tax on growth of wealth bill. He buys a 300 K€ boat with the Bahamas-money and sails into European waters with his boat. When mooring in a European port, it is established that the boat is not registered as an asset. Immediately the value of that boat is added to his European wealth total. After six months, the millionaire sails out of European waters and his wealth in Europe drops. Effectively, his assets increased by 1.5 tons over the entire calendar year. His tax assessment amounts to 50% * 100 K€ + 51% * 50 K€. A relatively expensive boat trip. Registration of all assets and European exchange of asset data is required.

Example 7. The same millionaire decides to pay the tax bill with the remaining 300 K€ Bahama money. Unfortunately, he forgot that as soon as he transfers the money from a non-European account to European accounts, it is a growth in wealth for the tax authorities. It will be included in de wealth tax calculations of the following year.

Example 8. Two friends have started a startup. The payment app they have developed becomes a great success. The value of their shares is rising very fast. To prevent sky-high tax bills (which can only be paid with loans, because their company is not yet profitable!), they decide to "dilute" their shares every year. Employees and users of the app can get a share in the company for free. With a capital growth tax, no European "Zuckerbergs" can arise. But a new type of cooperative companies with many enthusiastic shareholders involved in the company will arise.

Example 9. A project developer markets a luxurious home with land worth € 12 million. The question is, who will be able to buy this in the future of Europe if the maximum wealth of a private individual is limited to 10 M€? No one! The company therefore decides to rent out the wealth and to distinguish itself with an extensive range of services as added value. It provides employment growth. This will be the new trend. Having private wealth and ownership becomes unattractive. On the other hand, usage and repurposing of communal assets will increase strongly. It will be a strong incentive for our circular economy.

Example 10. A private individual has a painting of van Gogh in his living room that is valued at 20 M€ (his purchase amount). If he sells the painting he expects it will yield 3 times as much. He wants to sell the painting in order to move into a new, more expensive house. However, due to capital growth tax, 95% of his "profit" will go to the tax authorities. He comes up with a plan. It sells his painting to a museum for 20 M€. The museum also lends him another 10 M€ on favorable terms with which he can carry out his housing plans. (A loan = debt and is deducted from the assets). He does not have to pay taxes and can gradually pay off his debt if his other assets decrease in value. Cultural wealth becomes community wealth.

Example 11. The members of the royal house are multi-millionaires. Their wealth, palaces, castles and grounds have an important symbolic value. To avoid the loss of these assets due to fluctuations in market values, the assets are nationalized and members of the royal house receive a fixed amount for the stay in these buildings and for their representative duties.

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