

Background Paper

*Wealth Tax Commission*

# The costs of administering a wealth tax

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# THE COSTS OF ADMINISTERING A WEALTH TAX

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# 1. Introduction

Despite having proposed a wealth tax for the UK in a Green Paper in 1974, the Labour government at the time never implemented the levy. Upon reflection in 1989, the former Chancellor of the Exchequer, Denis Healey, stated: ‘We had committed ourselves to a wealth tax; but in five years I found it impossible to draft one which would yield enough revenue to be worth the administrative cost and the political hassle’.<sup>1</sup> This observation was borne out around the same time by the experiences with the Irish wealth tax which was introduced in 1975 and abolished by 1979. According to Sandford and Morrissey (1985), the total operating costs to taxpayers and the Irish Revenue were at least 25% of wealth tax revenue. However, these attempts to implement a wealth tax were nearly 50 years ago. What would be the administrative costs for a wealth tax today?

This paper aims to provide an up-to-date evidence base on the costs of administering a wealth tax based on the experience from taxes on wealth that currently exist in the UK and information from other countries that currently impose a wealth tax or have done so in the past.<sup>2</sup> It should be emphasised that these costs crucially depend on design choices. Motivated by this observation, the paper throughout links the presented evidence to the corresponding policy features.

It is important to note that the costs of administering a wealth tax are incurred both by taxpayers and the tax authority. Thus, this paper examines costs for each of these groups. In practice, this boundary is not fixed. It would be possible to shift costs from the taxpayer to the tax authority (or vice versa) depending on the design of the administrative process. For example, valuations could be conducted by the tax authority or by another government agency, rather than commissioned privately by taxpayers. In such circumstances, the effect on the total costs of administering the tax will depend on which side can deliver the relevant administrative services most efficiently.

In this paper, the costs to taxpayers are defined as the direct financial expenses incurred, e.g. professional advisory fees, and do not take into account the indirect costs of a taxpayer’s own time spent on administration. In relation to the tax authority, the analysis includes the costs of additional staff (payroll costs and overheads) on an operating basis, but it excludes any fixed costs of setting up new systems etc. associated with the initial introduction of the tax.<sup>3</sup>

The administrative costs can be represented in various ways. In the literature and official statistics, they are often expressed in percentage of tax revenue because this allows an intuitive interpretation and, from the government perspective, highlights what share of the intake is spent on collecting the tax and what share is available for other public expenditure. However, this representation is mechanically related to the associated tax rate, because – all else equal – the administrative costs do not vary much depending on the tax rate, but tax revenue varies significantly. As this paper aims to be informative for a range of wealth tax designs, including variation in the tax rate, the headline statistic generally used throughout the paper and in the

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<sup>1</sup> For more information on the attempts to implement a wealth tax in the UK, see Broadway, Chamberlain and Emmerson (2011).

<sup>2</sup> Troup, Barnett and Bullock (2020) provide a thorough analysis of how a wealth tax could be administered in the UK.

<sup>3</sup> For a detailed analysis of the process to deliver a wealth tax in the UK, see Pope and Tetlow (2020).

conclusions represents the administrative costs as a percentage of taxable wealth.<sup>4</sup> This figure has the advantage that it is independent from the wealth tax rate and can be interpreted as an implied additional rate (or surcharge). The disadvantage is that it implicitly assumes that costs are proportional to the tax base whereas the fixed cost element of tax compliance and collection suggests that, while the administrative costs may increase with individual taxable wealth as wealthier taxpayers have more complex financial circumstances, costs do not increase one-to-one with asset values.<sup>5</sup> Thus, the paper relates the costs to the number of taxpayers subject to a wealth tax by additionally reporting costs per taxpayer where these data are available. Further, costs are generally also reported as a percentage of wealth tax revenue because this is the relevant metric from the perspective of the tax authority.

Given that the estimates for the administrative costs of a potential UK wealth tax are subject to considerable uncertainty, we will report a central estimate as well as a lower and upper bound for both the costs to taxpayers and the tax authority. Note that these figures are ‘best guesses’ from triangulating the available evidence, rather than the result of a precise calculation.

This paper proceeds as follows. Section 2 examines the administrative costs of a wealth tax for taxpayers. Section 3 discusses the costs for the tax authority. Section 4 concludes.

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<sup>4</sup> Taxable wealth refers to the tax base of the wealth tax. Simply put, it includes the net value of assets subject to the wealth tax, i.e. assets minus liabilities, after deducting the exemption threshold and any other exemptions or allowances. A different but related concept is *chargeable wealth* which refers to net wealth of taxpayers but includes the asset values below the exemption threshold.

<sup>5</sup> Another issue with expressing administrative costs in percentage of taxable wealth is that assets subject to a relief are exempt from the tax base but may still generate costs to taxpayers and the tax authority as these reliefs have to be claimed and assessed.

## 2. Costs to taxpayers

This section focuses on the costs to taxpayers of administering a wealth tax. The compliance efforts of taxpayers involve activities such as disclosure, filing returns, obtaining valuations – a process that can be expensive for assets that do not have straightforward market values – as well as resolving disputes and litigation. A substantial share of these costs is incurred in the form of professional advisory fees for accounting, legal and valuation services – particularly for taxpayers that are at the top of the wealth distribution and have complex financial circumstances. Where ownership of a particular asset is divided between interests in companies, partners and trusts, the position can get even more complicated.

Systematic evidence on the administrative burden on taxpayers is scarce. The first subsection sheds light on taxpayer costs by gathering and synthesising information from a selection of UK firms that have extensive experience in handling compliance activities related to existing taxes on wealth, such as the annual tax on enveloped dwellings (ATED) and inheritance tax (IHT). The second subsection draws on estimates from the literature for countries that currently impose or have imposed a wealth tax in the past.

### Experience from UK taxes on wealth

The UK taxes most closely related to a wealth tax are ATED and IHT.<sup>6</sup> In the following, they are considered in turn. Each subsection first explains how the tax works and then discusses the associated administrative costs based on the information from the firms we contacted and asked to comment on the administrative efforts associated with tax compliance. Overall, the selected firms tend to be larger accountancy and law firms with a specialism in advising high-net-worth individuals. Moreover, they tend to handle more complex affairs than average for a given level of wealth. This may mean that the reported costs are an upper bound for the overall population that might be subject to a wealth tax, because taxpayers with moderate wealth primarily own assets (e.g. residential property, cars, pension accounts, listed shares, financial savings) that are more straightforward to value compared with other assets concentrated in the very wealthiest section such as private business. Wealthier taxpayers that are likely to be overrepresented in these firms' experience tend to have more diverse portfolios and hold more private business wealth which is particularly difficult to value. To shed light on how the share of asset holdings that are hard to value varies across the wealth distribution, Advani, Hughson and Tarrant (2020) classify assets into three simple categories based on how difficult their valuation is, following the taxonomy outlined by Pentelow (2020). Using data from the Wealth and Asset Survey (WAS), Advani, Hughson and Tarrant show that below individual wealth of £5 million, 'the vast majority of assets by value (90% or more) are in the "easy" or "mid" categories'. For individuals with wealth of £5–10 million, 34% of their wealth is in assets that are hard to value. The corresponding share for individuals with wealth above £10 million is about 68%.<sup>7</sup>

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<sup>6</sup> For a more detailed discussion of UK taxes levied on wealth, see Summers (2020) and Troup et al. (2020). For a more detailed review of the way in which ATED and IHT work, see Appendix A in Troup et al. (2020).

<sup>7</sup> However, note that this figure is based on a relatively small number of observations, so there is more uncertainty about its accuracy.

## Annual tax on enveloped dwellings

Annual tax on enveloped dwellings (ATED) is a tax in force since 1 April 2013 and broadly levied on any company wherever resident that owns residential property over £500,000 in gross value, ignoring liabilities.<sup>8</sup> There is no ATED, mansion tax or further annual taxes on properties owned directly by trusts or individuals, other than council tax. ATED is self-assessed separately from other taxes and an online return must be filed on or before 30 April each year. Even if a relief is available, a return must be filed and the relief claimed for each dwelling house owned by the company. The value in April 2012 – or at acquisition, if later – is taken. Revaluations occur every five years working one year in arrears. The tax is levied by reference to bands which are listed in Table 1 below. If you are not sure which value band your property falls into, you can ask HMRC for a ‘pre-return banding check’, provided that your property falls within 10% of a banding threshold.

Table 1: ATED chargeable amounts for 1 April 2020 to 31 March 2021

Property value	Annual charge
More than £500,000 up to £1 million	£3,700
More than £1 million up to £2 million	£7,500
More than £2 million up to £5 million	£25,200
More than £5 million up to £10 million	£58,850
More than £10 million up to £20 million	£118,050
More than £20 million	£236,250

Notes: Chargeable amounts depending on the property value under the annual tax on enveloped dwellings (ATED) for the tax year 2020–21.

Source: HMRC.

The reliefs most likely to apply to exempt a property from ATED arise if (a) the residential property owned by the company is rented to unconnected persons; (b) the property is part of property development or property trading; (c) the property is a farmhouse; or (d) the property is open to the public for a minimum 28 days each year. These reliefs mean that ATED affects a much narrower range of properties than the inheritance tax charge on enveloped properties introduced in 2017 (IHTA 1984 Schedule A1) where the only test is whether the property is residential; the fact that the property is let or trading stock, for example, is irrelevant for the purposes of the IHT charge.

We mainly consider three different costs: (i) filing costs, (ii) valuation costs, (iii) legal costs for solving disputes and litigation. The following paragraphs discuss these types of costs in turn.

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<sup>8</sup> Hotels, guest houses, boarding school accommodation, hospitals, student halls of residence, military accommodation are not treated as residential accommodation for this purpose.

First, professional advisory fees for filing an ATED return generally range between £500 and £1,500.<sup>9</sup> Several firms have declared that they charge a fixed cost of £1,000 for an ATED return without reliefs, irrespective of the value of the relevant property, because the reporting process does not depend on the property value in principle. The fixed fee reflects that there is a certain minimum amount of time that must be spent on completing the form and checking if a particular relief is still available or the valuation is accurate. Smaller firms and trust administration providers may charge less than £500 in very straightforward cases, for example where the letting relief is obviously available. For other companies, compliance costs may exceed £1,500, particularly if the availability of a relief such as property development requires a more complex analysis.<sup>10</sup> In short, costs can vary considerably not only by reference to the firm but also depending on the peculiarities of the property and the number of properties the company holds. Under these circumstances, compliance costs may be less proportionately per property.

In general, the costs of filing an ATED return are modest because the form is short and does not require a lot of information in comparison to IHT. A wealth tax will certainly require a longer form.<sup>11</sup> Nevertheless, given that the ATED charge at the lowest band is only £3,700, filing costs can make up a significant share of total taxpayer costs for ATED; they become proportionately less for higher property values or where the company owns more properties.<sup>12</sup>

Second, valuation costs depend on the rigor of the assessment, the size and location of the property, and the professional firm involved. A value estimate or ‘condensed valuation’ for the purpose of filing an ATED return costs taxpayers from as little as £250 to around £1,000, while expenses for a formal valuation report usually range between £1,500 and £3,000, depending on the property characteristics and contracted firm. Valuation costs can be much higher as well – up to about £10,000 – for properties that are large, of high value and/or situated in prime locations. As stated before, revaluations must be carried out every five years.

Despite the banding approach, filing an ATED return in practice generally still requires obtaining a valuation or at least a value estimate in virtually all cases. Thus, banding does not alleviate the burden of valuation altogether. However, banding seems to lower the valuation costs because the assessed value can presumably be less precise as the determination of tax due only depends on whether the property value is in the right band. This helps particularly to minimise valuation costs for the most expensive properties, where all that is needed is to know that they are definitely above the highest threshold and, thus, subject to the highest charge irrespective of their exact value. In the tax year 2018–19, about 150 ATED liable declarations were in the top band (2.4% of the total number of 6,330 ATED liable declarations) generating £32 million in revenue (23.0% of total ATED receipts of £139 million) (HMRC, 2020a). For properties in lower

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<sup>9</sup> All cost figures provided in the following exclude VAT.

<sup>10</sup> See for example *Hopscotch Limited v HMRC* [2020] UKUT 0294 (TCC) where the Upper Tribunal upheld a First-tier Tax Tribunal (FTT) decision that the redevelopment of a single house in order to sell it was not a property development trade; no ATED relief was therefore due.

<sup>11</sup> The form for filing an ATED return is available here:

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/383854/return-paper-version.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/383854/return-paper-version.pdf) [accessed on 23 November 2020].

<sup>12</sup> Note that compliance costs are also incurred by taxpayers who do not have an ATED liability because of an applicable relief but still need to file a return in order to claim the relief. These compliance costs may be of sizeable magnitude in total since the number of ATED relief declarations of 19,670 is much larger than the number of ATED liable declarations of 6,330 in tax year 2018–19 (HMRC, 2020a).

bands, providing a professional valuation can be avoided in rare cases if the property value is considered to sit safely within a band.

Third, the costs of resolving disputes and litigation seem to be limited. According to the firms' experience, the band in which a property falls is rarely queried by HMRC as professional valuations are almost always obtained before filing ATED returns and HMRC can be asked for a pre-return banding check if in doubt.<sup>13</sup> Enquiries into relief returns are also said by firms to be a relatively rare occurrence, although some noted that if a property was purchased by a company and then let, sometimes both stamp duty land tax (SDLT) and ATED enquiries were raised to check the letting was not to a connected person. Like IHT, ATED has its own separate rules on rights of appeal and enquiry.

In general, total compliance costs of ATED are rather low because (a) the single asset in question – residential property – is regularly valued, i.e. there is an accepted methodology, a broad community of valuers, a lot of data available and usually a significant number of comparables; (b) formal valuations only need to be carried out every five years; (c) the digital filing of returns and relief declarations is easy to handle and does not take up a lot of time; and (d) chargeable amounts are determined by assigning properties into fairly wide bands. Although the contacted firms did not all agree that banding helps taxpayers to lower administrative costs, it is likely to reduce the burden of valuation and disputes compared to an ad valorem charge. Other advantages of banding for taxpayers are that compliance is straightforward and it is easier to budget tax costs.

However, relative to the level of tax, the compliance cost for ATED can be substantial. Adding up filing and valuation costs, and expressing them as a percentage of tax due or value of assets is informative for the approximate magnitude of the costs and for how they depend on property values.<sup>14</sup> For illustrative purposes, take a property in the lowest band for which obtaining a valuation and filing a return is straightforward. Accordingly, assume that annual filing costs are around £500 and valuation costs that are incurred every five years are about £500 as well. Thus, annual compliance costs of ATED will be around £600 which represents 16% of tax due or 0.06–0.12% of the asset value. Even if compliance costs increase with the property value, probably due to increased complexity, their importance shrinks relative to the charged amount and asset value. For instance, assume filing costs of £1,500 per year and valuation costs of £5,000 over five years for a property with a value of £5–10 million. Annual compliance costs will be £2,500, representing 4% of tax due or 0.03–0.05% of the asset value. In the top band, compliance costs are likely to be particularly low because costs for valuation and dispute solving can be largely avoided. However, it should be noted that ATED requires lots of taxpayers to file returns where no tax is payable because of a relief. For them, the compliance costs represent 100% of the total expenses for the tax.

Comparing the features of ATED to a wealth tax, some important differences should be highlighted. First, a comprehensive wealth tax applies to all assets, not just a limited number of residential properties held in companies. The banding approach works well in the case of ATED because real estate is widely held and changes hands frequently, generating ample information on transactions available to the public. These features do not apply to some assets taxable under

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<sup>13</sup> In any event, FA 2013 sch 33 para 36 sets out the very limited grounds on which an appeal may be made on questions of valuation.

<sup>14</sup> For this purpose, we ignore the costs for resolving disputes and litigation because they are difficult to quantify and are only rarely incurred.

a wealth tax such as chattels and private company shareholdings. Second, ATED applies to a single asset type whereas a wealth tax is based on multiple assets held by an individual. Hence, small uncertainties at the level of individual assets could aggregate to large uncertainty at the level of an individual's total wealth. Third, ATED on residential property in the UK is capped for properties of above £20 million and there are few properties within the top band. Total individual wealth has a much higher ceiling, which amplifies the magnitude of absolute errors in valuation even if relative errors remain small. Fourth, only a small subset of taxpayers who own property through a corporate structure is subject to the tax.<sup>15</sup> These taxpayers tend to be familiar with professional assistance and the associated fees. It is to be expected that a wealth tax would apply to a much larger segment of the population, just because of the broader coverage of assets, although this also depends on the chosen exemption threshold. These distinctions cast doubt on whether the cost-effective structure of ATED can be fully applied to a comprehensive wealth tax. It is notable, however, that ATED does apply to non-resident and UK resident companies irrespective of whether the individual shareholders are resident in the UK or not and so provides some precedent for the possibility of enforcement in relation to taxes on real estate held by non-residents.<sup>16</sup>

## Inheritance tax

Inheritance tax (IHT) is a much more complicated tax in design, levied mostly on death but also on some gifts made in a person's lifetime where:

- (a) the donor has died within 7 (sometimes 14) years or
- (b) the donor has made gifts into trust rather than outright or
- (c) the donor has made gifts to a company or a closely controlled company has made gifts.

Information on filing returns for IHT400 on death from the contacted firms suggests that there is large variation in the administrative burden across estates. Expenses depend strongly on the complexity of the estate, determined mainly by total value as well as diversity and type of assets held, lifetime gifts made, the relationship between family members and whether good records have been maintained during lifetime. Moreover, the multiplicity of reliefs that can be claimed both during lifetime and death and the allocation of the nil rate band can generate considerable complexity. Of these, the only points relevant to a wealth tax (assuming a simple design without reliefs) would be the total value as well as diversity and type of assets held.

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<sup>15</sup> Again, note that there were 6,330 ATED liable declarations and 19,670 ATED relief declarations in the tax year 2018–19 (HMRC, 2020a).

<sup>16</sup> In *Tysim Holdings Ltd v HMRC*, FTT [2019] UKFTT 606 the company owned by a non-resident individual had made late payments of ATED for the years 2015–16, 2016–17 and 2017–18 on 20 December 2017. HMRC had imposed penalties against which Tysim Holdings Ltd appealed. The company argued that it had not been aware of its obligations under ATED until November 2017 and that it had a reasonable excuse. The Tribunal rejected the appeal and considered that an investor holding an interest in real property in a foreign country was expected to take steps to ensure that they were aware of changes in the law of that country.

Activities such as identification and valuation of assets and liabilities, as well as the recording and then calculation of lifetime gifts, contribute to the administrative costs to a very large extent. Disputes over wills are burdensome as well, but they occur less frequently in the experience of the firms we contacted. Valuation is particularly costly if the deceased was a shareholder of a private company or if multiple valuations for properties need to be obtained. Fine art is another asset category that is cumbersome to value (see Tennant, 2020). Although costs of wealth tax valuation in the context of art could be greatly eased by giving a small exemption per item for household goods (as occurs in most other countries), that could still leave problems for higher value fine art and similar items. One partial solution is to take the last acquisition value if the transaction has been carried out in the last five years. The costs of property valuation for a standard home are of similar magnitude as the cost of formal valuation reports cited above – roughly between £1,500 and £3,000 per property. More valuable and complex properties can cost much more than that, up to around £10,000.<sup>17</sup> Valuing private company shares is usually more expensive, with the costs depending on the contracted firm and the complexity of the valuation as well. Smaller firms may charge as little as £2,500 for very straightforward cases whereas complex valuations may well cost up to £25,000. Generally, this comprises valuing the entire firm and then assigning a value to the individual shareholder, including dealing with issues such as minority shareholding. In principle, the wealth tax could have an advantage over IHT in so far that the company only needs to be valued once, which produces the biggest share of the valuation costs, and this value could be used for assessing the share value of all shareholders that are subject to the wealth tax.<sup>18</sup>

In addition to their regular costs, valuation of property, fine art and private company shareholding may occasionally lead to disputes between the tax authority and taxpayers or the firms representing them. Other reasons for disagreement include the level of discounts for minority shareholding, availability of reliefs, and calculation of the tax especially where there is grossing or double grossing up.<sup>19</sup> Of the roughly 25,000 taxpaying estates that HMRC deals with per year, about 5,500 are investigated, i.e. between one fifth and one quarter.<sup>20</sup> These disputes are generally resolved within 12 months from opening to closure. Some tax practitioners note that, in their experience, it usually takes between one and three years to settle these enquiries on a largish estate, depending on the complexity of the issue. Since they deal with the most difficult cases, it should probably be no surprise that this timescale is longer than that of the average dispute. The costs of resolving disputes incurred by taxpayers, including valuation fees, can easily be £10,000 or above. In particularly protracted cases, the timescale can exceed three years considerably and the costs may well be much higher than £10,000.

Appendix B in Troup et al. (2020) provides a systematic overview of probate costs and timescales for the leading private client firms in the UK.<sup>21</sup> Abstracting from straightforward

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<sup>17</sup> See Mackie (2020) for more information on valuing commercial and residential real estate.

<sup>18</sup> For more detailed information on the valuation of private company shares, see Nelder (2020).

<sup>19</sup> A brief explanation by HMRC of how grossing up works is available here: <https://www.gov.uk/hmrc-internal-manuals/inheritance-tax-manual/ihtm26122> [accessed on 16 November 2020].

<sup>20</sup> The annual numbers of taxpaying estates passing on death are reported in the Inheritance Tax Statistics (HMRC, 2020b). The numbers of IHT investigations in the past tax years are available here: <https://www.ftadviser.com/pensions/2019/07/22/hmrc-investigates-iht-in-quarter-of-estates/> [accessed on 25 November 2020].

<sup>21</sup> According to informal discussions with HMRC, IHT compliance is not always delegated to professional agents, so probate fees are not incurred in every case. However, because the extent of compliance efforts of laymen is difficult to assess and value, the discussion in this section will focus on professional fees. How much this affects the implications for a wealth tax depends on the exemption threshold.

cases, the mean timescale applying for the grant of probate is between three and seven months among the included firms. Duration from grant of probate to completion of the process is another 6–14 months, resulting in a total administration timescale of 9–21 months. Averaged over all firms that express fees as a percentage of estate value, probate costs range between 1.9% and 2.8% of the gross value of the estate. Ignoring simple cases, average costs in absolute terms are £22,800 for medium complex estates up to £68,700 for highly complex estates. For simple cases, the total timescale is generally 3–12 months and costs are between £3,000 and £12,000. As these figures refer to the top UK private client firms that usually handle the most complex and high-value cases, the reported costs are presumably higher than the average probate fees.

Probate is a complicated process that involves activities serving the purpose of IHT compliance, such as form filling, valuing assets, providing legal advice and solving disputes with HMRC, as well as activities that are unrelated to taxation, such as applying for probate, verifying the beneficiaries, liquidating assets and settling liabilities, solving disputes over wills and distributing the estate. Another important task, serving both IHT compliance and non-tax-related purposes, is the identification of all assets and liabilities of the deceased. This is generally a much easier and less costly endeavour if there is a living taxpayer helping with the identification process. Further, IHT is a quite complex tax and filing IHT returns can involve many long and complicated forms.<sup>22</sup> A comprehensive wealth tax would apply fewer reliefs than IHT and cumulation of past lifetime gifts would be irrelevant as well, which should reduce compliance costs considerably. Thus, a substantial share of probate costs is not relevant for compliance with a wealth tax.

Troup et al. (2020) assume that at least half of the administrative activities related to probate would be required for compliance with a wealth tax. On this basis, they conclude that taxpayer costs could range between 1% and 1.5% of total assets in the first year of levying a wealth tax, due to their estimate that probate costs are typically 2–3% of estate value. However, note that this range for probate costs is the estimate given average timescales of 9–21 months. As the Office of Tax Simplification (OTS) (2018) notes in the *Inheritance Tax Review*, in a sample of about 800 estates provided by HMRC, ‘on average an inheritance tax form was filed, and a payment of tax made, within four months of the death’. Further, the review states that around 10% of payments were made after the deadline for IHT payments of six months. Based on the observation that the average timescale of IHT compliance is three to four times lower than the midpoint of the range of 9–21 months declared by the top private client firms for probate, we think that 0.6–0.7% is a more realistic estimate of the average compliance costs for IHT as a share of estate values. Since a well-designed wealth tax would be much simpler, the compliance costs should be significantly lower. Even the conservative assumption that half the costs of IHT compliance are incurred in the case of a wealth tax implies that administrative costs to taxpayers are around 0.3% of chargeable wealth. Thus, it appears that a more representative estimate of wealth tax costs derived from the experience of IHT would be in the range of 0.1–0.5% of total assets for most taxpayers. The evidence from other countries described below suggests that taxpayer costs could be considerably below this range.

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<sup>22</sup> For a detailed analysis of the complexities of IHT as well as recommendations for reform, see the IHT Review produced by the Office of Tax Simplification (2018, 2019). The various forms for IHT are available here: <https://www.gov.uk/government/collections/inheritance-tax-forms> [accessed on 23 November 2020].

There are two potential explanations why the figure in Troup et al. may be an overestimate for the majority of taxpayers. First, given the many differences between the probate process and compliance with a wealth tax discussed in the paragraph above, the assumption that ‘at least half’ of the administrative activities related to probate apply to a wealth tax as well seems conservative. Second, the estimate of probate costs in Troup et al. is based on the experience of the top law and accounting firms where we could expect to find the most complex and expensive cases, so they are likely to be an upper bound, as described earlier.

The estimates based on the evidence from IHT are for the costs that would be incurred in the first year of operation of an annual wealth tax, or for a one-off wealth tax. Such costs would certainly fall in subsequent years under a recurring wealth tax due to repeated filing and economies of scale in compliance activities, although the cost savings depend on the mandated interval of revaluation and the extent of change in the asset composition of taxpayers. As mentioned before, an important predictor of compliance costs related to IHT is whether good records have been maintained during lifetime. An annual wealth tax would avoid this cost-driver, at least after the first year, by establishing a reliable, periodic filing process.

## International experience

Additional evidence on the costs of administering a wealth tax to taxpayers comes from the experience with wealth taxes in other countries. However, there are only a few data points since compliance efforts of taxpayers are often difficult to quantify.

In Germany, where a wealth tax was imposed until 1996, the administrative cost of the wealth tax for taxpayers was estimated to be around 12.3% of the wealth tax raised, although it is not well documented what underlying activities account for these expenses (Spengel et al., 2013).<sup>23</sup> At the time of this assessment, the wealth tax rate for natural persons was 0.5% (Rehr, 2020), which suggests that the administrative costs to taxpayers represented around 0.06% of taxable wealth.

In a more recent peer-reviewed study based on a microsimulation model using data from the German Socio-Economic Panel (SOEP) adjusted for top wealth concentration, Bach, Beznoska and Steiner (2014) estimate that the compliance costs to taxpayers induced by the reintroduction of the German wealth tax would be much lower, between 0.6% and 3.6% of the wealth tax due, depending on design choices regarding personal allowance, child allowance and specific allowance for business property. Using the flat annual wealth tax rates between 0.4% and 0.9% underlying the simulations, the costs can be expressed as a percentage of taxable wealth. This calculation implies that the administrative costs to taxpayers represent 0.005–0.02% of taxable wealth. The variation in the costs across the different simulations are mainly explained by the different number of taxpayers that are subject to the wealth tax depending on the allowances.

Based on a small sample of individuals subject to the Irish wealth tax, Sandford and Morrissey (1985) find that average compliance costs of taxpayers, as directly observed in the form of professional fees, were as high as 18.5% of wealth tax revenue. Given that the Irish wealth tax

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<sup>23</sup> Note that after reunification, the German wealth tax was not imposed on the jurisdictions formerly part of the German Democratic Republic until its repeal because of a special provision (Rehr, 2020).

applied a single rate of 1% (Sandford and Morrissey, 1985), the compliance costs were around 0.19% of taxable wealth. Despite its significant magnitude, this value is a lower bound for the total taxpayer costs as only directly observable expenses are included. However, note that the Irish wealth tax was only levied between 1975 and 1978. Had the tax been in place longer than this three-year period, the administrative costs would undoubtedly have fallen over the next years (Sandford and Morrissey, 1985), but it is very hard to assess what share of the initial cost would have faded in the long run. Furthermore, Sandford and Morrissey (1985) show that compliance costs among taxpayers are distributed regressively, which is in line with the patterns observed for current UK taxes such as ATED. The reasons are that taxpayers marginally above the exemption threshold pay very little tax but incur sizeable administrative costs and that there are economies of scale in compliance efforts. This is likely a reflection of the fixed cost nature of filing returns and valuing property.

The United States has never levied a comprehensive annual wealth tax. However, rapidly rising income and wealth inequality has sparked a debate about the introduction of a wealth tax. Most prominently, during the 2020 Democratic Party presidential primaries, candidates Bernie Sanders and Elizabeth Warren presented policy plans to impose an annual wealth tax with high rates on very affluent taxpayers.<sup>24</sup> In an effort to evaluate the desirability of a wealth tax in the U.S. context, Leiserson (2020) uses information on deductible expenses from estate tax returns in 2017 that report gross estate above \$20 million to estimate that compliance costs to taxpayers would amount to around 0.3% of total assets. Assuming a tax rate of 2% on wealth above \$25 million for married couples and \$12.5 million for individuals, Leiserson (2019) provides an estimate for administrative costs to taxpayers of 19% of wealth tax revenue. Comparing this figure to compliance costs due to federal income tax in the U.S., which Marcuss et al. (2013) estimate to be a little over 10% of the tax take, suggests that the administrative costs to taxpayers from a wealth tax could be almost twice as high as from income tax.<sup>25</sup> Note that a higher wealth tax rate would mechanically lower the ratio of taxpayer costs to tax revenue, because the estimate in Leiserson (2020) is ultimately based on compliance costs for the estate tax in percentage of the gross value of the estate.

Finally, it is worth mentioning that the observation of substantial costs for administering a wealth tax extend beyond the context of high-income countries. In India, the administrative costs of the wealth tax for both taxpayers and the tax authority were believed to be high as well, contributing to its abolition in 2015 (Ta and Vanvari, 2020).

## Conclusion on costs to taxpayers

To assess the magnitude of compliance costs that taxpayers incur in the case of a wealth tax, this section has presented evidence from UK taxes on wealth and wealth taxes in other countries – both in absolute numbers in the form of professional fees for compliance activities and relative to taxable wealth or wealth tax revenue raised.

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<sup>24</sup> For a further examination of wealth tax proposals in the U.S., including the costs of administration, see Scheuer and Slemrod (2020).

<sup>25</sup> Marcuss et al. (2013) consider their estimate to be a lower bound because it does not account for compliance efforts related to information reporting and income tax withholding.

Considering the overall evidence from existing UK taxes on wealth and from international experience, our central estimate for the costs of administering a well-designed wealth tax for taxpayers is 0.1% of taxable wealth. The lower bound is likely around 0.05% of taxable wealth, which is similar to taxpayer costs for ATED, which is in principle a simpler charge to administer than a wealth tax although a broad-based wealth tax could avoid some of the costs incurred due to disputes over reliefs, and the wealth tax in Germany where costs were reduced due to the fact that real property did not have to be valued regularly. The upper bound is assumed to be about 0.3% of taxable wealth which is consistent with our interpretation of the evidence on IHT compliance as well as the estimate for a wealth tax in the U.S. by Leiserson (2020) that is based on estate tax data. Given that this upper bound is above the estimate for the Irish wealth tax, that was levied before digitisation helped to reduce administrative efforts and is generally considered to be an expensive charge, this is likely a conservative figure.

It is important to note that these numbers provide estimates for the average costs to taxpayers without attempting to assess how the costs vary by individual wealth. Taxpayer costs as a percentage of total assets could increase with individual wealth (in percentage terms) because assets that are hard to value are held more frequently by wealthier individuals, but they could also decrease due to the fixed cost element of filing and valuations.

The evidence from probate and IHT in the UK suggests that the taxpayer costs could be significantly higher than the estimates based on international experience. But, as argued earlier, because of the complexities of IHT, the fact that many activities necessary for probate and IHT compliance would not be relevant for a wealth tax and the presumed selection bias of the estimate that is based on the fees of the top private client firms in the UK, the figure provided by Troup et al. is likely to be an upper bound, not a representative estimate. Accordingly, we think that the international experience with a wealth tax provides a more appropriate reference point than probate fees in the UK.

Depending on the wealth tax rate, the administrative costs to taxpayers may still be significant compared to the wealth tax due. For illustration, assuming a 1% wealth tax and costs of 0.1% of taxable wealth, taxpayer costs represent 10% of the charge. In this example, the ratio of taxpayer costs to wealth tax due is lower but of similar order of magnitude as the historical estimates for the wealth taxes in Germany and Ireland. Moreover, it is consistent with the current cost figures for ATED which are likely to be higher for properties in the lower value bands and lower for properties in the higher value bands.

Regarding the fees for the main compliance activities, which are (i) form filling, (ii) valuing assets and (iii) providing legal advice and solving disputes, two things can be noted. First, the efforts and costs for form filling and legal advice in the case of a well-designed, broad-based wealth tax would probably be higher than for ATED but lower than for IHT, given the simplicity of ATED and the complexity of IHT. Second, valuation costs are likely to be higher than for both ATED and IHT as ATED only applies to a single asset and IHT applies a lot of reliefs to assets that are difficult to value. To indicate an order of magnitude based on the evidence presented above, a reasonable range for the costs of (i) form filling for a mid-sized, rather simple estate would be from £1,500 to £3,000 for a well-designed wealth tax. (ii) Valuation costs depend on the asset. A formal property valuation will probably cost between £1,500 and £3,000 for a standard home. Valuation costs could increase up to £10,000 for more valuable and complex properties. The valuation of private company shares is more expensive and may cost anywhere from £2,500 to £25,000. However, as shown before, hard-to-value assets such as unlisted shares become a significant portion of wealth only at very high levels of wealth. The costs of resolving disputes

are only incurred by a fraction of all taxpayers, with the exact number depending on the compliance morale and the frequency of investigations by HMRC (as noted above, 20–25% of IHT tax returns are investigated by HMRC). The additional costs for taxpayers due to legal advice and resolving disputes can be in the thousands of pounds and beyond £10,000 in the most protracted cases. Given the uncertainty about the average costs of each of these activities, it does not seem sensible to sum up these activities to provide a point estimate for the absolute administrative costs for the average taxpayer.

There are many factors that drive variation in the costs of these activities: size of the estate, because larger estates include more individual assets and cover a broader range of asset types; complexity of the estate; compliance morale, as providing imprecise valuations can lead to larger costs later if the return is challenged by the tax authority; availability of advice, e.g. because taxpayers at the very top of the wealth distribution work with family offices that provide the listed services on a permanent basis, implying that there is only little additional cost if any. Glucksberg and Burrows (2016) report that multi-family offices start to become relevant when families own total wealth of above \$100 million whereas single-family offices begin to matter for families with wealth above \$250 million.

Providing estimates for the administrative costs is a difficult and somewhat speculative endeavour as they inherently depend on the design of the wealth tax. A range of design choices could contribute to reducing administrative costs to taxpayers. Compliance could be simplified by integrating the wealth tax with the rest of the tax system, for example through coordination with the income tax by including the wealth tax on the annual tax return forms or at least aligning the timing.<sup>26</sup> Other countries that have or have had a wealth tax, such as France, Switzerland and Spain, follow similar approaches. This also helps to alleviate the problem with ATED that taxpayers benefitting from a relief do not know that they still have to file a return and then incur hefty penalties. Moreover, form filling should be digitised – the self-assessment system for income tax in the UK is generally considered to function well and could serve as an example. In Norway, filing wealth tax returns is particularly efficient because the forms are fully digitised and prefixed with information on the wealth tax base provided by banks, listed and unlisted companies (third-party information). Banding is an interesting option as well because it may reduce some costs of valuation since the assessed value is allowed to be less precise if you obviously fall within the middle of the band. If the wealth tax were effectively capped (with a fixed charge for the top band), then this could reduce the administrative costs to almost nil for the wealthiest individuals who knew that they were above the upper band and therefore subject to the cap. On the other hand, such an approach would introduce an element of regressivity in the tax schedule at the top, limit the revenue received, and only benefit the tiny number of individuals above the cap. Finally, the mandated interval for revaluations affects compliance costs considerably. Determining the optimal frequency of valuation updates requires balancing the trade-off between precision of valuations and associated compliance costs.

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<sup>26</sup> Notice that around one-third of individual taxpayers in the UK already file an income tax self-assessment return – generally individuals with income not subject to withholding tax or for whom it is difficult to compute the correct amount of withholding tax. This group includes ‘self-employed individuals, those with incomes over £100,000, company directors, landlords, and many pensioners’ (Advani, Elming and Shaw, 2019). Thus, it is likely that most individuals that would be subject to a wealth tax already file self-assessment returns.

### 3. Costs to the tax authority

This section aims to shed light on the costs of administering a wealth tax for the tax authority. The administration, collection and enforcement of a wealth tax can involve various activities on the part of tax authorities, including but not limited to processing forms, producing and examining valuations, conducting audits and going to litigation. Technically, we consider all costs incurred by government agencies that are related to the routine administration of a wealth tax, even if an agency is not institutionally part of the tax authority.

Following the same structure as the previous section, the first subsection discusses insights from existing UK taxes on wealth, whereas the second subsection presents information obtained from tax administrations in countries that impose or have imposed a wealth tax as well as evidence from the literature.

#### Experience from UK taxes on wealth

A useful starting point for assessing the administrative costs of a wealth tax to the tax authority (HMRC) in the UK context are official statistics on the costs of administering existing taxes – in particular taxes on wealth such as IHT. HMRC (2019) reports total revenue of £628 billion in the tax year 2018–19. The administrative costs of HMRC totalled £4 billion during the same period. Hence, taking into account all taxes, the administrative costs to the tax authority amounted to 0.52% of total tax revenue (HMRC, 2019). The administrative burden is not equally distributed across individual taxes. According to information provided by HMRC (Troup et al., 2020), the annual costs of administering IHT are £35 million. Expressed as a proportion of the IHT revenue of £5.3 billion, the administrative costs make up 0.66% of the IHT take – not much more than the overall average cost share. For comparison, collecting income tax (through self-assessment and pay as you earn) costs 0.72 pence, corporation tax costs 0.60 pence, national insurance contributions cost 0.18 pence and VAT costs 0.58 pence per pound of tax revenue, (HMRC, 2019).

In the most recent period for which full data are available, the total number of taxpaying estates passing on death in 2017–18 is 24,200 (3.9% of all UK deaths) with a total net capital value of £27.3 billion (HMRC, 2020b). This suggests that the administrative costs of IHT on part of HMRC are about £1,450 per taxpaying estate – well-invested expenses for an average IHT liability of £197,000. Putting the administrative costs for IHT into relation to the total net value of taxpaying estates, they amount to 0.13% of wealth subject to IHT.<sup>27</sup> Considering not only taxpaying estates but the total net capital value of all estates for which IHT returns are filed which is £95.2 billion, administrative costs represent around 0.04% of estate wealth. Although the non-taxpaying estates are typically of lower value, they presumably still generate some administrative costs for HMRC, so it is *a priori* not clear whether the total net value of all IHT-filing estates or all taxpaying estates is the more appropriate denominator. Because of all the reliefs from IHT, it is inherently difficult to choose the right denominator to put the

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<sup>27</sup> Note that this number expresses administrative costs as a percentage of *chargeable wealth*, i.e. including the asset values below the exemption threshold. As the standard IHT rate is 40% (only a small fraction of estates is charged at the reduced 36% rate, see HMRC, 2020b, Table 12.2), administrative costs represent around 0.26% of *taxable wealth*.

administrative costs in relation to the associated asset values. This complicates the comparison with a broad-based wealth tax levied on the same segment of the population as these exemptions would not be applicable.<sup>28</sup> Adding exempted assets such as pensions and business wealth to the IHT base would result in higher valuation costs while eliminating the need to police reliefs. It is likely that the increase in valuation costs would dominate on average, so the administrative costs would increase as a result. However, estimating the precise effect on the magnitude of administrative costs requires an extensive modelling exercise which is beyond the scope of this paper.<sup>29</sup>

## International experience

Additional information on the costs of administering a wealth tax for the tax authority comes from other countries that levy a wealth tax or have done so in the past. Official statistics on the administrative costs of the wealth tax have been surprisingly difficult to obtain, even for countries that currently levy a wealth tax. Thus, this section combines information from government statements, from the literature on wealth taxes and from tax administrations in countries that still have a wealth tax – Norway, Spain and Switzerland – which we contacted and asked directly for information on administrative costs.

In France in 2016, before the wealth tax ('impôt de solidarité sur la fortune', ISF) was abolished and replaced by a tax on residential property ('impôt sur la fortune immobilière', IFI, established in 2018), total administrative costs for the tax authority amounted to close to €103 million.<sup>30</sup> The total costs can be decomposed into €35.3 million for management (includes activities such as valuation, collection and litigation) and €67.6 million for 'control' (includes activities such as enforcement and tax audits). These costs consist of payroll expenses for all jobs directly and indirectly involved in collecting the wealth tax as well as the share of operating costs, such as property or IT, attributed to the administration of the wealth tax. Administrative costs as a percentage of wealth tax revenue were 2.07%.<sup>31</sup> In comparison, the ratio between administrative costs and the respective tax revenue was 1.8% for income tax and 2.52% for dwellings tax. Thus, the administrative efforts related to the wealth tax were not significantly higher than for other major taxes. For illustrative purposes, the administrative costs can also be computed per wealth tax payer using the information that there were 351,152 wealth tax returns filed in 2016, resulting in total wealth tax revenue of €5,051 million (DGFIP, 2017). This exercise suggests that administrative costs per wealth tax return were around €290, while the average wealth tax payment was about €14,400. Given that net chargeable assets were about €986,556 million in 2016, the administrative costs for the tax authority represent 0.01% of

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<sup>28</sup> Chamberlain (2020) examines the design of the wealth tax base, concluding that a wealth tax should, in principle, cover all types of assets.

<sup>29</sup> Advani, Hughson and Tarrant (2020) assess the effect of broadening the IHT base on administrative costs, tax revenue and estate values.

<sup>30</sup> This official information on the administrative costs of the French wealth tax (ISF) was provided by the Minister of Public Action and Accounts in response to a formal enquiry in the French Senate in June 2019. Available: <https://www.senat.fr/questions/base/2019/qSEQ190209168.html> [accessed on 18 September 2020].

<sup>31</sup> To be precise, this is the ratio between administrative costs and gross yield of the wealth tax without adjusting for tax refunds.

chargeable wealth.<sup>32</sup> Note that this number may understate the magnitude of the administrative costs because the figure for net chargeable assets provided above does not account for some of the numerous reliefs that were applied under the French wealth tax. However, the administrative costs for the tax authority are bounded at 0.03% of *taxable wealth* when accounting for the reliefs because this number would imply that the average wealth tax rate was equal to the top marginal wealth tax rate of 1.5%.<sup>33</sup>

The reported ratio between administrative costs and wealth tax receipts in France of 2.07% in 2016 is somewhat higher but still consistent with the 1.6% in 1997 reported by Pichet (2007). Similarly, collection costs for the wealth tax as percentage of wealth tax revenue were just a little above the total administrative costs that amounted to 1.4% of total tax revenue in France in 1997 (Pichet, 2007).

In Germany, the administrative costs of the wealth tax that was discontinued in 1996 have been controversially discussed, with estimates strongly varying in magnitude.<sup>34</sup> The federal government estimated that the costs of administration as a percentage of wealth tax revenue raised amounted to 4–4.5% (Rehr, 2020). However, this figure does not include the costs of property value determination, so the true costs should be higher. Bauer (1988) estimates a ratio of 10.8% when attributing 20% of the administrative efforts that also serve property tax and local business tax, in particular activities related to assessment of the tax base, to the wealth tax.<sup>35</sup> For comparison, Bauer (1988) estimates that, taking into account all taxes, the ratio between total administrative costs to the tax authority and total tax revenue was 1.87% in 1983. Other studies conclude that the costs of administering the wealth tax for the tax authority could have been as high as 20% of wealth tax revenue, although the underlying assumptions are not well documented (Spengel et al., 2013). Multiplying again each estimate with the relevant wealth tax rate for individuals at the time, which was 0.5% in 1978–1994 and 1% in 1995–1996 before the wealth tax was discontinued (Rehr, 2020), implies that the administrative costs amounted to around 0.04–0.1% of taxable wealth.

In contrast, the aforementioned peer-reviewed study by Bach, Beznoska and Steiner (2014) estimates that the administrative costs for the tax authority of a potential German wealth tax could be as low as 0.2–1.4% of wealth tax raised, depending on the magnitude of personal allowance and child allowance. Revenue losses from valuation corrections for real estate could add 1.9–4.1% of wealth tax revenue to the costs. Adding up these two costs incurred by the tax authority and applying the underlying flat annual wealth tax rates of 0.4–0.9% implies that the administrative costs of the tax authority represent about 0.015–0.03% of taxable assets. These estimates are lower than the historical evidence from Germany but very close to the official

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<sup>32</sup> Detailed statistics on the number and assets of French wealth tax payers between 1999 and 2017 are available here: <https://www.impots.gouv.fr/portail/statistiques> [accessed on 18 November 2020].

<sup>33</sup> The French wealth tax applied a progressive schedule with rates of 0.5–1.5%. Thus, the effective average tax rate cannot have been higher than 1.5%. Note again that assets subject to reliefs might still produce administrative costs for the tax authority, so the administrative costs of 0.01% of chargeable wealth are an informative estimate in any case. For more information on the French wealth tax, see Dupas (2020) and Tirard (2020).

<sup>34</sup> For a more extensive discussion of the administrative costs of the German wealth tax, see Rehr (2020) and Spengel et al. (2013).

<sup>35</sup> Of the remaining 80% of common administrative costs, 50% are allocated to property tax and 30% are attributed to local business tax. Spengel et al. (2013) argue that this assumption places too little of the administrative burden on the wealth tax.

statistics on the French wealth tax in 2016 which suggests that they are not unrealistic in modern-day tax systems.

The work on the Irish wealth tax by Sandford and Morrissey (1985) also provides a rough estimate of the administrative costs for the revenue equalling 14% of the wealth tax take. Applying again the flat tax rate of 1% implies that these costs represent 0.14% of the tax base. The conjecture that the administrative costs might have been lower in the long run applies in this case as well. However, Sandford and Morrissey (1985) report that the administration of the wealth tax was not adequately staffed, which might have kept the administrative costs to the revenue low while increasing the compliance costs for taxpayers.

In response to our enquiries, the tax authorities in the OECD countries that currently levy a wealth tax – Norway, Spain and Switzerland – have only been able to provide indicative evidence on the costs of administering the wealth tax.<sup>36</sup>

The Ministry of Finance in Norway did not have separate reports on or estimates of the costs of administering the wealth tax, although administrative costs are taken into account when evaluating tax reforms. Furthermore, the ministry confirmed that the wealth tax causes more challenging valuation issues than other taxes, both for taxpayers and the tax authority. To reduce administrative costs, Norway has introduced a system for the valuation of real estate that is almost automatically updated from year to year. The development of this system entailed high one-off costs but was able to reduce ongoing running expenses. However, taxpayers can dispute the official valuation if it exceeds the documented market value, which has generated new costs. The assessment of most assets other than real estate relies on third-party reporting that is used to prepopulate the self-assessment tax returns. Unlisted firms declare the firm value for wealth tax purposes in their business tax return. The tax value is somewhat formulaic based on the balance sheet, but special reporting is needed for commercial property. Goodwill and self-developed patents are explicitly exempted from the firm value for wealth tax purposes. If all these systems are in place, the running costs of administering a wealth tax do not seem to be extraordinarily high. In short, with a combination of exemptions and some formulaic valuations, ongoing costs may be kept relatively low.

Because the wealth tax in Switzerland is collected only at the sub-national level, i.e. by cantons and municipalities, the Swiss Federal Tax Administration does not have information on the administrative costs.<sup>37</sup> The federal political system of Switzerland grants extensive financial and fiscal autonomy to cantons and partially to municipalities and does not prescribe standardised accounting models. We contacted the tax authorities in all 26 Swiss cantons to enquire about the administrative costs associated with the wealth tax. Most cantonal tax offices declared that they do not produce statistics on the costs of administering the wealth tax. The main reason for this lack of information is that the processes to administer the income tax, the wealth tax and the refunding of the withholding tax are tightly entangled, so a precise attribution of costs to individual taxes is difficult and might not be informative. However, the qualitative and

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<sup>36</sup> Spain's central government declared that they do not have information on the collection costs of the wealth tax, because its administration is largely delegated to the regions. The responses of the regional governments to our enquiries are pending.

<sup>37</sup> For a more detailed description of the institutional features of the Swiss wealth tax, see Eckert and Aebi (2020).

quantitative information provided by the cantonal tax offices sheds light on the administrative burden of the Swiss wealth tax.

According to the cantonal tax administrations, the administrative effort for the joint assessment of income tax and wealth tax is mainly spent on examining taxable income and the numerous deductions, such as commuting costs, pension account contributions and child benefits. Most activities needed to administer the wealth tax serve other purposes as well. Collecting and checking information on taxable assets, which in the case of financial products leads to the compilation of a comprehensive list of securities, serves as a plausibility check of capital income flows that are subject to income tax. Moreover, Switzerland levies income tax on imputed rents, so valuing property is necessary for this purpose anyway. This supporting role of wealth tax in the enforcement of income tax is quantitatively important since receipts from income tax are many times higher than from wealth tax.<sup>38</sup> In addition, determining the value of securities is important for refunding the withholding tax.

Given this overlap in administrative activities, several cantonal tax authorities have pointed out that the assessment of the wealth tax is merely a by-product of these processes. Most of the administrative workload for the wealth tax – gathering personal data in the tax register, processing forms, sending out assessments and invoices, enforcement and collection of payments – is incurred anyway. Only rarely are additional checks carried out that only serve the purpose of the wealth tax.

Despite the general lack of official statistics, some cantons have provided data on the administrative expenses for the wealth tax. The canton of Aargau (population of around 690,000 in 2020)<sup>39</sup> estimates that 30 full-time equivalents (FTE) are tasked with the administration of the wealth tax. In 2016, the latest year for which data are available, wealth tax revenue collected by the canton and municipalities was 282 million Swiss francs.<sup>40</sup> At the same time, taxable wealth amounted to 79,002 million Swiss francs. The total number of taxpayers in the canton of Aargau, who must all declare their assets on the tax return in the Swiss system even if their wealth is negligible, was 375,111. For illustrative purposes, we can do a back-of-the-envelope calculation assuming an average wage of 60,000–120,000 Swiss francs among the personnel administering the wealth tax. Adding overheads of 60–80% on top of salaries results in operating expense of 2.88–6.48 million Swiss francs. Thus, this rough calculation suggests that the costs of operating the wealth tax in the canton of Aargau represent 0.004–0.008% of taxable wealth and 1.0–2.3% of wealth tax revenue. Put in relation to the total number of taxpayers, the average cost per taxpayer is 8–17 Swiss francs, compared to average wealth tax payments of about 750 Swiss francs. The tax office at the canton of Aargau notes as well that part of the costs of assessing wealth would be incurred anyway for the purpose of enforcing the income tax, so this is an upper bound.

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<sup>38</sup> Taking into account all state levels (federal, cantonal and municipal), income tax revenue is about seven to eight times higher than wealth tax revenue in Switzerland in 2017. For some cantons, this ratio can be ten or above. See the annual report on Switzerland's financial statistics for more information. Available: <https://www.bfs.admin.ch/bfs/en/home/statistics/general-government-finance/tax-system-receipts/receipts.assetdetail.10287487.html> [accessed on 10 November 2020].

<sup>39</sup> Population data for Switzerland from the Federal Statistical Office are available here: <https://www.bfs.admin.ch/bfs/en/home/statistics/population.html> [accessed on 23 November 2020].

<sup>40</sup> These figures only consider taxpayers who are resident in the canton of Aargau. Including non-resident taxpayers results in wealth tax revenue of around 291 million Swiss francs in 2016.

The canton of Ticino (population of around 350,000 in 2020) reports aggregate figures for the joint taxation of income and wealth. In Ticino, about 200 FTE are employed for the administration of the income tax and the wealth tax, resulting in payroll costs of around 18 million Swiss francs. Licensing and maintenance for computer software needed for the assessment of the income and wealth tax cost an additional 5.8 million Swiss francs. Income tax receipts total about 1.9 billion Swiss francs while wealth tax revenue amounts to 255 million Swiss francs.<sup>41</sup> These numbers suggest that the joint administrative effort for income tax and wealth tax (payroll and IT costs) represents 1.1% of the intake in the canton of Ticino. This calculation includes the revenue from the federal income tax because its assessment and collection are almost entirely carried out by the cantons.<sup>42</sup> The cost estimate from the canton of Ticino is consistent with the information from the canton of Aargau reported above.

## Conclusion on costs to the tax authority

Drawing conclusions on the magnitude of administrative costs to the tax authority from the evidence presented above ought to be done carefully, given the significant variation in policy features, size of jurisdiction and period during which the wealth tax was imposed. Tax systems have evolved considerably over recent decades. The automation and digitisation efforts undertaken have contributed to improvements in administrative efficiency, as the Norwegian and Swiss models show.

Although the experience with the Irish wealth tax levied in 1975–1978 suggests that a wealth tax may produce very substantial administrative costs, the short period during which it was levied and the improvements in administrative efficiency over recent decades raise doubts whether these costs are accurate reference points for a wealth tax in the UK if it were implemented today. The overall evidence suggests a central estimate for the administrative costs of a modern wealth tax for the tax authority of about 0.05% of taxable wealth. As a lower bound, we think the costs could potentially be as low as 0.01% which is the order of magnitude of the corresponding figure for the French wealth tax. Notably, the administrative costs as a share of taxable wealth seem to be even lower for the Swiss wealth tax which has a low threshold and a broad base.<sup>43</sup> The upper bound is likely around 0.1% of taxable wealth, which is at the higher end of the estimated range for the costs of IHT and the German wealth tax, and below but of similar order of magnitude as the costs of the Irish wealth tax. The complexities of IHT and the administrative efficiency gains since the abolition of the wealth tax in Germany and Ireland, as well as the evidence from more recent periods and particularly France and Switzerland, suggest that the administrative costs to the tax authority can be kept below that upper bound.

How much of wealth tax revenue is spent on administering the levy again depends on the tax rate. To illustrate, administrative costs of 0.05% of taxable wealth represent 5% of associated revenue in the case of a 1% wealth tax and 2.5% of associated revenue if the wealth tax rate is

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<sup>41</sup> The tax administration of the canton of Ticino communicated these numbers based on the official cantonal budget for the year 2021.

<sup>42</sup> The Federal Tax Administration has a supervisory and coordinating role for these processes, but these costs are negligible.

<sup>43</sup> Note that the Swiss evidence should be interpreted carefully as data are only available for two cantons and there are no harmonised official statistics on the administrative costs of the wealth tax.

2%.<sup>44</sup> Note that the recent data from France and Switzerland show that the administrative costs to the tax authority account for around 2% of wealth tax revenue raised in both countries, despite imposing average wealth tax rates below 1.5%. These numbers imply that administering the wealth tax likely continues to generate higher costs as a share of associated revenue than other taxes.<sup>45</sup> On the other hand, the administrative efforts for the wealth tax may contribute towards easing the burden of administering and enforcing other taxes, as the example of Switzerland shows. These positive externalities are hard to quantify.

The Swiss model also demonstrates that the wealth tax must be well integrated into the tax system to keep the administrative burden low. Moreover, it is important to automate administrative processes and digitise the filing of tax returns. Establishing extensive third-party reporting can reduce the administrative burden for both taxpayers and the tax authority. The fewer reliefs and exemptions there are, the simpler the forms overall and the fewer boundaries there are to navigate, although it also necessarily means more valuations have to be done which can increase costs.

Finally, it is important to point out that variation in the costs of administering a wealth tax to the tax authority does not just reflect bureaucratic inefficiencies. Rather, more intensive administrative efforts on the part of the tax authority can improve compliance, reduce the tax gap and lower the administrative burden of taxpayers, for example.

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<sup>44</sup> Note that taxable wealth is also affected by the wealth tax rate to some extent because of the induced behavioural responses. Advani and Tarrant (2020) analyse the existing empirical evidence on how individuals react to a wealth tax and provide an estimate of the elasticity of taxable wealth for a well-designed UK wealth tax.

<sup>45</sup> As noted above, the overall administrative costs to the tax authority represented 0.52% of total tax revenue in the UK in the tax year 2018–19 (HMRC, 2019).

## 4. Conclusion

The administration of a wealth tax is a complex endeavour for both taxpayers and the tax authority. The evidence collected and discussed in this paper gives some indication of the likely costs of administering a wealth tax in the UK based on experience with existing UK taxes on wealth and information from other countries that currently levy a wealth tax or have done so in the past.

The presented evidence suggests that the administrative costs are not negligible, in particular for taxpayers. This observation is consistent with the finding from the tax literature that the costs to taxpayers exceed the expenses of the tax authority (Leiserson, 2020). As a tentative conclusion on the administrative costs of a well-designed wealth tax, our central estimate for taxpayer costs is 0.1% of taxable wealth with a lower bound of 0.05% and an upper bound of 0.3% whereas the central estimate for the administrative costs to the tax authority is 0.05% of taxable wealth with a lower bound of 0.01% and an upper bound of 0.1% (see Table 1 below). It is important to note that these figures represent a ‘best guess’ based on the presented evidence, rather than a precise calculation.

Table 2: Estimates for the costs of administering a wealth tax as a percentage of taxable wealth

	Costs to taxpayers	Costs to the tax authority
Lower bound	0.05	0.01
Central estimate	0.1	0.05
Upper bound	0.3	0.1

Notes: Administrative costs of a broad-based, well-designed wealth tax to taxpayers and the tax authority as a percentage of taxable wealth. Costs to taxpayers include professional fees for form filling, valuing assets as well as providing legal advice and solving disputes. Costs to the tax authority include expenses for activities such as processing forms, examining valuations, conducting audits and going to litigation.

Source: Author’s calculations.

It is noteworthy that these figures represent estimates for the average costs as a percentage of taxable wealth. We have not attempted to model precisely how taxpayer costs as a share of taxable wealth vary with total assets. However, we observe that there are two countervailing narratives about how they may be connected. On the one hand, two factors indicate that these costs are likely to decline as a share of taxable wealth. First, this is what we observe under ATED, as shown in section 2 of this paper. Second, it seems very likely that there is a fixed cost element to filing and valuations, with some element of variable cost that may even be capped at the highest levels (i.e. at ‘family office’ levels of wealth). On the other hand, the evidence that the number and value-share of hard-to-value assets tends to increase with total assets is a factor that works in the opposite direction (see Advani, Hughson and Tarrant, 2020). Consequently, we conclude that in the absence of more detailed data on taxpayer costs, it is reasonable to assume that the average cost holds across all taxpayers up to a maximum ‘cap’ represented by the level of wealth at which a taxpayer could be expected to employ permanent staff to manage their wealth, i.e. at family office levels of wealth.

Any sensible policy proposal for a wealth tax ought to balance the potential tax revenue against its potential costs. This comparison reveals what share of the tax take is effectively available for

government spending and what costs are incurred by taxpayers beyond direct tax payments. As it is clearly undesirable to levy a tax which produces costs that surpass its revenue, the costs of administering a wealth tax provide a lower bound for the wealth tax rate to consider.

Expressing the administrative costs as a share of wealth tax revenue requires assuming a wealth tax rate. Adding up the central estimates for the costs to taxpayers and the tax authority reported above and assuming a 1% wealth tax implies that total administrative costs represent 15% of wealth tax revenue raised. Although this is still significant, the overall evidence strongly suggests that the total administrative costs of a UK wealth tax as a percentage of wealth tax revenue could be kept substantially below the historical reference point of 25% estimated by Sandford and Morrissey (1985) for the Irish wealth tax levied in the 1970s. This seems sensible given that technological progress has raised administrative efficiency over recent decades.

In the end, the costs of administering a wealth tax will depend crucially on design choices. A higher exemption threshold tends to reduce costs, because the necessary assessment of wealth would be carried out for a lower number of taxpayers. However, based on the suggestive evidence presented in this paper, Switzerland seems to succeed in operating a wealth tax with low rates, a comprehensive tax base and low exemption thresholds efficiently, incurring only moderate administrative costs.<sup>46</sup> Presumably, Switzerland manages to keep the administrative costs low by integrating the wealth tax well into the tax system, exploiting administrative overlap with other existing taxes and applying formulaic valuation for assets that are hard to value such as business wealth. Another important cost factor is the revaluation interval. If valuation updates are required less frequently, the administrative costs can be reduced, as the experience with ATED demonstrates. Another insight from ATED is that banding may help reduce the costs of valuation because less precision is required. Finally, the example of Norway shows that establishing a digital infrastructure that automates third-party reporting and facilitates digital filing helps to simplify compliance and alleviate the administrative burden for taxpayers and the tax authority.

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<sup>46</sup> Because the wealth tax is only levied at the sub-national level in Switzerland, wealth tax rates and exemption thresholds vary by canton (and municipality to a lesser extent). Depending on the canton, top marginal wealth tax rates are between 0.1% and 1% and exemption thresholds are between 25,000 Swiss francs and 200,000 Swiss francs (Brülhart et al., 2020).

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