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Do We Need Taxes on Personal Wealth? A Historical and International Perspective

by

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Abstract

This paper examines evidence on trends in the concentration of wealth since before the Industrial Revolution, but concentrating on the past century. Traditional measures of wealth concentration show a decrease in the inequality of wealth holdings over the past 100 years. Non-traditional measures, including the capitalized values of pension plans, public health services, public education and other public services, suggest an even much greater improvement in wealth distribution. Wealth transfer taxes in Canada were introduced when wealth concentration may have been close to its peak in Canada. The withdrawal of these taxes by the provincial and federal governments followed a shift toward greater equality. There is little evidence that the wealth transfer taxes improved the distribution of wealth, but their appeal may, in part, have been due to highly concentrated ownership of wealth. The paper briefly reviews the history of wealth transfer taxes in Canada and considers factors which may affect the return of taxes on personal wealth.

1. INTRODUCTION

Canada, at present, is free of taxes on personal wealth. This means there are no death taxes of the estate and successions type, gift taxes, or annual net wealth taxes, all of which are commonly used in other industrialized countries. Should we wish the absence of these particular forms of taxation in Canada to be temporary or permanent? The recent report of the wealth tax working group of the Ontario Fair Tax Commission (1993) "contains no conclusions or recommendations since the group as a whole was unable to agree on specific reform options". A special issue of *Canadian Public Policy* also examined personal wealth taxes, and although no consensus was reached, one of the editors concludes that "(P)erhaps, Canada should seriously consider the taxation of inheritances or gifts and bequests.... Even if these taxes do not raise much revenue, taxation of inter-generational transfers might be appropriate for reasons of fairness and efficiency" (Mintz, 1991, p. 260). Other studies by individuals are less equivocal and have argued that "a fair and balanced tax system should include either a wealth tax or a wealth transfer tax" (Bale, 1989, p. 48). The concentration of personal wealth has been among the reasons given for taxing wealth and the transfer of wealth. It is therefore important to consider what we know about wealth concentration.

The remainder of the paper is organized as follows: sections 2 and 3 discuss shortcomings of the more traditional measures of wealth distribution; section 4 considers the degree of wealth concentration that may be acceptable, and section 5 examines evidence on wealth concentration in industrial countries over the past two centuries; section 6 provides a brief review of the history of wealth transfer taxes in Canada during the past 100 years, and section 7 considers the likely role for wealth transfer taxes and net wealth taxes in Canada's future. The paper does not discuss the likely economic effects of taxes on the transfer of wealth or of net wealth taxes. This is partly due to the extensive coverage of this issue elsewhere[1], partly due to continuing differences in views among economists on this topic[2], but primarily due to other evidence presented in this paper which relegates arguments concerning economic effects of such taxes to a relatively minor role in determining their future.

2. ITEMS NORMALLY OMITTED IN WEALTH DISTRIBUTION MEASURES

For our purposes the term wealth is synonymous with "net worth" or "net wealth", which refers to the value of assets net of liabilities. Most measures of personal wealth exclude some forms of wealth. The "conventional" measures estimate the cash value of certain assets, but exclude other important assets. The most recent survey undertaken by Statistics Canada (1987) included bonds, stocks and shares, deposits, owner-occupied homes, cars, and net investments in personal businesses.[3] It excluded equity in private pension funds, insurance policies, the value of collectibles, and the value of consumer durables other than motor vehicles. It also excluded the value of public pensions and the value of human capital. Measures for other countries also tend to include the items such as those in the Canadian study, and may or may not include the value of additional consumer durables, insurance policies, and the like.

"Conventional" measures of wealth omit items which are large and have been of growing importance in the twentieth century. The spread of higher education, the rapid growth of public pension plans, and the general growth of key public services, such as health services, significantly affect the distribution of broadly defined wealth. Although this paper refers to broader measures of wealth, most data cited pertain to "conventional" measures. In some cases, the value of public pensions is included, but not the value of human capital or the value of claims to the flow of public goods and services.

HUMAN CAPITAL

The importance of human capital has long been recognized. Lindert (1986), taking a historical perspective, notes that

> "While any choice of a discount rate is highly arbitrary when capitalizing human wealth that could be only rented and never sold, almost any reasonable rate would still make human capital approach, or surpass, half of all capital anytime in the last three centuries."[4]

This statement highlights the significance of omitting human capital from estimates of wealth distribution. In fact, human capital tends to be largest early in one's working life, prior to accumulation of wealth in other forms. It gradually decreases over one's working life. At the end of a working life, when there may be substantial accumulation of wealth in other forms, human capital will be at a low point. Given this situation, without the inclusion of human capital wealth will be much more concentrated among the elderly and may be vastly overstated.

THE CAPITALIZED VALUE OF PENSIONS

The capitalized value of employment and state pensions is a second major element omitted from normal wealth distribution estimates. The Inland Revenue Service in the U.K. annually provides alternative estimates which show wealth to be much less concentrated when it includes the value of pensions. And the capitalized value of social security in the U.S., when included with regular estimates of wealth, increased wealth by 54 per cent for a large segment of the population. A similar adjustment seems likely for Canada.[5] Given that this form of wealth is much more equally distributed than normally included forms of wealth, the result again is that the conventional estimates exaggerate wealth concentration.

OTHER ITEMS

The twentieth century has also been a period of rapid growth in the provision of government goods and services. The role of government, if measured as taxes/GDP, increased from around 10 per cent a century ago to around 40 per cent in 1990 for industrialized countries. The capitalized value of claims to the flow of services from the government and its assets is more equally distributed than other forms of wealth.

Education and health are two important areas of government service. In Canada, as in other countries, increased access to education has contributed to wealth dispersion in the twentieth century. However, there are no estimates of the impact of this phenomenon in Canada or in other countries.[6] The capitalized value of anticipated health services provided by the public is an aspect of wealth which differs among countries. The expansion of public health in Canada is likely to have reduced the concentration of wealth in Canada since the 1960s.[7] While such a phenomenon may make the taxation of wealth more acceptable in that pools of wealth are less needed to protect against catastrophic illness, the increased equality in wealth, which includes capitalized benefits of anticipated health services, seems likely to reduce concerns over inequality.

3. MEASUREMENT METHODS AND PROBLEMS

The three primary methods of estimating the distribution of wealth in a country are the "estate multiplier" method, the "investment income" method, and the "sample survey" method. All three have been used in the United Kingdom and the United States. One or more of the methods have been employed in other countries. Canada now relies exclusively on survey data.[8]

The estate multiplier method, even if generally thought the best available, has its problems. Estate tax returns usually are filed only for those estates sufficiently large to be taxable. It is then necessary to make assumptions about wealth held by the population not included in the estate tax returns. Assumptions #1 and #2 in Table 1 show the difference in wealth distribution in the U.K. in 1972 when it is assumed that those who do not file estate tax returns have no wealth and when they have an average of 1,000 pounds in wealth. The share of total wealth controlled by the top 10% falls from 71.9% to 64.1% and the share controlled by the bottom 80% rises from 10.8% to 21.4%.

Table 1
Wealth Estimates and Sensitivity to Assumptions:
U.K. Estimates for 1972

	Assumption:	#1	#2	#3
Top	1%	29.9	26.8	17.4
	5%	56.3	51.4	34.9
	10%	71.9	64.1	45.7
	20%	89.2	78.6	59.3
Bottom	80%	10.8	21.4	40.7

#1 Estimates are based on estate tax returns and assume that those not filing returns have no wealth.
#2 It is assumed that the population not included in the estate tax returns have wealth of £1,000 per head.
#3 Wealth is adjusted to reflect the gap between estimates based on estate tax returns and balance sheet totals, and also to include occupational and state pension rights.

Source: Harbury and Hitchens (1979), p. 8.

Another important problem with the estate multiplier method is that estate tax returns are for individuals, and wealth distribution by households or by families may be of greater interest than that for individuals. It is quite possible for wealth concentration among individuals to decrease significantly, while that among families changes little if wealth is dispersed more evenly among family members. Even with such major imperfections, there is a consensus among experts that the estate multiplier method is superior to the alternatives.[9]

The second method for estimating wealth distributions is the investment income approach. This method, too, has serious shortcomings. First, some assets, such as collectibles, may generate no income flow and yet may be significant. Such assets are likely to be concentrated among the most wealthy. Second, certain types of assets may yield different average returns to wealth holders in different classes. There is evidence that the return on equity investments is higher among those with higher levels of wealth. Such individuals are in a better position to assume the risks which accompany higher returns. Third, forms of income that are not taxable, for example the imputed income from dwellings or consumer durables, may not get included. The distribution of this form of income may be more equal than other forms of investment income. Fourth, there is the general problem of determining the appropriate rate of return to use for each asset type in a dynamic environment. Finally, if the tax returns are on an individual basis, data on family wealth may be lacking.

Problems with wealth surveys are also serious. First is the problem of ensuring that the few "extremely" wealthy are adequately covered by any samples. In order to ensure adequate representation by those in the high end of the wealth distribution the sample would have to be unreasonably large. To avoid this, selective sampling of the highest wealth groups must be done. Second, underreporting, or a complete lack of reporting, is common.

In addition to the shortcomings of the three methods there is the omission of the major items previously discussed.

4. What Degree of Inequality is Acceptable?

> "The distribution of wealth, therefore, depends on the laws and customs of society. The rules by which it is determined are what the opinions and feelings of the ruling portion of the community make them, and are very different in different ages and countries, and might be still more different, if mankind so chose..." (J.S. Mill quoted by Heilbroner, p. 108).

We, of course, do not know when wealth becomes sufficiently concentrated to be generally unacceptable. Rawl's (1971) states in his *A Theory of Justice* that

> "All social values - liberty and opportunity, income and wealth, and the bases of self-respect - are to be distributed equally unless an unequal distribution of any, or all, of these values is to everyone's advantage" (p. 62)

Any existing inequalities must reasonably be expected to be to the advantage of all, and where there is advantage attached to certain positions, these positions must be open to all.[10] Thus in the case of the distribution of wealth, the objective of wealth taxes, as with other tools of social and economic policy, must be to establish a level of wealth inequality which is thought to be beneficial to all.

Can democratic society survive without taxes which are designed to affect wealth concentration and the transfer of wealth by inheritance in particular? Bayly's (1902, p.7) observation on this matter was that

> "Succession Duty seems to be an institution of democracy. It is in the most truly democratic countries in the world, England, Switzerland and the Australian Colonies, that this form of taxation finds its highest development."

Shoup (1966, p.108), speaking about the U.S., seems to agree in arguing that "(o)ur existing social values insist upon some limit, or some restraining force, on the accumulation by any one person of wealth through gift or inheritance". The Rowell-Sorois Commission (1940, p. 157) of the 1930s notes that "large incomes and large estates may be considered as undesirable in themselves... Heavy taxation may, in this case, be treated as something which will have a stabilizing and democratizing effect on the community". And Hartle (1988, p.421) has referred to the absence of taxes on bequests as "a thorn buried deep in the flesh of the body politic".

The limit or restraining force mentioned by Shoup no longer exists in Canada, and Canadians are aware of great individual wealth in their midst, wealth which has often been inherited. While the Rowell-Sirois Commission was concerned with the possibly adverse effects of amassed wealth, the others appear to be more concerned with the ability of individuals to become wealthy through no effort or ability of their own. There is a sense of injustice which accompanies the accumulation of wealth through inheritance that seemingly does not accompany self-created wealth.

At a time when wealth was heavily concentrated and perpetuated through intergenerational transfer in advance of death and at time of death, the injustice of these transfers of wealth was particularly evident. Writing in 1848 John Stuart Mill concluded that

> "I see nothing objectionable in fixing a limit to what any one may acquire by the mere favour of others, without any exercise of his faculties, and in requiring that if he desires any further accession of fortune, he shall work for it" (p. 228).

This was at a time when the Industrial Revolution had caused a substantial increase in the concentration of wealth among the very wealthiest in the U.K., and a time when uprisings throughout Europe were supporting wider suffrage and liberalized land policies. Wealth at this time was still heavily concentrated in land holdings, particularly in Eastern Europe but also elsewhere, and land wealth was passed from generation to generation.

Toward the end of the 19th century, even some of the wealthiest of the period agreed with the growing sentiment in support of wealth transfer taxes. Andrew Carnegie, an individual some credit for the impetus toward the introduction of estate taxes in the North America, wrote in 1889 that

> "Of all forms of taxation this (death duty) seems the wisest... It is difficult to set bounds to the share of a rich man's estate which should go at his death to the public through the agency of the State, and by all means such taxes should be graduated, beginning at nothing upon moderate sums to dependents, and increasing rapidly as the amounts swell."[11]

Recent public policies suggest that substantial inequalities in wealth may be, for whatever reasons, quite acceptable in some societies. The elimination of all federal and provincial death taxes in Canada by 1985, all federal and state death taxes in Australia by 1982, estate taxes in New Zealand by 1993, and large reductions in federal and state death taxes in the United States in the 1980s support such a conclusion. Such may be consistent with R. H. Tawney's (1951, p. 107) observation that the middle classes may acquiesce "in sharp distinctions of wealth and power, provided that, as individuals, [they thought] they were free to scale the heights" (p. 107).

5. Wealth Concentration over Time

Wealth Narrowly Defined.[12]

Keeping in mind our earlier caveats on the problems of measurement, what do we know about wealth concentration and its development over the centuries in the now industrialized countries? Table 2 sets forth evidence on the concentration of wealth in England and Wales from 1670 to 1988. From 1670 to 1875, the share of household net worth controlled by the top 1 per cent increased from 49 to 61 per cent, while that of the next 9 per cent fell from 34 to 23 per cent. There was a perpetuation of the concentration of wealth in England and Wales over these two centuries. Wealth concentration in England and Wales continued to increase into the twentieth century, but the trend appears to have reversed sharply by the 1920s. The share held by the top 1 per cent fell from 69 per cent in 1911 to 17 per cent in 1988, that of the top 5 per cent from 87 to 38 per cent, and that of the top 10 per cent from 92 to 53 per cent. These changes are dramatic.[13] There has been a very sharp decline in U.K. household wealth inequality from 1920 to 1990.[14]

Levels of wealth concentration seem also to have increased in Canada and in the United States in the nineteenth century. One U.S. study, based on estate data, concluded that "the share of wealth held by the rich probably drifted upward during the nineteenth century, the support for this statement being stronger for the latter half of the century than for the first half" (Gallman, 1969, p. 2). A second study (Williamson and Lindert, 1980, p. 56) found that "wealth concentration rose over most of the period 1774-1860, with especially steep increases from the 1820s to the late 1840s".

Table 2
Distribution of Wealth in England and Wales, 1670-1988

Year	Top 1%	Top 5%	Top 10%
1670	49	73	83
1740	44	74	86
1810	55	74	83
1875	61	74	84
1911	69	87	92
1925	61	82	88
1938	55	77	85
1950	47	74	-
1960	34	60	72
1970	30	54	69
1980	23	43	58
1981	18	36	50
1986	18	36	50
1988	17	38	53

Sources:

Data for 1670-1875 is from Lindert (1986), p. 1145.

Data for 1911 is from Harbury and Hitchens (1987), p. 248, and 1925-1980 is from Shorrocks (1987), p. 32; data for 1980 pertains to the U.K., not just England and Wales but would be very similar for England and Wales.

Data for 1981-1988 is taken from *Social Trends* 21 (1991) and is for marketable wealth for the U.K.

It seems likely that the top 1 per cent of households held a quarter or more of total personal wealth, and the top 10 per cent held from 70 to 80 per cent of personal wealth in the U.S. toward the end of the 1800s. Concentration in Canada appears to have been as great or greater. Osberg and Saddiq (1988) estimated that the top 1 per cent in Nova Scotia in 1871 held 39 per cent of total personal wealth, and the top 10 per cent held 81 per cent. To the extent that Nova Scotia was representative of Canada at that time, the concentration of wealth in Canada in 1871 was much greater than it is today. Very high levels of wealth concentration existed in the U.K. and North America at the time estate and inheritance taxes were introduced in the 18th and 19th centuries.

Following periods of increasing wealth concentration through the nineteenth century, a major decrease in wealth concentration in the U.K. and in North America occurred during the first half of the twentieth century. Estimates of wealth distributions in the U.S. and Sweden indicate a substantial fall in the concentration of wealth during the twentieth century. The share of wealth held by the top 1 per cent in Sweden (Table 3) fell from 50 per cent in 1920 to 21 per cent in 1975, and that for the top 5 per cent from 77 per cent to 44 per cent. In Sweden, as in the U.K., rapid growth in homeownership contributed to equalizing wealth holdings. Spant (1987) found that as a share of total household assets, owner-occupied housing and secondary dwellings increased from 18 per cent in 1945 to 44 per cent in 1975. As in the U.K., the change toward greater equality has been dramatic.

Table 3
Household Wealth Distribution in Sweden, 1920-1983

	Top 1%	Top 5%	Top 10%	Top 20%
1920	50	77	91	100
1930	47	74	88	98
1951	33	60	76	92
1966	24	48	64	82
1975	21	44	60	80

Source: Spant (1987), p. 60.

Available evidence for Canada also shows a sharp fall in wealth concentration, as conventionally measured, over the hundred years from 1870 to 1970 (see Table 4). By 1970 the top 1 per cent and 10 per cent of Canadian households held 20 per cent and 58 per cent, respectively.

Table 4
Family Wealth Concentration in Canada, 1871 and 1970

		1871 *(Nova Scotia)*	1970 *(Canada)*
Top	1%	39	20
	5%	72	43
	10%	81	58

Sources: Osberg and Suddig (1988); Davies (1979).

There have been few studies that bring together comparative estimates of recent wealth distributions for a number of countries (see Harrison (1980) and Kessler and Pestieau (1991). Results in Table 5 show that the share of total wealth held by the top 5 per cent is less in Canada than in other countries, with the exception of Sweden and the U.S. The share held by the top 1 per cent is less in Canada than in all but Sweden and France. Wealth ownership in Canada, relative to other countries, does not seem to be particularly concentrated.[15] Nor is it particularly dispersed. Nonetheless, after a half century of declining wealth concentration, the share of wealth in the hands of the richest remains large. The top 1 per cent of wealth holders held from 16 per cent (Sweden) to 32 per cent (U.K.) of total wealth. Nevertheless, the distribution of wealth ownership has changed significantly during the current century. One further conclusion drawn from international comparisons is that "there appears to be a convergence among industrialized countries in the level of wealth inequality" (Wolff and Marley, 1989, p.22). Significant forces such as the spread of education, homeownership, public pensions and other public services, and, perhaps, progressive tax rates, have been forces at play in all countries.

Table 5
Household Wealth Distribution in Eight Countries

	% of Top Wealthholders			
Country	*1%*	*5%*	*10%*	*20%*
France (1977)	19	45	61	81
Belgium (1969)	28	47	57	71
U.K. (1974)	32	57	72	85
Germany (1973)	28	na	na	na
Denmark (1973)	25	47	60	75
Sweden (1975)	16	35	52	65
U.S.A. (1972)	25	43	na	na
Canada (1970)	20	43	58	74

na means not available

Source: Kessler and Masson (1987), p. 153

WEALTH MORE BROADLY DEFINED.

When household wealth is more broadly defined, the twentieth century trend toward increased equality in the distribution of wealth is even more pronounced. The effect of including the reserves of trust funds, the total value of pension reserves and the value of social security benefits in estimates of the share of total wealth held by the top one per cent of wealth holders in the U.S. is shown in column (2) of Table 6. When these forms of wealth are included the share of the top 1 per cent is about the same in the 1920s, but falls from 26.8 to 20.5 per cent by 1972, and from 17.3 to 13.8 per cent in 1976.[16]

Table 6
U.S. Wealth Distribution over Time: Share of Total Assets of Top 1% of Wealthholders, 1922-81

	W_1^*	W_2^*
1922	37.1	37.9
1939	35.9	33.4
1949	23.9	20.5
1958	25.4	20.7
1969	27.3	21.0
1972	26.8	20.5
1976	17.3	13.8
1981	22.0	-

W_1 = cash surrender value of total assets less liabilities and is the wealth currently available to the household or individual.

W_2 = W_1 + reserves of trust funds less retained value in W_1, + the total value of pension reserves (net of any cash surrender value in W_1, + present value of social security benefits.

Source: Wolff and Marley (1989), pp. 769 and 786.

Evidence for the U.K. in Table 7 is similar. The share of the top 1 per cent falls from 31 per cent to 21 per cent in 1971 when the capitalized value of public and private pension benefits are included, and from 17 to 10 per cent in 1988. The significant change from 1911 can be seen if we compare the 69 (the top 1 per cent) and 92 (the top 10 per cent) per cent figures in Table 3, prior to the existence of significant pensions, with the 10 (top 1 per cent) and 36 (top 10 per cent) per cent figures of 1988 in Table 7.

Table 7
Population Wealth Distribution in the U.K., 1971 to 1988

	Marketable Wealth		Marketable Wealth plus Occupational and State Pension Rights	
	Top 1%	Top 10%	Top 1%	Top 10%
1971	31	65	21	49
1976	21	50	12	34
1981	18	50	11	32
1986	18	50	10	34
1988	17	53	10	36

Source: Inland Revenue Statistics 1980, 1982, 1990.

6. THE TAXATION OF PERSONAL WEALTH IN CANADA

There have been several major points of significant change in the use of death and gift taxes in Canada over the past century. Personal wealth was highly concentrated in Europe and North America when provinces introduced succession duties in the 1890s. The Dominion government entered the gift tax field in 1935 and in 1941 imposed the first federal successions duty, nearly a half century after the provinces had introduced similar taxes. Under tax rental agreements the federal rates were doubled in 1947 and provinces, with the exception of Quebec and Ontario, agreed to vacate the field in return for half of the revenues. This provincial share was increased to three quarters in 1963, and at that time British Columbia decided to again collect its own tax. The federal law was changed to a simpler estate tax in 1959.

Provincial movement out of the death tax field began in 1967 when Alberta decided to return its share of the federal estate duty to the estates from which it was collected. The federal government abolished its estate and gift taxes with the tax reform effective January 1, 1972. And in 1979 and 1985, Ontario and Quebec, respectively, were the last two provinces to withdraw from the death tax field. Within less than a century, from 1892 to 1985, the federal government and all of the provincial governments had introduced death taxes, had administered them separately as well as on a revenue sharing basis, and had subsequently withdrawn from the field. Federal involvement had lasted only three decades.

PROVINCIAL WEALTH TRANSFER TAXES PRIOR TO 1940

Initially (see Table 8) rates on estates passing to widows had not exceeded 5 per cent (Manitoba was an exception), regardless of estate size. Table 9 shows the rates applicable to larger estates passing to spouses and other preferred beneficiaries in the mid-1930s. By the 1930s the maximum rates applied to estates bequeathed to widows rose to 29 per cent in Ontario, and rates were generally above 15 per cent if $1 million was bequeathed to a spouse. Succession duties accounted for 7.6 per cent of Ontario's provincial revenues by 1910, 15.5 per cent by 1920, 19.6 per cent by 1930. As late as 1945 they accounted for over 10 per cent of provincial revenues. The rise in revenues up to 1930 was due to growth in the number of taxable estates, and to increases in tax rates.

The growing revenue importance of death taxes and rising tax rates contributed to concerns about tax competition between provinces. The Rowell-Sirois Commission (1940) concluded that inheritance taxes could not be used by provinces without harming the economy, and more specifically that "succession duties, as at present imposed by the provinces, operate to distort

Table 8
Features of Early Provincial Succession Duties

Province	Basic exemption	Exemption for "close" family[1]	Number of rates and brackets for close family	Range of rates close family[2]	collateral[3]	strangers
				.... (in percent)		....
Ontario (1892)	$10,000	$100,000	2	2.5-5.0	5.0	10.0
Quebec (1899)	3,000	3,000	6	0.5-3.0	.0-8.0	10.0
Nova Scotia (1895)	5,000	25,000	2	2.5-5.0	5.0	10.0
New Brunswick (1901)	5,000	50,000	3	1.25-5.0	5.0	10.0
P.E.I. (1894)	3,000	10,000	2	1.5-2.5	2.5	7.5
Manitoba (1893)	4,000	25,000	10	1-10	1-10	1-10
B.C. (1990)	5,000	25,000	3	1.5-5.0	1.5-5.0[4]	1.5-5.0[4]

[1] "Close" family refers to fathers, mothers, children, wives, husbands, grandchildren, sons-in-law, and daughters-in-law in five provinces. New Brunswick excludes grandchildren. Quebec includes fathers-in-law and mothers-in-law. This concept changed over the years with grandparents included in some provinces.

[2] The maximum rate begins to apply at different levels. In Ont., Que., and N.B. it applies at $200,000, in P.E.I. at $50,000, N.S. at $100,000, B.C. at $500,000 and Manitoba at $1 million.

[3] This includes other family such as siblings and their offspring and aunts and uncles. In Quebec, rates vary from 3 percent on siblings to 6 percent on grandparents and 8 percent on distance relatives.

[4] In British Columbia's initial act, rates on "close" family were half those on others.

Source: Bayly (1902)

Table 9
Marginal Provincial Successions Duty Rates for Preferred Beneficiaries in the Mid-1930s (in percent)

Net Value of Estate	Nova Scotia	New Brunswick	P.E.I.	Quebec	Ontario
$ 100,000	5.5	3.0	5.0	6.5	7.5
1,000,000	18.5	11.5	5.0	20.5	18.0
5,000,000	27.0	15.0	5.0	25.0	29.0

Net Value of Estate	Manitoba	Saskatchewan	Alberta	British Columbia
$ 100,000	4.6	5.0	6.5	2.5
1,000,000	17.25	22.5	16.5	15.0
5,000,000	17.25	26.0	19.0	15.0

Source: Samuel Quigg, *The Law Relating To Succession Duties In Canada* (Toronto: Carswell, 1935), pp. 296-324.

investment throughout Canada in a way which is economically undesirable"(p. 152)". The Commission recommended that the provinces withdraw from the death tax field. This advice was not accepted.

FEDERAL DEATH AND GIFT TAXES

Although the provinces decided not to vacate the succession duties field, the federal government entered the field with the Dominion Succession Duty Act in 1941. The federal tax followed the form of the provincial duties, by and large, being composed of two separate rate structures: one based on the size of the total estate, and the other determined by the size of the individual succession. Federal rates were doubled in 1947 when eight provinces, under the Tax Rental Agreement, agreed to abolish their succession duties in return for half of the revenues collected under the federal tax.[17] This raised the top marginal rate under the federal duty to 54 per cent. The provincial duties continued in Ontario and Quebec and were credited against federal duties up to half the federal duties payable.

The federal government simplified and reduced its death tax in 1959 when it moved from a successions duty to an estate duty. No longer were dual rates applied, and no longer was it necessary to have four classes of beneficiaries. But rates were still very significant. With the federal tax allowing for a credit for the provincial succession tax up to half the amount of the federal tax, an Ontario study found that the marginal rate on estates in Ontario rose to a maximum of 60.35 per cent on "preferred" beneficiaries and to 70.75 per cent on "strangers". In the case of Ontario and Quebec the provincial succession duties substantially exceeded the credit permitted by the federal government. In sum, with the introduction of the federal succession duty in 1941, death tax rates on larger estates in Canada became substantial if no action to avoid was taken. This held true from 1941 through 1971 for most of Canada. Table 10 shows that provincial plus federal taxes as a share of the aggregate net value of taxable estates ranged from 19 to 26 per cent in the final ten years of the federal tax, and rose significantly after 1968. The tax reform of 1971 abolished the federal estate and gift taxes effective January 1, 1972. This was also the date when Canada extended its income tax to capital gains deemed to be realized at time of death.[18]

Table 10
Estate and Succession Duty Revenues as a Percentage of the Aggregate Net Value of Estates that are Taxable under Federal Statutes, 1963-72

Fiscal Year Ending in	(a) Aggregate Net Value	(b) Net Federal Tax (in millions)	(c) Provincial Tax	[(b)+(c)]/(a)
1963	713	75	72	20.6%
64	821	91	86	21.6
65	888	85	72	19.9
66	971	90	108	20.4
67	1140	106	118	19.6
68	1136	101	109	18.5
69	1276	119	122	18.9
70	1077	111	141	23.4
71	1105	128	158	25.9
72	1129	128	138	23.6

Sources: Statistics Canada, *Provincial Government Finance: Revenue and Expenditure* 1963 to 1975, Catalogue 68-207

7. THE FUTURE OF PERSONAL WEALTH TAXES IN CANADA

Taxes on personal wealth have been a little discussed topic over the past two decades. The of Toronto conference in 1990 interrupted the profound silence on the topic, but only briefly. "Out of sight and out of mind" has been the general status of personal wealth taxes in Canadian public policy discussions. A generation of Canadian students has studied public finance with little attention paid to the role of taxes on personal wealth. The Carter Commission and the 1972 tax reform encouraged this lack of attention. The Commission's focus on income taxes, and its failure to recognize a role for wealth taxation separate from that of the income tax system, contributed to the silence with respect to taxes on personal wealth. The repeal of the federal estate and gift taxes withdrew these tax forms from the public eye. There is little evidence that discussion of personal wealth taxes in the classroom or in provincial or federal departments of finance is about to heat up, and there are reasons for this.

MORE EQUAL WEALTH DISTRIBUTION

One factor is that wealth in industrialized countries has become much more equally distributed over the past century. Wealth distribution, particularly when broader measures are used, is much more equal in 1993 than it was in 1892 when Ontario introduced Canada's first successions duty. Wealth concentration in the nineteenth century foreshadowed the adoption of death taxes by Canadian provinces in the 1890s, the widespread use of progressive inheritance taxes in Europe, Australasia and North America at the turn of the century (Seligman, 1908), and the gradual increase of the rates of these taxes over the next three decades - a period of high and relatively stable wealth concentration.

Improved equality of wealth has been accompanied by the decline in the use of personal wealth taxes in Canada and elsewhere in recent decades. Table 11 shows the general decline in personal wealth taxes as a share of total tax revenues in OECD countries from 1965 to 1990.

An unanswered question is whether personal wealth taxes have contributed much to greater equality in the distribution of wealth. Available evidence is inconclusive. Aaron and Munnell (1992, pp.127-28) observe that wealth concentration estimates for Sweden and Great Britain "show a marked decline in concentration from the 1940s to the 1980s, perhaps reflecting efforts over this period in both countries to equalize the wealth distribution through progressive tax policies", but other studies in the U.S. and the U.K. provide little evidence that the use of death taxes does much to reduce wealth inequality (Brittain, 1977). Such evidence also is lacking for countries where annual taxes on net wealth are used.

MAXIMIZING VOTES

A politically optimal tax structure equalizes marginal *political* costs per dollar of additional revenue across all revenue sources and across all taxpayers (Hettich and Winer (1988) and Gillespie (1991)). Tax systems are designed to meet specified expenditure levels in a way that costs least in terms of lost votes. The clear implication of this is that we would have taxes on personal wealth if the votes were there. The relevant question, therefore, is whether the political cost of personal wealth taxes is likely to decrease sufficiently relative to other revenue sources in order to cause such taxes to be enacted in Canada.

Table 11
Combined revenue from net wealth taxes on individuals and estate, gift, and inheritance taxes, as a percentage of total tax revenue in 1988, 1976 and 1965

Ranking in 1990	Country	1990	1976	1965	Ranking in 1965
1	Switzerland	3.21	3.42	4.46	1
2	Japan	1.41	0.85	0.71	21
3	Norway	1.32	0.91	1.67	10
4	Greece	1.26	1.12	0.95	18
5	France	1.17	0.46	0.56	22
6	Netherlands	1.03	0.85	1.86	9
7	Spain	1.04	0.65	1.09	16
8	United States	0.96	1.41	1.99	7
9	Denmark	0.81	0.81	2.09	6
10	Belgium	0.69	0.72	1.17	14
11	United Kingdom	0.65	0.88	2.62	3
12	Germany	0.64	0.76	1.53	11
13	Luxembourg	0.64	0.54	1.14	15
14	Sweden	0.60	0.62	1.29	13
15	Austria	0.57	0.73	0.85	19
16	Finland	0.51	1.14	1.07	17
17	Portugal	0.50	0.50	2.48	4
18	Ireland	0.39	0.97	1.87	8
19	New Zealand	0.29	1.32	2.30	5
20	Italy	0.14	0.20	0.85	19
21	Turkey	0.12	0.33	0.17	23
22	Australia	0.00	1.37	2.74	2
23	Canada	0.00	0.25	1.48	12
OECD unweighted average		**0.78**	**0.90**	**1.61**	

Includes: Recurrent net wealth taxes on individuals and estate, gift, and inheritance taxes.

Source: Calculated from OECD (1992)

DEMOGRAPHY

The aged are becoming an increasing share of our population. One estimate of the change in share of Canada's population that is 65 and over for the period to 2025 is as follows:

1985	1995	2005	2015	2025
(percentage of population 65 and over)				
10	12	13	17	21

Source: Calculated from Masson and Tryon (1990), p. 457.

From 1985 to 2025 the share is expected to more than double. Wealth may become more widespread in Canada as the percentage of the population over 65 grows. Since wealth dispersion tends to be highest among young adults, the aging of the population will be accompanied by increasing equality of wealth as conventionally measured. The share of the voting population who own significant amounts of wealth will increase. The implications of this for a tax on net wealth seem reasonably clear - as the revenue potential for wealth taxes grow, they may become less rather than more popular with the electorate.

The demographic change may result in a decrease in support for wealth transfer taxes for another reason. As families have become smaller and the ownership of assets, including homes, has become widespread, an unprecedented share of the population now expects to inherit something substantial. If, as in the 1980s, it is increasingly difficult for the young to purchase their own home, the "right" of inheritance may gain support.[19]

INTERGENERATIONAL SENSITIVITY

Much has been done to reduce the prevalence and depth of poverty among the aged over the past twenty years (Economic Council of Canada, 1992). Less progress has been made in reducing poverty among those of working age. There has, simultaneously, been rapid growth in the size of government debt and concern about the tax burdens that this will place on future generations. In light of family and intergenerational linkages (see Barro, 1974), parents may come to consider bequests an obligation they have to future generations, and younger adults may see inheritances as necessary for intergenerational equity. There is growing concern that future generations may be worse off than the present generation. This may decrease the appeal of wealth transfer taxes which impede the intergenerational transfer of wealth.

COSTS OF COMPLIANCE AND ADMINISTRATION

The Ontario Committee on Taxation (1967, p. 147) found the statute for the Ontario successions duty "frequently so abstruse that it has almost gained universal notoriety among practitioners as being the worst piece of tax legislation on the books in the Province". Special exemptions for farming properties or for properties passing to specified individuals, the valuation of properties such as annuities and trusts, and the treatment of gifts prior to death are among the issues that have complicated statutes.[20] An awareness that opportunities for avoidance are open particularly to those who can afford expert counsel lessens the attractiveness of levying heavy death taxes. A dimension of equity is lost.

Difficulties in achieving ideal wealth transfer taxes have lessened their political attractiveness. Nonetheless, many experts agree with Brown (1991, p.349) that "there is no administrative or conceptual reason why some moderate and up-to-date form of estate taxation might not be part of the Canadian tax scene".

The administrative and compliance problems associated with the introduction of an annual net wealth tax are likely to be greater than for wealth transfer taxes. First, it would be a totally new form of taxation in Canada. Its purpose and rationale would have to be clearly explained. The difficulties this entails were in evidence with the GST which involved the introduction of one form of sales tax and the withdrawal of another. One issue would be the probing eye of "big brother", as tax authorities would require an annual accounting of wealth as well as income. It seems highly unlikely that Canadians would accept this change quietly, or otherwise.

FARMS AND SMALL BUSINESSES

Wealth transfer taxes and net wealth taxes fall on well-organized segments of the population. Farmers and the small-business community are significant in number; the latter has increased while the former group has declined. Both are reasonably well-informed on tax matters, and in the case of farmers have more than proportionate representation due to the drawing of constituency boundaries. In addition,

general sentiment has supported the family farm and corner grocery as a source of strength in Canadian society.

The "farm block" is given credit for the abolition of wealth transfer taxes in Australia, and supported the early withdrawal by Alberta and Saskatchewan of their death taxes. Where death duties have persisted, it is usual for there to be some form of preferential treatment for farms and small businesses that are passed on within the family. With a vocal small business community, continuing support for the family farm, a growing segment of aged with substantial wealth, and increased awareness of the mobility of capital and skilled individuals between provinces and between nations, the necessary constituency for the introduction of substantial annual wealth taxes or wealth transfer taxes in Canada does not exist (see Banting, 1991).[21]

GLOBAL AND INTERPROVINCIAL TAX COMPETITION

At a time that Canada wishes to attract off-shore capital and to attract entrepreneurial immigrants who bring capital with them, substantial wealth transfer taxes may create problems.[22] Australia, without net wealth or wealth transfer taxes, competes with Canada for capital and immigrants from the Pacific Rim. Wealth transfer taxes have declined substantially in the U.S., and interstate tax competition and the aging of the U.S. population are likely to contribute to a continuation of this trend. The U.S. has no annual net wealth tax.

Whereas death duties have continued in use in federal states, tax competition among provinces and states contributed to their abolition in Australia and Canada, and to a substantial lessening of their role in the U.S. Bird and Bucovetsky (1976, p. 40) found that the withdrawal by Prince Edward Island of its successions duty "led directly to that of three neighboring provinces, apparently largely for competitive reasons, for fear of loss of investment to the island 'tax haven'". In the U.S., Eckl (1986, p.305) concluded that "(a)s interstate tax competition intensifies, it seems likely that the trend toward reducing or eliminating state inheritance and estate taxes will continue, placing their existence in peril". The U.S. encourages states to use death taxes by allowing state taxes to be credited against federal death taxes up to a point. Head (1974) argued for a similar "tax umbrella" in Canada under which provinces might be allowed a credit up to 95 per cent of the federal tax.[23] The tax competition arguments indicate that if wealth transfer taxes are to play a significant role in Canada it will require either a federal tax or federal umbrella in the area.

In sum, the taxing power of provincial and state governments in Canada and Australia, the access by interest groups to decision makers at this level of government, and tax competition among states and provinces, cause these two countries to be unique in their failure to use net wealth and death taxes.

8. CONCLUSION

Moderate death taxes, similar to those used by the federal government in the U.S., could be introduced in Canada. The administrative costs need not be great so long as a reasonable exemption is provided and rates are moderate. Many will agree with J.S. Mill's arguments for "fixing a limit on what anyone may acquire by the mere favour of others". Any such limit can be expected to change from time to time.

As in the U.S., the federal government must, by allowing provincial taxes to be credited against federal taxes, limit the extent of possible tax competition. Without such an "umbrella" tax competition among provinces will prevent effective use. Thus, the reintroduction of death taxes in Canada requires more effective federal-provincial cooperation than was achieved in the past.

There is, however, no evidence that even moderate death taxes would currently have much support in Canada. This may change as concern grows over the increased inequality in incomes and wealth that developed in the 1980s. Policy changes in the U.S. affect Canada's tax environment. Growing awareness of the wealth that resulted from financial transactions and, to a lesser extent, higher salaries for executives in the past decade may lead to increased support for taxes on wealth. If the U.S. makes greater use of taxes on personal wealth, it will encourage the use of similar taxes in Canada.

It is important to recognize that the distribution of wealth in Canada has become much more equal than it was a century ago when the first death tax was introduced in Ontario. Although the top 1 and 5 per cent continue to own a large share of personal wealth, there has been a remarkable decrease in the concentration of wealth in Canada and in other industrialized countries. This achievement may be a major reason for reduced interest in the use of death taxes and other forms of taxation on personal wealth in Canada.

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taxes. Many argue that the tax on deemed gains at time of death, as a tax on deferred income, is an appropriate extension of the income tax, and in no way weakens arguments for taxes levied on the transfer of wealth or on net wealth. A counter-argument is that a tax on nominal (as opposed to real) capital gains when inflation is greater than zero is, in part, a tax on wealth rather than income. Spain is the only OECD country which currently taxes capital gains at time of death and also imposes wealth transfer taxes at time of death. Although the U.S. has death duties, unlike Canada it does not tax capital gains as income at time of death. The base used by the heir in calculating capital gains at time of sale is the value at time of death of the donor.

[19] According to Levy (1987, p. 68), "..in 1973 a young man (in the United States) would have had to spend 21 percent of his gross earnings for payments on a typical home. But in 1984 a 30-year-old man - now a member of the baby boom cohorts - would have had to spend 44 percent of his gross earnings to carry a median-priced home". Similar concerns were heard in Canada.

[20] Cooper (1979) discusses the variety of means available to reduce wealth transfer taxes in the U.S. These include gifts during life, spending money in creative ways that enhance the value of other property that has been transferred to heirs, transferring properties in a form that reduces their marketability and hence their valuation for tax purposes, creating conservation easements consistent with the wishes of heirs, and using trusts and other estate planning techniques. Taxes provide incentives to seek creative solutions to minimize the tax.

[21] The self-employed grew from 11.1 per cent of all workers in 1976 to 14.5 per cent in 1991. This group increased by 71 per cent, while all other workers increased by 25 per cent over the same period.

[22] The U.S. has made it unattractive for Canadians and other non-residents to hold personal wealth in the United States. If such wealth exceeds $60,000 at the time of death, the U.S. Estate Tax rates of from 18 to 55 per cent apply to the value. Such property includes real estate, shares of a U.S. corporation, debt obligations issued by U.S. residents, and other personal property. In contrast, the exemption permitted for residents in the U.S. is $600,000. Nonresidents investing in Canada face no comparable tax.

[23] The mobility of labour and capital in response to wealth transfer taxes is not known. Nonetheless, there is growing evidence that both labour and capital are more mobile than they were decades ago and that tax policy is affected by this. See Bossons (1987), Papke (1987), and Lee and McKenzie (1989) for a discussion of related issues and reference to other materials.