WEALTH TAX WITHIN EUROPE IN THE CONTEXT OF A POSSIBLE IMPLEMENTATION IN ROMANIA– THE EXISTING WEALTH TAX AND ITS DECLINE IN EUROPE

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ABSTRACT: *The purpose of this paper is to focus our attention on the conceptual basis upon which the wealth tax system may be implemented in Romania taking into consideration former and actual presence of wealth tax within Europe. The idea of increasing the taxable basis based on imposing the wealth constitutes one of the most important debate topics on the agenda of the Romanian Parliament and Government and also within specialists' theoretical approaches. The vast range of such approaches and further solutions is to be analysed in the global context of direct taxation in Europe and worldwide and particularly relevant for the complexity of the problem is the evolution of wealth tax during the last decades and also the very important context of moving corporate main offices in countries with more advantageous systems of taxation.*

KEY WORDS: *wealth tax; property taxes; direct taxation; fiscal solutions; economic downturn*

JEL CLASSIFICATION: *H24*

1. INTRODUCTION

The starting point should be the assertion that "fiscal policy decisions reflect the related tax system and ensure its functionality in order to obtain the aimed economic effects" (Dobrota & Chirculescu, p.207-213). In the specific condition of worldwide economic downturn, Romania has also faced new challenges in finding various solutions and designing fiscal and budgetary scenarious in respect of fiscal policy and budget policy that may lead to limit the effects of economic and financial crisis.

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Some economists agree that most taxes distort economic behaviour, which leads to reduced economic efficiency and hence reduced economic output. Under these circumstances the analysis in respect of wealth tax reveals that it has a negative impact in economic growth in a number of ways. But first of all it is important to define the concept of wealth, generally defined as a direct tax imposed on the wealth possessed by individuals, but usually finding various meanings and understandings in each country taking into consideration the different tax policy and fiscal environment.

2. WEALTH TAX CONCEPT IN THE ECONOMIC LITERATURE

According with the finance and business dictionary wealth tax is defined as: "tax on accumulated wealth a tax on somebody's accumulated wealth, as opposed to their income" (available on http://www.qfinance.com/dictionary/wealth-tax). Another definition positioned the wealth tax as a tax which is levied on the wealth held by a person or entity and being mostly levied on net worth, i.e. the amount of someone's wealth minus his or her debts. Several nations all around the world use the wealth tax to raise funds for the government, using various types of wealth taxes and taxable basis.

A wealth tax is generally conceived of as a levy based on the aggregate value of all household holdings actually accumulated as purchasing power stock, cash, bank deposits, money funds, and savings in insurance and pension plans, investment in real estate and unincorporated businesses, and corporate stock, financial securities and personal trusts. Net wealth tax can be distinguished from property taxes due to the fact that property taxes are imposed on the gross amount of property, without any reduction for debts and usually are imposed only on certain kinds of property, while net wealth tax is a more or less comprehensive tax on net worth, i.e. the value of property reduced by debt (Thuronyi, 2003, p.329).

What it is very important to first define is that the wealth tax is a tax not on income but on assets, i.e. that the taxable basis will vary from country to country according with the fiscal policy and taxable revenue based-interest, as follows: taxes on premises, houses, real estate properties, cars, art collections, jewellery, stocks and bonds, bank accounts, pensions, investments, companies owned in whole or in part and the taxable persons may be individuals or corporate persons (the example of India).

Another characteristic revealed by the economic studies has enhanced on one hand the fact that most of the governments levying this net worth tax are advanced welfare states with a relatively high government spending to GDP rate. (France, India) and on the other hand the long-term trend in wealth-tax receipts as a share of total taxes and of GDP has generally been downward or constant in many of these countries (Hansson, 2002).

Most of the countries apply in the field of direct taxation only the property taxes on the market value of real estate assessed almost by the local tax authorities, because they rely upon the fact that real estate cannot be moved out of another jurisdiction, whereas income, paper wealth, etc. are more easily moved to other localities where they may be taxed less or not at all. In comparison with wealth tax apply to other assets than real estate properties, it was in many areas demonstrated that real estate tax revenues can be a very effective way to raise large sums of money, as people who hold valuable real estate investments can owe substantial property taxes annually. In regions where overall real estate values are high, property tax revenues provide a great deal of revenue to local governments.

3. EXISTING WEALTH TAXES WITHIN EUROPE

France is the only EU country to impose a standard wealth tax model since 1981. In the continent of Europe, Norway and Lichtenstein have versions of it, Switzerland levies at cantonal level at variable, mostly low levels, Hungary start implementing it since 1st January 2010 and Spain wants to reintroduce it since mid 2010. Several countries have abolished their versions of the tax in recent years, including Austria (1994), Denmark, Germany (1997), The Netherlands (2001), Iceland (2006), Finland (2006), Sweden (2007) and Greece (2009). Others countries, including Britain and Belgium, have never had such a tax, although the similar concept was implemented through the Window Tax of 1696 (tax introduced under the Act of Making Good the Deficiency of the Clipped Money in 1696 under King William III, designed to impose the prosperity of the taxpayers).

Italy offers another pattern of possible wealth tax philosophy implementation, such as a limited temporary application form 1992 from the next 3 years. Officially wealth tax was abolished a few years later (1998) (Heckly's, 2004, pp. 39-50).

In case of Spain the government abolished in 2008 a wealth tax that charged 0.2 to 2.5 percent on assets above 600,000 Euros, amounted a general impact in the annual state revenues to 2 billion Euros (around 0.2 percent of GDP), but Spain's Socialist government will impose a new tax on the wealthy mid 2010 broadening its deficit-cutting campaign to 3% of the GDP in 2013 from 11.2% in 2009, after unions threatened a general strike to protest against austerity measures. This new tax will affect (according with the Spain Prime Minister Luis Rodriguez Zapatero debates in the Parliament) only people with" high-economic capacity" and "it won't affect general taxes and it won't affect 99.9% of the Spanish population".

France. Individuals resident in France and non-residents with assets in France are taxed on the basis of their assets in excess of 790.000 euro (Starting with 2009) as at 1 January each year applying the wealth tax known as ISF (*Impot de Solidarité sur la Fortune*). This direct was one of the Socialist Party's 1981 electoral program's measures, titled 110 Propositions for France and has represented in 2006 approx. 1,28% from the general state budget revenues, i.e. 3,68 billion Euro collected from the taxpayer.

Residents are liable to wealth tax on their net worldwide assets including all properties, subject to the provisions of tax treaties, based on the wealth of the household, including spouse and infant children. Taxable assets include: real estate, cars, other vehicles, debts due to you, furniture (except antiques), horses, jewellery, shares, bonds and the redemption value of any life assurance, but there are also exempt assets, such as: those necessary to a business conducted by its owner or their spouse; pictures, tapestries, statues, sculptures, lithographs, antiques over 100 years old, funds in a pension fund constituted in respect of an employment or business, subject to certain conditions and also portfolio investments and cash held by non-residents.

A new law was enacted on 6 August 2008 exempting the non-French assets of anyone arriving in France after that date for five years, provided that they were not resident in France at any point during the five years prior to their arrival in France.

Table 1. French Wealth Tax Bands 2010

Fraction Taxable	Rate of Tax (%)
Up to €790,000	0
€790,000 - €1,290,000	0.55
€1,290,000 - €2,530,000	0.75
€2,530,000 - €3,980,000	1.00
€3,980,000 - €7,600,000	1.30
€7,600,000 - €16,540,000	1.65
Over €16,540,000	1.80

Source: http://www.french-property.com/guides/france/finance-taxation/taxation/wealth-tax/rate/

Norway. The tax qouta is up to 0.7% (municipal) and 0.4% (national) and represents a percentage of 1,1% levied on net assets exceeding Nkr. 470,000.

Liechtenstein. Net worth tax is charged on the net assets of the taxpayer: assets, securities, cash, deposits and valuables at a maximum rate of 0.9%. Liabilities, such as mortgages and loans are deducted and assets and liabilities are taken in at fair market value.

Switzerland. Individuals are subject to an annual wealth tax in all cantons (political regions) and communities and no wealth tax is levied at federal level. Wealth tax is levied on the entire wealth of a tax liable individual i.e., all movable and immovable assets, rights and claims of monetary value, securities, participations, etc. but household effects and articles of personal use are exempted. Wealth tax should not decrease the net wealth of an individual, but indirectly tax the income deriving from this wealth. Wealth tax can thus be understood as a tax amending income tax.

Tax resident individuals are subject to wealth tax on their world wide assets. Non-resident individuals are liable to wealth tax only for assets closely linked to Switzerland (i.e., for real estate and permanent establishments located in Switzerland, but not for securities deposited on a Swiss bank account or participations held in a Swiss company). Even though the tax liability of non-residents is reduced on assets linked to Switzerland, the progressive tax rate is always determined on the basis of an individual’s worldwide wealth. The tax payable varies between cantons to cantons. Subject to slightly differing cantonal regulations the amount of gross assets is reduced by the underlying debt so that only an individual’s net wealth is taxed.

In general, all assets are evaluated at their fair market value. Some assets are, however, subject to specific valuation rules (e.g., participations in stock quoted companies are usually evaluated at their stock price at the end of the tax period whereas for non quoted securities estimated values determined according to published valuation regulations apply). The annual wealth tax stands at approximately 1.5% in many cases. In most cantons tax rates follow a progressive scale. The base rate is determined in the cantonal tax law. The amount of wealth tax is computed by multiplying the individual's net wealth with this base rate and subsequently multiplying the result with the cantonal and communal tax multipliers as published on a yearly basis.

Luxembourg. The net worth tax in Luxembourg is known as the Fortune Tax and is levied on resident and non-resident corporate entities. For businesses, the two main components of Net Worth are Real Estate Unitary Value and Business Net Worth which is an adjusted version of net worth as calculated for the Corporate Income Tax. The rate of tax is 0.5%. However, for most companies the amount of Fortune Tax payable is offsettable against Corporate Income Tax, subject to some balance sheet reserve requirements.

Hungary. Wealth tax has been introduced in Hungary as of January 1, 2010 having as main target the governmental needs to meet budget deficit targets attached to the country's International Monetary Fund-led bailout. The taxable basis was established as follows: real estate, watercraft, aircraft and high-powered automobiles. Due to the fact that the law fails to provide clear guidelines to determine the property's market value as the taxable basis the regulation in case of wealth tax for high-value real estate have been struck down by the Constitutional Court and only a tax on high-value yachts, planes and helicopters and cars has been finally confirmed. Wealth tax advance should be paid by May 20, 2010 and September 30, 2010 and the wealth tax return deadline is the personal income tax return submission deadline of the related tax year (i.e. the 2010 wealth tax should be reported by May 20, 2010, as an attachment to the personal income tax return).

4. SOME REASONS OF THE WEALTH TAX DECLINE IN EUROPE

One of the most recent examples of wealth tax being abolished is that of The Netherlands, under the 2001 General Tax Reform. However, while the wealth tax was removed, it was just as soon replaced by a 30% tax on theoretical revenue on capital, assumed to equal 4% of net assets (excluding main place of residence and capital invested in personal enterprise). As a result, wealth tax there stands at 1.2%; at the same time, actual revenue on capital (interests and dividends) is fully exempt. That being said, it is admittedly too early to assess the impact of the said reform.

In other countries, such as Finland and Norway, where wealth tax still applies, it has been criticised, though it seems unlikely that it will be done away with in the near future. To wit, Norway's Skauge Committee recommended, in a report on tax reform handed in to the government in February 2003 that the tax be cut in half and, in the longer term, done away with entirely. However, the prospect of such a measure stirred negative reactions in public opinion.

France, too, is familiar with beating around the wealth tax bush: removed by the Chirac government in 1986, the tax was re-established by the Rocard government in 1989, under a new name – perhaps drawing on the solidarity-based capital tax, which had been temporarily instituted by the 15 August 1945 Order.

The scientific literature has surprised some reasons why wealth tax was abolished in some European countries, as follows:

- *It contributes to capital drain.* This is the factor that most influenced the Irish and Dutch governments, when they decided to do away with the tax. As they had realised, it had a harmful effect on the country's economic activity, causing productive capital to leave and discouraging foreign investors from coming in. In contrast, the desire to prevent capital drain was less a factor for Austria. This could, admittedly, be due to the country's banking and tax system, which is attractive to investors. The same is true of Germany, where capital drain played a secondary part, the decisive factor being the Constitutional Court's decision, and the cost-return ratio observed.

- *It entails high management costs yet low returns.* In this age of fiscal competition, governments and authorities also need to be competitive and have shown a clear preference for modern taxes with high yield, as in VAT or France's CSG. The complexity of wealth tax is such that a large number of civil servants are required, to perform the checks, when it rarely yields more than 1% of total tax income in most countries. It is that complexity which, as early as 1976, made the Germany's Union Fiscal Civil Servants demands the abolition of wealth tax. In Austria too, the complexity and lack of clarity around the tax played a decisive part in bringing it down. In The Netherlands, a comparative study listed the various taxes by management cost (cost of tax collection for the government and costs borne by taxpayers to come in compliance with tax legislation), compared to the revenue brought in: the aggregated cost (those borne by taxpayers, on the one hand, and by the government, on the other) amounted to 26.4% of the tax's yield, as compared to 4.8% with income tax.

- *It distorts resource allocation.* In Germany and Austria alike, the wealth tax was levied both on corporate capital and individual wealth. As a result, companies and shareholders were hit with double taxation. While it would, admittedly, have been possible to remedy that by limiting taxation to individual wealth, this would have brought about a degree of fiscal discrimination against individual enterprises, which would have remained subject to tax. The tax system would thus not have remained neutral as regards corporate taxation. It is true that the German tax authorities might also have exonerated working equipment, as France had done, but given the tax's high collection cost, they did not wish to reduce its yield further.

Imbalances can also arise in how savings are spread between the various types of assets, given that some of them are exempt from tax. In Finland, for instance, checking accounts, savings accounts and certain types of bonds (in particular those where an automatic deduction is taken on interests, at the source) are all tax exempt. Moreover, since real estate there is under-valued, the Finnish wealth tax is by no means neutral regarding how various investments should be carried out. In Germany, such distortion is even more noticeable, hence the Constitutional Court's decision. The various types of assets were not given equal treatment. Real estate was considerably under-valued, as the official taxation bases used were, for the most part, those of 1964.

For instance, it was estimated that the land's official value was around 50% that of market value, the value of farming and forestry properties only 10% and that of unlisted corporate shares only 35%. In contrast, listed securities and financial assets cannot be undervalued. Thus, while Germany's wealth tax creates economic distortions, it is also inequitable, and it is that aspect, above all, that the Constitutional Court sought to condemn.

- *Wealth tax is not as equitable as it appears*. This is probably the most serious criticism under which the tax can fall, as it was precisely in order to ensure equity that it was instituted. To witness, in France, the fact that the solidarity wealth tax was instituted at approximately the same time as the subsidised minimum mainstreaming income (RMI) is highly symbolic: the total yield from the former was approximately equal to the total cost of RMI, as though the wealthiest people were coming out to help the least privileged populations. However, it has to be recognised that, in most industrialised countries, disparities in income and estate have considerably increased over the last twenty years, despite the existence of wealth tax. Inheritance tax has probably been more effective in re-distributing resources than annual wealth tax, in that the latter would need to be confiscatory in order to bring about any real redistribution. This is exactly what the Constitutional Court in Karlsruhe stated when it criticised German wealth tax: that the sum of wealth tax and income tax should not be greater than half of a taxpayer's income. The tax thus gives rise to a dilemma: either it is effective in fighting inequalities, or it is confiscatory – and it is for that reason that the Germans chose to eliminate it.

5. CONCLUSIONS

Despite recent debates in the political arenas of a number of European countries in the wide context of the economic downturn, there has been little empirical study of the relationship between the wealth tax and economic performance. In Romania there was a recent legislative initiative that sets the proposal to levy an annual quota of 0.5% affecting people net wealth over 500,000 euros, considering the family's wealth, including spouse and their underage children.

The taxable basis should have been real estate goods and properties, financial rights and values belonging to the individual, his/her spouse and their children (underage) in the case they administrate the individual's goods. The law project also sees that resident individuals should pay an annual duty for net patrimony owned in Romania and overseas, while non-residents pay for the net patrimony owned in Romania, on condition that the international convention addressing double taxation is respected.

Using the information presented above our assumption is that in case of Romania the advantages of levy the wealth tax over the fiscal benefits (increasing the state revenues in the near future and also in a mid and long perspective) are not material. The arguments in favor of wealth tax are less than the arguments against the wealth tax and therefore the Romanian government should take into consideration these assumptions.

Even if the wealth tax would generate revenues, which could be used to decrease the national debt, on the other hand the same wealth tax would generally incur high management costs, for both the taxpayer and the administrating authorities, compared to other taxes.

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