6. Wealth and inheritance taxation: theory and evidence from the Nordic countries

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The taxation of wealth and inheritance has attracted much attention among academics and policymakers alike. In this chapter, we offer a brief overview of the theoretical and empirical research on wealth and inheritance taxation, and we discuss the specific experiences of these taxes in the Nordic countries. This chapter should be of particular interest to policymakers and practitioners in the Netherlands, which is a small open economy sharing many political, economic and institutional features with the Nordic countries.

Our discussion begins with a theoretical overview that addresses the main arguments in favour of and against taxes on wealth and inheritance. We then document the use of wealth and inheritance taxes in advanced economies, focusing particularly on the main features of these taxes in the Nordic countries. We also discuss the effects on wealth accumulation, tax avoidance and inequality, and we highlight political-economy considerations. Although research on these issues is limited, the particular experiences of wealth and inheritance taxation in the Nordic countries have received quite some academic attention, partly because of data availability, but also because these countries represent expansive welfare states with high ambitions regarding economic equality.

Based on our review, we reach the following conclusions:

- The theoretical case for a wealth tax is weak if – a big if – capital income is taxed fully. Moreover, international capital mobility has limited the feasibility of taxing the very wealthy, which in turn has weakened the case for taxing the less wealthy.
- Net wealth taxes have largely disappeared from OECD countries. However, estate and inheritance taxes are still employed in several countries, perhaps because inheritances are considered 'windfalls'.
- Both net wealth and estate and inheritance taxes face political and economic difficulties in taxing small and family businesses.

6.1 Wealth taxation

A wealth tax commonly refers to as a tax on the stock of net household wealth.[1] The exact definition of the wealth tax base varies across jurisdictions and over time, but in principle it includes all kinds of real estate property (housing, holiday homes, land, etc.), financial assets in bank deposits, fixed-interest securities and corporate shares, listed and closely held, and sometimes also valuables such as cars, boats, antiquities, art, etc., everything net of debt. Because most countries also tax income from property and capital, the wealth tax tends to become a form of 'surtax' on property and financial assets.

From a technical point of view, a wealth tax can be understood as a tax on the (common) normal return on all assets. When combined with a tax on capital income that also taxes the normal return, the wealth tax effectively becomes a 'double tax' on the normal return to capital and this

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[1] An exception is Luxembourg that has a net wealth tax on corporations.

is not what many believe to be a proper tax system. Instead, one would typically like to have a higher tax on above-normal returns. The main reason is that many scholars view excess returns as reflecting economic rents with weak connection to individual effort. There are, of course, counter-arguments to this view. Guvenen et al. (2019) argue that additional taxation of excess returns (beyond that which is levied on the normal rate of return) is inefficient if this extra taxation disproportionally falls upon high-skill investors (who are more likely to achieve above-average returns).[2] Norway taxes above-normal returns through their so-called shareholder model where dividends and capital gains corresponding to a normal rate of return are exempt from tax, and any excess returns are fully taxed according to the personal tax rate on capital income (see Södersten, 2020, for a recent discussion).

If the government could tax all sources of income that accrue to individuals, a wealth tax would not be needed. Hence, the main argument in favour of wealth taxation derives from situations where the government (for different reasons) cannot properly tax capital income. This can be because the returns on many assets are deliberately not taxed (e.g. housing wealth) and, when they are taxed, there are problems to do so properly. Especially in the case of capital gains, it can be difficult to levy capital income taxes at desired rates due to lock-in effects. If capital gains cannot be properly taxed, then a wealth tax is perhaps the only way to target the wealth holdings of the wealthiest. In short, the main role of the wealth tax is to serve as an instrument to correct for the incompleteness of the tax code when it comes to taxing capital income.

Some distinct arguments in favour of wealth taxation have been proposed. First, people can derive utility from holding wealth itself, for example, due to the power and influence it can convey (see Saez and Stantcheva, 2016). For this reason, an egalitarian wealth distribution can be desirable, motivating direct redistribution of wealth. Second, the wealth holdings of one individual can impose (negative) positional externalities on others (see, e.g., Konrad 1992; Aronsson, Ghosh and Wendner, 2020), which implies that wealth should be taxed to counter the inefficient accumulation of wealth for positional reasons. Third, a wealth tax with a large basic exemption is a way to tax the wealth holdings of the wealthiest, as argued by Saez and Zucman (2019) in their recent proposal for a wealth tax in the United States.

6.1.1 Defining an appropriate wealth tax base

One of the main challenges when implementing wealth taxation concerns the definition of an appropriate wealth tax base. Although the wealth tax, in principle, should be a broad-based tax that covers all assets, this has turned out to be difficult to achieve in the real world.

In the case of non-financial assets, some are relatively easily observed, such as dwellings, urban and agricultural land and forest, and this is also the reason why historically taxes in the pre-industrial era often were defined in terms of asset ownership rather than income streams. However, the valuation of these non-financial assets has not always been simple. Many times, thin markets make it difficult to assess market values, as there is no proper trading and pricing that can inform tax collectors about the proper value. Furthermore, there are also more conceptual valuation problems, as in the case of agricultural land and forests.[3]

In the case of financial assets, some of them are relatively straightforward to include in the wealth tax base, such as bank deposits, fixed-interest securities and listed corporate shares. These assets are also generally denominated in market values, which makes them easy to assess for taxation.

[2] However, this alludes to the existence of a market failure, which could be addressed directly through other instruments (see Gerritsen et al., 2020, for a discussion).

[3] These properties are well defined in terms of size and location, but their value is also a function of how much the soil yields. For example, the value of forest land reflects both the current mass of timber tracts and their future growth.

However, there are specific forms of financial assets that give rise to considerable problems for tax administrators: business assets and pension wealth. We will deal with these below.

Finally, the wealth tax base sometimes includes valuable consumer durables such as cars, boats and antiquities, as well as precious metals, jewellery and fine arts. All these items have sizeable influence on the actual wealth position of individuals, but are difficult to observe and tax appropriately. Thus, for practical reasons, both durables and valuables are usually exempted from wealth taxation.

6.1.2 The taxation of business equity

Arguably, the biggest concern with the wealth tax is the taxation of business assets (corporate equity). Business assets represent a complex mix of non-financial and financial assets, and to determine their correct market values is, many times, extremely difficult as the vast majority of firms are not listed on any stock exchange. A large error margin can have serious real consequences when translated into a tax levy. For this reason, most countries implemented large discounts, in some cases total tax exemptions, on the value of business assets when determining the wealth tax base. For households, similar problems arise.

A wealth tax on the stock of capital is equivalent, at least in principle, to a tax on an imputed capital income flow. This gives rise to specific problems in the case of businesses. When a firm has no cash flow, or maybe even a negative cash flow (if it is suffering losses), then the tax can cause liquidity problems. This may lead to difficulties in the financing of new investments because retained earnings are the largest single source of firms' funding. In some cases, the owner may even need to sell shares in the company to pay the tax, which could trigger additional capital gains taxes that elevate the effective tax rates. This is the double taxation on normal returns that arises when the wealth tax is imposed on top of capital income taxes (see the discussion above). In Sweden, during the 1950s, 1960s and 1970s, the combined tax effect led to effective wealth tax rates on large corporations of over 6% (Du Rietz and Henrekson, 2015). In other words, a wealth tax can cause both corporate finance and corporate governance problems for firms. Because large closely held companies tend to dominate the portfolios of the wealthy, the wealth tax can generate serious problems for the share of the private business sector that relies on domestic investors for their marginal source of corporate finance.

6.1.3 The taxation of pension wealth

A specific set of challenges are associated with including certain forms of pension wealth into the wealth tax base. Private pension savings in designated accounts, life insurance arrangements and other similarly funded private income-maintenance arrangements are equivalent to normal savings and therefore not difficult to include in the wealth tax base. However, collective pension savings in defined-contribution plans administered by a third party, often an insurance company, are more problematic to include. While these assets are held in an account with the insured person's name on it, the funds cannot typically be withdrawn until retirement, after which it is paid out either all at once or sequentially. This raises the question of how wealth with such restrictions should be valued for tax purposes and how potential liquidity problems associated with such taxation should be handled.

A specific set of challenges arise in the case of unfunded pensions (defined-benefit or pay-as-you-go), where the wealth is related to a promise of future pension entitlements. Such pension assets are common in the public social security systems of many countries, but are also used extensively in the private sector as part of occupational pension plans. Because of this heterogeneity in pension assets, pension wealth has not systematically been incorporated into the wealth tax base in any country that we know of. However, pension income is usually taxed as labour income in most countries.

In sum, the challenges associated with defining and measuring the wealth tax base are substantial. The exemption of large business assets, valuable durables or pension assets from the tax base has made the wealth tax less legitimate because the principally important broad-based feature of the wealth tax is not respected in practice. Furthermore, exemptions can make wealth taxation less progressive, or even regressive, because exemptions, to a large extent, benefit households in the very top of the wealth distribution.

6.2 Experiences from wealth taxation

Wealth taxation, in the sense of a specific tax on the stock of household net worth, is not used by many countries today. In Europe, only four countries (Luxembourg, Norway, Spain and Switzerland) still have such taxes, while in the mid-1990s more than a dozen countries employed wealth taxation. There is thus a clear downwards trend in the use of wealth taxation among rich countries.

However, some countries are using variants of wealth taxation. One of these variants is to tax imputed capital income, calculated from the stock value of net assets. For example, the Netherlands has a so-called box tax system where one of the boxes (box 3) contains financial assets such as bank deposits, bonds and shares, annuities, and real estate (other than owner-occupied property). A rate of return (a presumptive return) is assumed to be earned on the net value of the assets in the box, with the rates gradually increasing in the net value of the assets in the box. The imputed capital income is then taxed at a flat rate of 30%. In contrast to the broad base in the Netherlands, Sweden levies a presumptive tax on the imputed capital income from certain financial assets (held in special savings accounts) but debt is not deducted and the same rate of return applies independently of the net value of assets.[4]

The fiscal importance of wealth taxation can be assessed in several ways. One way is to look at tax rates, which have usually been around 0.5%–1%, many times with some degree of progressiveness and always with a large basic exemption. Another way to assess the fiscal importance of wealth taxes is to examine the total amount of wealth taxes (including real estate and wealth transfer taxes) paid by individuals and to relate it to either GDP or total tax revenues. Figure 6.1 presents revenue statistics for individually paid wealth taxes in 10 OECD countries as a share of GDP since 1980. Wealth tax receipts have ranged from between 0.1% (the OECD average has been stable at just over 0.2%) to 1% of GDP, with Norway and Switzerland standing out as the countries where the wealth tax has had the greatest fiscal importance. Considering that total capital tax revenues usually are around 5% of GDP (see Bastani and Waldenström, 2020), the wealth tax has thus represented about one-twentieth of all capital tax revenues in most countries.

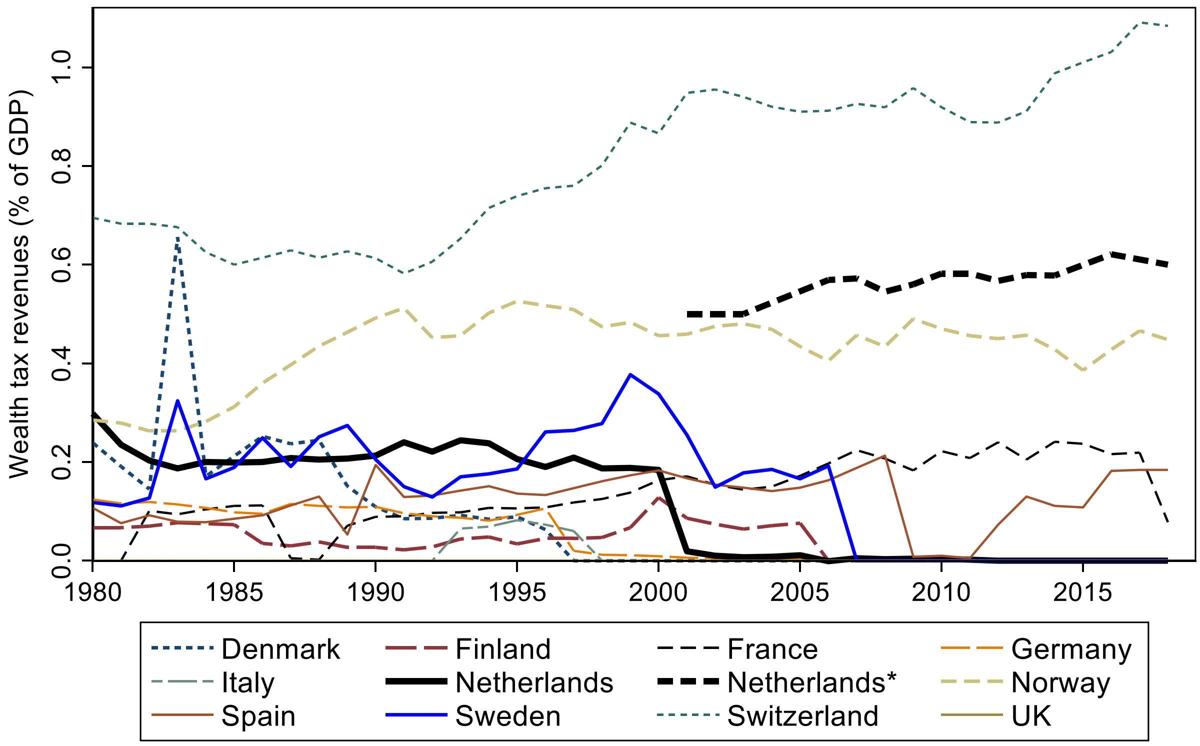
In the Nordic countries, wealth taxes have been used until the late 1990s, but today only Norway has a wealth tax. Denmark abolished its tax in 1997, Finland in 2006 and Sweden in 2007. In Norway, the tax base contains heavily discounted values of property and the basic exemption is 1.5 million Norwegian kroner, equivalent to 150,000 euros. The tax rate is flat at 0.85% of the tax-assessed value.

The reasons for abolishing the wealth tax in the Nordic countries have been widely discussed. One important reason was the increased international mobility of capital in the wake of the capital account liberalizations that swept through the Western world in the 1990s. These liberalizations made it easier for wealthy individuals to avoid the wealth tax. Another reason for

[4] The Swedish system of taxing imputed capital income has some additional details. For example, it uses different tax rates across asset types (imputed pension wealth returns are taxed at 15% whereas all other imputed capital income is taxed at a rate of 30%, which is the standard flat capital income tax rate). See Bastani and Waldenström (2020) for details.

abolishing the wealth tax in the Nordic countries was the increased political tension between different groups of wealthy households that were treated differently by the various wealth tax regimes. The increase in house prices during the 1990s and 2000s had made many homeowners liable to the tax but, at the same time, owners of family businesses, who often commanded much larger fortunes, were typically exempt from the tax altogether. With the wealth tax representing a relatively small share (0.2%–0.3%) of total tax revenues, well-organized groups lobbying against the tax eventually succeeded in eroding its political support.

Figure 6.1. Wealth tax revenue as a share of GDP in 10 OECD countries (percentage of GDP)



Notes: Series come from OECD Revenue Statistics, item 4210 ‘Individual recurrent taxes on net wealth’, except for ‘Netherlands*’, which shows revenues from the imputed return to the total of box 3 capital assets (the data were compiled by Bas Jacobs using information from Statistics Netherlands, CPB Netherlands Bureau for Economic Policy Analysis and the Ministry of Finance of the Netherlands).

6.2.1 Economic effects of wealth taxation

Few studies have analysed the effects of wealth taxation on wealth accumulation and wealth inequality. The main reason for this is a lack of detailed microdata on asset ownership in the population. Two recent studies of Nordic wealth tax data attempt to study the effects of wealth taxation on efficiency and avoidance.

Jakobsen et al. (2020) have perhaps made the most ambitious attempt so far to identify the real effects of wealth taxation by analysing behavioural responses of taxpayers. Using a rich Danish administrative data set and the gradual abolishment of the Danish wealth tax between 1989 and 1997, they find clear reduced-form effects of wealth taxes in the short and medium run, with larger effects on the very wealthy than on the moderately wealthy. Connecting these reduced-form estimates to a calibrated model, they obtain an implied long-run elasticity of taxable wealth with respect to the after-tax rate of return of 0.77 for the moderately wealthy and 1.15 for the very wealthy. The order of magnitude of the estimated effects indicates fairly notable efficiency costs of the wealth tax. The estimates should, however, be interpreted with some caution because the estimates capture the effect of wealth taxes on those who are already wealthy, omit migration responses related to wealth tax, and do not capture general equilibrium effects on asset prices and wage rates.[5]

Seim (2017) analyses the elasticity of taxable wealth in Sweden, also using administrative data, but instead employing an empirical approach focusing on measuring the bunching of taxpayers around kink points in the wealth tax schedule. He studies a shorter time period and a more restrictive set of assets, but finds that wealth taxation in Sweden did not spur any large behavioural responses in terms of bunching at kink points. The responses that were observed could mainly be attributed to reporting issues and avoidance behaviour, and not to real accumulation effects.

A recurrent question when it comes to the abolishment of the Swedish wealth tax in 2006 is whether the abolishment had any effect on wealth inequality. Unfortunately, answering this question is hindered by two circumstances. The first is that most of individual wealth data ceased to be collected after the tax repeal. The second is the almost simultaneous occurrence of the financial crisis of 2008–2009. Lundberg and Waldenström (2018) used capital income tax data and property holdings from tax assessments to estimate Swedish wealth inequality before and after the repeal of the Swedish wealth tax. Their main finding is that wealth gaps increased during the end of the 2000s, with one potential explanation being that the tax repeal was capitalized into asset values, benefitting wealthier households.[6] Asset decomposition analyses also show that the poor seemed to empty their bank holdings during the crisis years, which caused widening gaps in financial assets.[7]

Tax-driven capital flight to offshore tax havens has been another, lively debated, aspect of Sweden's wealth taxation. The discussion has concerned both its order of magnitude and the distributional profile of hidden offshore wealth. Recent scholarly efforts have shed some light on both of these questions, but it is fair to say that a lot of uncertainty remains. Roine and Waldenström (2009) used two complementary macro-statistical models, one based on calculating the gap in financial savings between national and financial accounts and the other based on accumulated net errors and omissions in the balance of payments. These sources are uncertain by construction, and they have been shown to be sensitive to adjustments in the computation of the national accounts and the financial accounts. Their estimate suggests that Swedes hold roughly 5% of total domestic financial assets in offshore tax havens. Alstadsæter, Johannesen and Zucman (2019) present similar estimates for Sweden, but instead use differences in national balance sheets across countries to back out hidden wealth. Their estimate for 2007 is that 3% of households' financial assets were held in tax havens.

As for the distributional effects of offshore wealth, Roine and Waldenström (2008) estimated the effect on the income distribution by adding an assumed return from the offshore wealth to the disclosed domestic incomes of the top decile and percentile in the income distribution. They find that the effect on income shares is moderate for the top decile; their income share increases from 25% to 27% of total income after adding the offshore wealth returns. Looking at the top percentile, adding the same amounts has a relatively larger effect, increasing the top percentile income share from 7% to 9%, which is an increase by roughly one-quarter. Roine and Waldenström (2009) did a similar exercise for the wealth distribution. They found that adding

[5] See also Ring (2019) for a recent paper analysing wealth tax responses using Norwegian data, finding evidence of a positive effect on savings in response to wealth taxation, financed mostly by increased labour earnings.

[6] For an individual with a taxable wealth of 10 million Swedish kronor (SEK), the wealth tax in 2006 was 127,000 SEK. Assuming a lifetime real return of 3%, the net present value of all future wealth tax payments is 4.25 million SEK (127.000/3%), which thus would imply a mechanical tax-reform effect of an increase by 40% for previously taxed fortunes.

[7] Another aspect is that the value of financial assets tends to decline more rapidly than the value of real estate in downturns, while the opposite holds during upturns.

the estimated offshore wealth to the reported wealth of Swedish households belonging to the top percentile in the domestic wealth distribution leads to an increase in their share of total private wealth from around 20%, up to 25%–30% of total wealth. This is a relative increase by one-quarter, up to one-half. Alstadsæter et al. (2019) made another estimate of the effect of hidden wealth in foreign tax havens on the wealth distribution in Denmark, Norway and Sweden. Using information about named tax evaders linked to administrative wealth registers in Sweden, they found that the majority of tax evaders belong to the top wealth groups in Sweden; about 80% of them were in the top 0.01 percentile. These findings highlight the difficulties in targeting the wealthiest groups in society with a wealth tax.

Altogether, our knowledge about the effect of wealth taxation on wealth accumulation, tax avoidance and the economic distribution is inconclusive. Studies conducted in different countries are difficult to compare because of the differing implementation of wealth taxation. Moreover, the data are not always comparable. The studies cited above have found indications that wealth taxes prevent the accumulation of business assets, especially in the very top of the wealth distribution, whereas the accumulation of housing wealth or other popularly held assets seems to respond much less. Tax-driven capital flight to offshore havens seems to be related to the relatively high levels of capital taxation in rich countries, and it seems that it is the predominantly richest households who are engaging in these activities. These pieces of evidence suggest that wealth taxation dampens wealth accumulation in the very top of the distribution while inducing the wealthiest to spend resources to hide wealth in offshore havens.

6.3 Inheritance taxation

The taxation of intergenerational wealth transfers can practically be designed in different ways. The *inheritance tax* is paid by someone who inherits from a deceased person, the *estate tax* is a tax on the assets of a deceased person, and the *gift tax* is a tax on gifts between people during their lifetime.[8]

Bequests can have substantial behavioural impacts on recipients, mainly due to income effects affecting labour supply and early retirement. These income effects are not distortionary per se, but it is important to take these into account as behavioural responses to the acquisition of inheritances can lower tax revenue from labour income taxes, and increase pension-related government expenses. This provides an efficiency reason to tax bequests (see Kindermann, Mayr and Sachs, 2020). On the donor side, however, there can be efficiency costs of inheritance taxation if a major motivation to work or accumulate wealth is the desire to transfer wealth across generations. The efficiency costs of taxing bequests are smaller if bequests are unexpected, as substitution effects are avoided.

The main equity argument for inheritance taxation is that those who receive inheritances tend to have higher incomes and are therefore better off. For many people, the central equity argument in favour of inheritance taxation is that receiving an inheritance represents an ‘unearned advantage’ that should be taxed to equalize opportunities in society. However, the equity role of inheritance taxes is not entirely straightforward to assess. First, an inheritance gives utility both to the donor (through the ‘joy of giving’) and to the receiver. This ‘double-dividend’ of giving is considered an argument in favour of subsidizing inheritances (Farhi and Werning, 2010). Second, the power of inheritance taxation to redistribute wealth is in practice greatly undermined by the difficulties to properly tax the succession of (non-listed) family businesses, which represent a major share of aggregate inheritance flows.

[8] See Cremer and Pestieau (2011), Kopczuk (2013) and Bastani and Waldenström (2020) for reviews.

As with the wealth tax, the interaction between the bequest tax and the rest of the tax system is important. On the one hand, one may argue that if all bequests are intentional (i.e. like a form of saving), and all capital incomes are taxed, then there would be no reason to tax bequests at all if the entire returns to the assets that constitute the bequests are completely taxed. On the other hand, given that bequests often consist of real estate, and governments lightly tax or even subsidize housing, or family-firm succession, which is often subject to reduced rates as well, an inheritance tax might be necessary to counter this distortion.

An important question is whether an optimal inheritance tax (that trades off the costs and benefits of inheritance taxation) is positive. In the standard infinite-horizon model with a representative agent where generations are perfectly linked through altruistic bequests, the taxation of bequests is isomorphic to the taxation of capital income in the Chamley–Judd framework. However, this is not a very realistic framework to analyse optimal inheritance taxation as it misses the fact that individuals are heterogeneous both in terms of their earnings abilities and in terms of their bequest behaviour, which can create substantial inequality in the long run. Farhi and Werning (2013) extend the work of Farhi and Werning (2010) by introducing heterogeneity in parental altruism and find that estate taxes can be positive if preferences for redistribution are sufficiently egalitarian. Piketty and Saez (2013) construct a model where each generation both gives and receives bequests and there is a correlation in earnings abilities across generations. They find that if those who receive large inheritances are more likely to be individuals with a high earnings ability, then the optimal tax rate is positive and quantitatively large if the elasticity of bequests is low, bequests are relatively concentrated, and those who receive small inheritances carry a large weight in the social welfare function.

The administrative definition of the inheritance or estate tax base is similar to the one used for wealth taxation. Thus, inheritance and wealth taxes share many practical problems. In principle, all transferred assets should be part of the tax base and they should be valued at market prices. In practice, however, many assets are assigned values for tax purposes that are far from their true market values because of heavy discounts or, in some cases, full exemptions. Business equity typically enjoys large discounts and the inheritance tax base only includes a fraction of the full value of business equity. Listed shares are relatively easy to handle, whereas shares in closely held corporations, or business assets in unincorporated enterprises, are more problematic to value. Most countries have introduced valuation discounts on business equity in non-listed firms. In Sweden, such discounts were first introduced in the 1970s, and from 1991 they imply that only 15% of business assets should be included in the estate tax base.

The issue of taxing family-firm successions is arguably the most hotly debated aspect of inheritance taxation. For example, in the Netherlands, there is a very friendly regime for family firms, which allows for large tax concessions for family businesses. Mainly the very wealthy benefit from it and the tax advantages can be very large. A popular argument in favour of such concessions and against inheritance taxation, in general, is that inheritance taxation can destroy family firms because of liquidity problems that the heirs face when exposed to the tax. Those who propose to include family firms in the tax base emphasize the equity argument and the need for treating all assets and heirs equally. However, there are also efficiency arguments for the inclusion of family firms in the inheritance tax base. For example, taxing these inheritances reduces lock-in effects in the taxation of capital income at the corporate or personal level. Moreover, some studies show that heirs may actually not be the best suited to run the businesses they inherit, implying that there could be efficiency gains from taxing bequests so that family firms are diverted to professional owners and managers (see Bennedsen et al., 2007).

Another issue is that liabilities and latent tax debt on capital gains are not transferred to heirs in most countries. These exclusions could have important real effects but, despite this, they have not been discussed much by researchers. For example, the fact that heirs do not inherit any net debt the decedent may have upon death contributes to equalizing the distributional effects of inheritances.

6.4 Experiences of inheritance taxation

Inheritance and estate taxes have existed in all Western countries for several centuries. Contributing to their popularity was surely the fact that they represented taxes on well-defined tax bases in times when governments typically had much less developed technologies for tax collection relative to modern economies, and also people's debts always needed to be settled at death before any funds could be distributed to heirs. Many rich countries still tax inheritances in one form or another, as indicated by Figure 6.2.

Figure 6.2 depicts the share of tax revenue relative to GDP for inheritance, gift and estate taxes in OECD countries since 1980. It is clear that taxes on intergenerational transfers represent a small fraction of tax revenues, about one-half of 1% of all taxes and about one-twentieth of capital taxes.[9] Looking at the trends over time, the figure shows that the levels vary somewhat between years, but there is not much drift in the overall level, which lies around 0.2%–0.3% of GDP over the entire period for these countries (the OECD average has been 0.1%–0.2% of GDP). The fact that inheritance tax revenue as a percentage of GDP has been relatively constant over time, combined with the fact that tax rates on inheritance have remained roughly constant over this period in most countries, indicates that the inheritance tax base has not experienced base erosion in any significant way due to the increasing mobility of capital.[10] However, estimates for France and Sweden indicate that aggregate annual inheritance flows in the economy have increased substantially since the 1990s, largely due to the increases in the relative values of private wealth over the same period (Piketty, 2011; Ohlsson, Roine and Waldenström, 2020), indicating a possibly increasing extent of tax avoidance.

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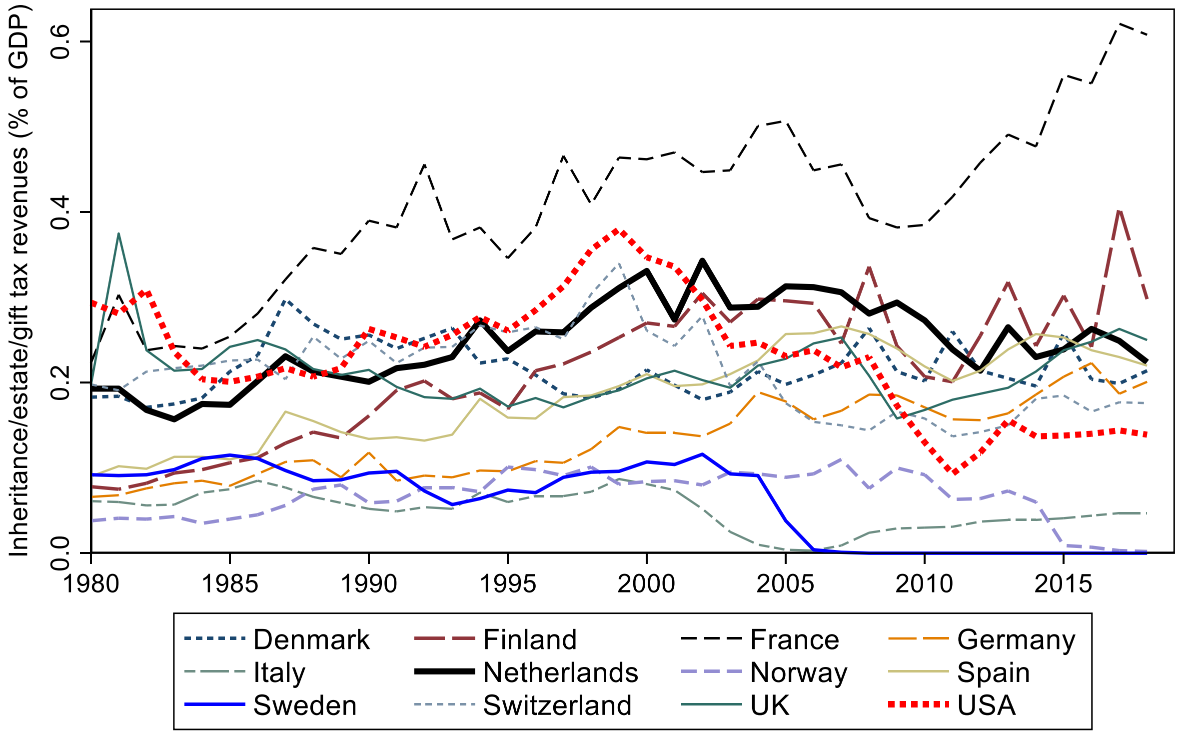
[9] Taxes over GDP range between 30% and 50% in the post-1980 era and the capital taxes have been roughly one-tenth of total taxes in all countries and years (Bastani and Waldenström, 2020).

[10] The fact that this is the case also for many of the small, open European economies, including the Nordic countries and the Netherlands, is also an important observation.

Figure 6.2. Inheritance, gift and estate tax revenues in 12 OECD countries (percentage of GDP)



Source: OECD Revenue Statistics, item 4310 'Estate and inheritance taxes'.

It is instructive to compare how marginal tax rates and basic exemption amounts for inheritance and estate taxes differ across countries. We focus on the case when the beneficiary is a child, which represents the largest group of heirs who generally face the lowest marginal inheritance tax rates and the most generous basic exemptions.[11] In the Netherlands, child beneficiaries start paying an inheritance tax of 10% on bequests over 20,000 euros and the tax increases to its highest marginal rate, 20%, on bequests over 124,727 euros. Denmark uses a flat inheritance tax of 15%, paid on bequests exceeding roughly 22,000 euros. In Finland, an inheritance tax of 7% is paid on bequests exceeding 20,000 euros, and the marginal tax increases on larger bequests up to a top tax rate of 19%, paid on inheritances above 1,000,000 euros. In Iceland, there is a flat 10% inheritance tax on bequests of 10,000 euros and higher. In an historical perspective, these tax rates are lower than those many countries had during the early post-war era, when marginal tax rates on large bequests and estates often reached levels of 60%–90% (Scheve and Stasavage, 2012; Henrekson and Waldenström, 2016). The basic exemptions vary greatly across countries.

Empirical studies of the economic consequences of inheritance taxation are few. The main reasons are that data are scarce and it is extremely difficult to distinguish real capital accumulation effects from tax avoidance responses, where the former are the most interesting from an economic perspective. In a survey of the literature, Kopczuk (2013) concludes that the effects of inheritance taxation on taxable inheritances appear to be relatively small in magnitude. In an early influential study, the same author examined estate tax planning in the United States, exploiting the timing of receipt of news about terminal illness (Kopczuk, 2007). The results show that the estates of individuals who received the bad news early decreased in value, primarily due to tax planning. Goupille-Lebret and Infante (2018) examine the effects of changes in the French

[11] See Worldwide Estate and Inheritance Tax Guide 2019 (available online at https://www.ey.com/en_gl/tax-guides/worldwide-estate-and-inheritance-tax-guide-2019).

inheritance taxation on private savings in life insurance funds. Using discontinuities in the tax code with respect to time and age, they attempt to disentangle real accumulation effects from avoidance responses and they find modest effects on real capital accumulation.

In the Nordic countries, inheritance taxation has been studied in a few papers. Henrekson and Waldenström (2016) examine the evolution of the Swedish inheritance tax over a century and point to evidence that the historically high tax rates in the 1950s, 1960s and 1970s were associated with significant avoidance behaviour and cross-border capital flight among the wealthiest. In an unpublished study of Swedish administrative register data on inheritances and firm performance, Escobar (2017) finds that firms whose owners inherit significant amounts tend to last longer than other comparable firms do. However, this phenomenon does not seem to be driven by higher productivity, measured as firm profits or owners' incomes, but instead by enabling small business owners of lower ability to carry on longer.

When assessing the distributional implications of inheritance taxation, it is necessary to take into account the distribution of inheritances as well as the economic position of those who acquire them. The empirical literature has generally found an equalizing effect of inheritances because the distribution of wealth among the decedents tends to be more equal than the distribution of wealth among the heirs (see, e.g., Elinder, Erixson and Waldenström, 2018). Still, sufficiently progressive inheritance taxation combined with appropriate adjustments of taxes and transfers can also serve as an instrument to enhance redistribution.

To properly understand the evolution of inheritance taxation in the Western world, it is necessary to take into account political-economy considerations. Scheve and Stasavage (2012) analyse the political determinants of inheritance taxation over the past 200 years. They argue that historically important increases in inheritance taxation during the first half of the twentieth century can be explained by mass mobilization for warfare, rather than the extension of suffrage. The proposed explanation is that mobilization in times of war implies that people will risk their lives in war. Therefore, people will demand that the rich also make sacrifices by contributing with their wealth.

The dismantling of the inheritance tax in Sweden in 2004 is an interesting story from a political-economy perspective. The exceptionally low basic exemption for bequests in Sweden (see Bastani and Waldenström, 2019) in combination with rising house prices during the 1990s meant that a large fraction of heirs, about one-third in 2000, had to pay the tax. At the same time, the government introduced extended tax reliefs for business equity in the 1990s, which effectively meant that most large bequests were almost tax-exempt. In other words, more and more taxpayers at the lower end of the distribution had to pay the tax while fewer and fewer at the top had to do so. In addition, there was a wide perception that inheritance tax avoidance was common, which further undermined the perceived effectiveness of the tax. When the Social Democratic government eventually proposed abolishing the tax, not even the left-wing party opposed it.

6.5 Concluding discussion

In this chapter, we have reviewed central themes in the economic analysis of wealth and inheritance taxation as well as practical experiences of wealth and inheritance taxation in the Nordic countries. We have discussed the most important theoretical arguments in favour of and against such taxes and we have surveyed a selection of the empirical research literature.

Wealth taxes have almost disappeared from the fiscal policy toolbox in modern economies, whereas many countries still use inheritance taxes, notably some of the world's largest economies. In the Nordic countries, only Norway employs a proper wealth tax, while Denmark, Finland and Iceland still employ inheritance taxes.

A wealth tax can be a useful instrument to tax the wealth holdings of the wealthiest, especially if there are restrictions on the optimal use of capital income taxation. However, the possibility for small, open economies to tax internationally mobile wealth and inheritance flows has limitations, especially when it comes to the top of the wealth distribution. The liberalization of capital accounts in the 1990s implied that cross-border flows became more common, and this has had a large impact on the perceived effectiveness of capital taxation in the Nordic countries.

In the Nordic countries, and in the Netherlands, the tax revenue from wealth and inheritance taxes, as a fraction of GDP, has been on an almost constant level for decades. Inheritance flows and aggregate private wealth (as a fraction of GDP) seem to have increased, which can be explained by either an eroding tax base or falling tax rates. The fact that some countries have chosen to abolish wealth and inheritance taxes, and others not, seems to be explained by practical tax design issues and political economy aspects, rather than purely economic reasons.

One important and contentious issue in the context of wealth and inheritance taxation is the potential need for the preferential treatment of wealth pertaining to family firms. In Sweden, the concern for family-firm successions led to extensive tax discounts and even full exemptions. These exemptions shifted the tax burden from the very wealthy to upper middle-class households with expensive residential property. In Sweden, this gradually eroded the political support for wealth and inheritance taxes, ultimately leading to their abolishment. An important lesson for other countries is therefore that it is not only the economic rationale for inheritance and wealth taxes that determine their support in the population, but perhaps, most importantly, their perceived legitimacy.

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