On Some Implications of Wealth Taxes on Inequality in India

Economic inequality (income and wealth inequality) in India today is very high compared to international and historical standards. Further, due to low tax-GDP ratio and the resultant low spending on public services the situation of inequality is getting accentuated fast. Reforming the whole set of ‘Wealth Taxes’ can serve the twin purpose of curbing extreme inequality by redistributing income as well as augmenting revenue from direct taxes creating fiscal space for investing in social sector.

Inequality in India:

Globally, it is now increasingly being acknowledged that inequality is bad because it undermines the sustainability of economic growth,\(^1\) leads to slower poverty reduction,\(^2\) compounds the inequalities between men and women,\(^3\) drive inequalities in health, education, life chances\(^4\) etc. and also leads to social and political instability and civil conflict,\(^5\) which further harms the economy. So, this could jeopardise the whole democratic set up of a country. Like many other countries, India is also plagued by various types of inequalities; viz., income inequality, wealth inequality, gender inequality, etc. Oxfam’s constant campaign against the unequal economic order has caught global attention from long past. The most recent report of Oxfam, on the basis of global evidence, proclaims that government is not powerless to tackle various forms of inequalities; and it can be checked and reduced.\(^6\) So, inequality is not inevitable; it is a policy choice.\(^6\)

As far as the wealth inequality is concerned, although estimates of inequality differs across various studies, it is established that inequality in India is high and it is increasing rapidly. The State of World Wealth Report 2013 revealed that during 2000 to 2013, India’s private wealth has reportedly zoomed up by 300 percent – from USD 1.2 trillion to 3.6 trillion; whereas the bottom 70 percent of India’s households owned only about 20 percent of this wealth.\(^7\) The number of billionaires in India increased from only 2 in the mid-1990s to 46 in 2012 and wealth of these constituted 10 percent of India’s GDP in 2012.\(^8\) The number of billionaires has increased further to 111 in 2016.\(^9\)

This has also been resonated in the Credit Suisse report, which shows that the wealth share of top 1 percent in India is soaring. Chart 1 shows that during the period from 2002 to 2017, the wealth share of top 1 percent of population has increased from 23.1 percent to as high as 45.1 percent. The top decile of the population, in 2017, holds 73.3 percent of the total wealth in India, which has increased from 57.0 percent in 2002. As the wealth share of the top strata is increasing; consequently, share of bottom strata is shrinking proportionately out of the total wealth pie.

Chancel and Piketty (2017) have also observed that the share of national income accruing to the top 1 percent population is now at its highest level of 22 percent since 1922.\(^10\) A detailed study done by Anand and Thampi (2016), estimates wealth inequality on the basis of All India Debt & Investment Survey Data, shows that during 1991 to 2002, Gini coefficient\(^11\) of net worth increased marginally from 0.66 to 0.67, whereas, during the next decade (from 2002 to 2012) this coefficient increased substantially and stood at 0.75 in 2012.\(^12\) This implies a rapid increase in concentration of wealth, during 2002–2012, in favour of the top strata of the population. The study also found that the “main sources of these unequal patterns in wealth accumulation were land and buildings.”\(^12\)

Recommendations:

India must restructure the whole set of ‘Wealth Taxes’ and widen the wealth tax base for augmenting direct tax revenue and bring progressivity in the tax system.

Inheritance tax and net wealth tax must be reintroduced to tackle the extreme concentration of wealth.

Rates of various wealth taxes could be moderate and threshold limit could be high; but, there should be least number of exemptions.
To tackle the problem of inequality, ‘redistribution of income through taxation’ is considered as the most effective tool with the government. Among the various types of taxes, a set of direct taxes, known as ‘wealth taxes’ can effectively hit at the root of the problem of inequality. In the absence of wealth or inheritance tax, Thomas Piketty rightly pointed out, the phenomenon of increasing concentration of wealth was very likely manifested in India. In the context of growing social inequity and injustice, wealth taxes could be an option to curb it as well as to generate additional resources. Recently, World Bank, in one of its reports, proclaims that property and inheritance taxes can bring progressivity in tax system and augment revenues. It further helps to limit intergenerational inequality.

It would be noteworthy to mention here that direct taxes are the major sources of the revenue for the governments across the globe. On the contrary, heavy reliance on indirect taxes (66.4 percent of total tax collection in 2015-16) makes the Indian tax system itself regressive. Within the whole set of direct taxes, keeping aside the personal income tax and corporate taxes, there are a gamut of certain kind of taxes, which could be categorised as ‘wealth taxes’ (see the diagram below) and global evidence suggests that a substantial amount of resources could be mobilised through wealth taxes (see table 1). Additionally, along with revenue mobilisation, wealth taxes have a critical role for addressing the problem of wealth concentration or inequality.

**WEALTH TAXES: CONCEPTS**

Wealth taxes, in principle, covers a whole range of assets such as real property (houses and land), personal property such as jewellery, pictures, furniture, cars and boats, stocks and shares, business assets, cash and bank balances, etc. All these assets and related taxes could be classified in the following categories.

**1. ASSET BASE**
- (a) General Wealth Tax - It is a ‘recurrent tax’ on net wealth.
- (b) Special Wealth Tax - It is basically taxes on immovable properties, i.e., property tax.

**2. ASSET TRANSFERS**
- (a) Tax on transferring assets - Inheritance and Gift taxes
- (b) Transaction taxes on land transfer, capital transfer etc.
  These are ‘one time’ taxes.

**3. APPRECIATION OF VALUE**
- (a) Tax on the appreciation of value
  Like, financial assets (bond and securities) and/or real state.

It is evident that wealth taxes encompasses a whole range of assets and consequently, an array of different nature of taxes. Globally, wealth tax across countries comprises of tax on either any one or a combination of more than one forms of wealth mentioned above, namely, possession of wealth, transfer of wealth and appreciation of wealth. For a global comparison, all forms of wealth taxes, in the International Monetary Fund’s (IMF) Government Finance Statistics (GFS) Manual has been categorised under the broad head – ‘Property Taxes’, which subsumes the following taxes.

1. **(a) General Wealth Tax:** It is recurrent taxes on net wealth. It is also known as annual wealth tax/net worth/net wealth tax. In India, it is generally called wealth tax. However, for the sake of avoiding any confusion, it will be termed as ‘net wealth tax’ in the subsequent discussions.

2. **(b) Special Wealth Tax:** Recurrent taxes on immovable property such as Municipal Property Tax, Land Revenue and Tax on non-urban immovable property and property tax by rural local bodies i.e. Panchayats in India;
2. [a] **Tax on Transferring Assets**: These taxes are estate duty, inheritance and gift taxes. Estate duty and inheritance taxes are used interchangeably.

[b] **Transaction Taxes**: These are taxes on financial and capital transactions. Securities transaction tax, and stamp & registration fees in India belong to this category.

3. [a] **Tax on Appreciation of Value**: This is basically non-recurrent, that is, one-time tax on revaluation of capital and property. For example, tax on increase in land value due to any government project in an area. Apart from the aforementioned taxes, GFS also includes property tax, namely, ‘Other recurrent taxes on property.’ For example, tax on cattle, jewellery and other external signs of wealth belongs to the category. So, it is evident that ‘property taxes,’ as defined by the IMF, actually subsumes all forms of wealth taxes. So, in the subsequent discussion, for avoiding confusion, we will term all these different forms of wealth taxes collectively as ‘Wealth Taxes.’ A brief overview of the global experience of wealth taxes will be sketched in this policy brief with a more detailed discussion in the context of India.

**WEALTH TAXES: GLOBAL EVIDENCE**

It is noteworthy that many G20 and BRICS countries have mobilised substantial amount of resources in the form of wealth taxes, as documented in the GFS of IMF. Table 1 shows that countries like United States, Canada, Japan, France, United Kingdom, Argentina etc. had collected substantial amount of tax revenues from wealth taxes over the years. In 2015, France had collected taxes equivalent to 4.22 percent of GDP from various types of wealth taxes, which was 15.4 percent of their total tax collections. Among other high income countries, Canada, United States, Japan and United Kingdom also had collected as much as 14.3%, 13.5%, 12.5%, 12.4%, of total tax revenues, respectively, from wealth taxes.

<table>
<thead>
<tr>
<th>COUNTRY</th>
<th>YEAR</th>
<th>PROPERTY TAX (AS % OF GDP)</th>
<th>TOTAL TAX REVENUE (AS % OF GDP)</th>
<th>SHARE OF PROPERTY TAXES (AS % OF TOTAL TAX REVENUE)</th>
</tr>
</thead>
<tbody>
<tr>
<td>UNITED STATES</td>
<td>2015</td>
<td>2.72</td>
<td>20.12</td>
<td>13.5</td>
</tr>
<tr>
<td>MEXICO</td>
<td>2014</td>
<td>0.30</td>
<td>11.55</td>
<td>2.6</td>
</tr>
<tr>
<td>INDONESIA</td>
<td>2015</td>
<td>0.25</td>
<td>11.98</td>
<td>2.1</td>
</tr>
<tr>
<td>CANADA</td>
<td>2014</td>
<td>3.74</td>
<td>26.13</td>
<td>14.3</td>
</tr>
<tr>
<td>JAPAN</td>
<td>2014</td>
<td>2.42</td>
<td>19.39</td>
<td>12.5</td>
</tr>
<tr>
<td>KOREA</td>
<td>2015</td>
<td>1.55</td>
<td>17.18</td>
<td>8.7</td>
</tr>
<tr>
<td>AUSTRALIA</td>
<td>2015</td>
<td>1.54</td>
<td>26.03</td>
<td>5.9</td>
</tr>
<tr>
<td>GERMANY</td>
<td>2015</td>
<td>0.64</td>
<td>22.92</td>
<td>2.8</td>
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<tr>
<td>RUSSIA</td>
<td>2015</td>
<td>1.15</td>
<td>19.39</td>
<td>5.9</td>
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<tr>
<td>FRANCE</td>
<td>2015</td>
<td>4.22</td>
<td>27.42</td>
<td>15.4</td>
</tr>
<tr>
<td>UNITED KINGDOM</td>
<td>2015</td>
<td>3.31</td>
<td>26.80</td>
<td>12.4</td>
</tr>
<tr>
<td>SOUTH AFRICA</td>
<td>2015</td>
<td>1.66</td>
<td>28.72</td>
<td>5.8</td>
</tr>
<tr>
<td>ITALY</td>
<td>2015</td>
<td>1.63</td>
<td>28.49</td>
<td>5.7</td>
</tr>
<tr>
<td>CHINA</td>
<td>2014</td>
<td>1.60</td>
<td>19.48</td>
<td>8.2</td>
</tr>
<tr>
<td>BRAZIL</td>
<td>2015</td>
<td>1.46</td>
<td>22.77</td>
<td>6.4</td>
</tr>
<tr>
<td>TURKEY</td>
<td>2015</td>
<td>0.37</td>
<td>21.74</td>
<td>1.7</td>
</tr>
<tr>
<td>ARGENTINA</td>
<td>2015</td>
<td>2.85</td>
<td>24.97</td>
<td>11.4</td>
</tr>
<tr>
<td>INDIA</td>
<td>2009-10</td>
<td>0.48&lt;sup&gt;27&lt;/sup&gt;</td>
<td>15.50</td>
<td>3.1</td>
</tr>
</tbody>
</table>

Source: Government Finance Statistics 2017, IMF. Data for Mexico, Argentina & Canada are taken from OECD Country Profiles.
Even countries with the similar types of socio-economic status of India, such as, Argentina and China had also mobilised substantial amount; i.e., 11.4 % and 8.2% of their total tax revenue from wealth taxes. South Africa had also collected 5.8% of total tax revenue (1.66% of GDP) from wealth taxes. Although comparable figure for India is not available in the GFS, an estimate shows that India's revenue collection from wealth taxes was only 0.48 percent of GDP\(^2\) in 2009-10 which was lowest compared to BRICS countries and G20 countries (except Turkey and Mexico). As percentage of total tax revenue in India in 2009-10, it was only 3.1 percent. Lower collection of revenue from wealth taxes is because of very narrow wealth tax bases in India compared to the G20 & BRICS countries\(^4\) as well as due to a large number of exemptions.\(^1\)

It is evident from the Table 1, that many high income and few middle income countries collect substantial amount of revenues from wealth taxes, although the general trend in developing countries is the opposite. It has been revealed by a recent World Bank Report that, in general, in developing countries, property taxes (wealth taxes) are underutilised, representing about 0.5 percent of GDP.\(^15\) The report also expressed its concern about the declining trend of wealth tax collections in the developing countries, at a time when the concentration and accumulation of wealth are on the rise worldwide. However, the discourse, perception and adoption of policies on this issue is changing time to time.

Globally, net wealth tax had never been widespread as compared to other forms of wealth taxes\(^16\) on the grounds of unsatisfactory fiscal efficiency due to the high costs of collection as well as the risk of negative effects on savings and investment activity.\(^16\) Against the general perception that the fiscal importance of net wealth tax is limited, many developed countries are successful in generating substantial amount of resources. Over the years, several OECD countries, abolished the net wealth tax and in 2010, only in a handful of OECD countries this tax existed. However, the trend has been reversed in the wake of last financial crisis, which started in 2008. The 2008 financial crash, weak recovery and demands of deficit reduction have pushed wealth taxes further up the political agenda, yet the question of how best to tax property and wealth remains unresolved.\(^2\) In the aftermath of the crisis, few countries viz., Spain, Iceland, Cyprus had reintroduced\(^20\) this tax for mobilising additional resources and France has broadened the scope of taxes on net wealth appreciably.\(^15\) In contrast to the net wealth tax, in 2010, 23 out of 30 OECD countries used wealth transfer taxes\(^2\) (inheritance tax).

It has already been mentioned earlier that in general, wealth taxes are underutilised in developing countries. A detailed scrutiny on the wealth taxes could ventilate that India is not an exception from most other developing countries in terms of mobilising wealth taxes. Despite the fact that inequality is steadily growing in India over the decades, there was no policy driven intervention through tax policy, although it is considered as the most effective policy tool with the government to address income/wealth inequality. Quite the reverse, Government of India has abolished inheritance tax in March 1985, gift tax\(^22\) in October 1998, and net wealth tax since April 2016. Long-term capital gain tax also got more liberal\(^23\) since 2004-05. Although wealth taxes (all forms of wealth taxes) is an important source of tax revenue, especially in tax structures of most of the other G20 and BRICS countries, as evident from the Table 1, it is clearly a neglected source of revenue collection in India.

**WEALTH TAXES IN INDIA:**

In the early years of post-independent era, several eminent experts unanimously advocated for a broad based wealth taxes. Gulati first proposed ‘Capital Tax’ (wealth taxes) to augment the resources for investment.\(^2\) As per Gulati’s estimate, it would have yielded between INR 52-57 crore (including agricultural sector) in 1953-54. The amount was nearly as high as the amount collected through land revenue at that time.\(^19\) As a proportion of total tax revenue it ranged between 7.7 to 8.5 percent in 1953-54.

In 1957, the famous economist, Kaldor in his report on ‘Indian Tax Reform’ had recommended a package of taxes which was designed not only to increase the total tax yield but also help to plug the many loopholes that existed in the Indian Tax system at that time.\(^19\) Kaldor elucidated that “in a community where there is such a wide gap between the position of a privileged minority of well-to-do and the vast majority who live in dire poverty social cohesion can only be achieved if economic inequality is effectively lessened and the tendency towards increasing concentration of wealth is effectively counteracted”.\(^2\) In this context, Kaldor also proposed net wealth tax and he estimated (using insufficient information) that it would have yielded to the government about INR 17.25 crore.\(^19\)

Krishnan (1972) also felt that “industrialisation had generated an upward movement in prices of urban house property and land values and also in other forms of assets including financial assets. For maintaining the tempo of economic growth sufficient resource mobilisation is required. This can be done only if a broad-based property and net wealth tax is introduced with relatively low rates but embracing a feasible maximum number of property and wealth holders.”\(^1\) However, despite substantial revenue generating potential, revenue collections always remained meagre throughout the period since the introduction of the wealth taxes till 2018, when it was abolished. A couple of contributing factors behind
this low revenue collection, as observed by Krishnan (1972), were the very narrow base of wealth taxes in India with plethora of exemptions.

As an instance, the case for the ‘net wealth tax’ can be cited here. As per the Wealth Tax Act 1957, net wealth of INR 100000 in the case of individuals and INR 200000 in the case of Hindu Undivided Families (HUF) were exempted from paying wealth taxes. Further, there were a number of exemptions (see details in Krishnan 1972) under the wealth tax act. The financial implications of all these exemptions were huge and due to these exemptions revenue collection under wealth tax never reached up to the mark. Krishnan (1972) had done a detailed analysis of financial implication of these exemptions, and he found that under the Wealth Tax Act 1957, a typical individual with total wealth (in different portfolios) of INR 1088000, was liable to pay only INR 1832 as wealth tax, whereas he would have to pay INR 14560 (almost 8 times more) in absence of all exemptions, except the initial exemption of INR 100000. He opined that if a large number of exemptions continue to be given, the elasticity26 of tax yields with respect to tax rates is likely to be extremely small. That is, there would not be much improvement in tax yields, even by increasing the tax rate.

The paper also reveals that while the statutory rates of net wealth taxation has ranged from 0.25 to 3.0 percent, the effective rate of taxation had been less than 0.5 percent due to these exemptions. So, these factors ultimately lead to low wealth tax collection. Over the years, the initial exemption limit increased but, in 2015-16, the net wealth tax rate was only 1 percent of the amount that exceeds INR 3 million on the valuation date.27 Despite the low rates, the collection of net wealth tax revenue in 2015-16 was INR 10.8 billion (0.074% of total tax revenue). However, the wealth tax has been abolished from the financial year 2016-17, on the ground of procedural bottlenecks and low revenue generation; instead of addressing the loophole.

Krishnan (1972) estimated that the potential yields from ‘property and net wealth tax’ in 1969-70, could vary from INR 2.2 to 3.5 billion. Given the total tax revenue collection in 1969-70 of INR 40 billion, property and net wealth tax collection in that year would have ranged between 5.2 to 8.3 percent as proportion of total tax revenue. Let’s assume that proportion of property and net wealth tax collection (i.e., 5.2 to 8.3 percent of total tax revenue) remained the same over the years, that is, even in 2015-16 the ratio remains the same. In this situation, around INR 762.48 billion to 1213.04 billion (given total tax revenue of INR 14556.48 billion in 2015-16) of revenue could have been collected from these taxes, which is a huge amount in absolute terms. And, presently mobilising that amount is quite possible, given the fact that over the years, private wealth in India has accumulated rapidly and consequently, share of private wealth out of the total wealth of India has also grown substantially.

**CONCLUDING REMARKS:**

Evidence suggests that India’s tax-GDP ratio is very low compared to many developed and even serval developing countries; and heavy reliance on indirect taxes, has made the whole tax structure very regressive. For increasing tax-GDP ratio and making the tax structure more progressive, instead of increasing tax rate, at present, broadening direct tax base could be the most effective way. As India’s corporate tax and personal income tax rates are ‘moderate’ and wealth taxes are almost unutilised, there is ample scope for increasing direct tax revenue. Mobilising more resources through direct taxation can also curb inequality through redistribution of income; and on the other hand, fiscal space with the government could be enhanced, creating scope for the government to invest more in the social sector.

However, in the sphere of the direct taxation, India is collecting most of the revenue mainly from two taxes, i.e., corporate and personal income taxes. In the purview of the direct taxes, rest other direct taxes, categorised as ‘wealth taxes’, is not effectively used by the government of India, so far; neither as a source of revenue, nor as a tool for curbing inequality. As the global experience shows that property and wealth taxes have huge revenue mobilising potential, India can also utilise this for enhancing its fiscal space. It should be noted that wealth taxes subsume a number of taxes; and it is not the only way to impose all of them at a time in every country. Many countries have picked few of those taxes from the package of wealth taxes, as per their requirement to supplement the direct tax revenue and also successful in collecting considerable amount of revenues. India can also adopt such strategy, but, a certain amount of revenue targets, consistent with the economic scenario, must be there. Instead of a piecemeal approach of restructuring only wealth taxes separately, there should be a holistic approach. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. That is, broadening wealth tax base and setting wealth tax rates, must be consistent with the corporate and personal income taxes liabilities, so that, any entity or individual taxpayer is not penalised due to high tax burden. However, at the present juncture, government can redesign the whole gamut of wealth taxes and can choose few most buoyant28 wealth taxes viz., property tax, inheritance tax, capital gains tax, dividend tax etc. and implement those properly. Above all, rate for every specific taxes should be fixed after thorough review. The threshold may be kept high, but number of exemptions should be as least as possible. Otherwise, despite setting tax rates even much higher, ultimately it would appear meaningless and futile, in achieving the desired objectives of mobilising resources or addressing inequality.

Ranges from 0 to 1. Typically, Gini coefficients of a nation’s residents, and is the most commonly used measure of inequality. The value of Gini coefficient ranges from 0 to 1. Typically, Gini coefficients of income in the range of 0.30 to 0.35 are considered to be present in egalitarian societies and values exceeding 0.4 are considered inegalitarian. Source: World Bank, 2015.

A tax is said to be buoyant if the tax revenues increase more than proportionately in response to a rise in national income or output. Source: World Bank, 2015.

Prior to 2004–05, long-term capital gains (LTCG) on securities (gains realised on disposal of securities held for more than one year) were taxed at flat 10% without indexation. Short-term capital gains (STCG) were taxed progressively like normal income. Since 2004–05, long-term capital gains have been exempted from tax in lieu of Securities Transaction Tax (STT) and STCG are taxed at the rate of 15%. Source: Prakash et al (2016) Revisiting Capital Gains Tax on Securities in India, EPW, May 14, 2016 Vol. LI No 20.

Change in tax yields for 1 per cent change in the tax rate. The calculation is done on the basis of a valuation date, which is normally March 31 of the immediately previous assessment year. Retrieved 7 November 2017, from http://business.mapsofindia.com/india-tax/types/wealth.html

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