In the line of duty: On wealth taxes, Singapore must decide what it most wants to achieve; and know what it could cost

WHEN Deputy Prime Minister Heng Swee Keat said there was scope to review Singapore's wealth taxes in the Budget 2021 Debate, Chris Woo nearly fell off his chair. Mr Woo is PwC Singapore's tax leader, with a career spanning three decades. He cannot recall when wealth taxes - defined as taxes on an individual's stock of assets, and not on income, profits or transactions - were last given such serious consideration by the government.

Wealth taxes are gaining traction, as countries dig deep to fund their pandemic responses. Calls for net wealth taxes are growing; namely, taxes on an individual's net worth.

Bolivia adopted one in December. This month, US Democrats led by Elizabeth Warren proposed an Ultra-Millionaire Tax Act, which would annually tax households worth over US$50 million by up to 3 per cent.

One-off taxes are also on the table. Argentina - which already had a recurring net wealth tax - passed one in December. This calls on individuals worth over 200 million pesos (S $2.94 million) to surrender up to 3.5 per cent of their wealth in the country, and up to 5.25 per cent of their wealth abroad.

The United Kingdom's Wealth Tax Commission has also proposed a one-off measure.

Meanwhile, a swell in Singapore's super-rich ranks has not escaped notice. Knight Frank's Wealth Report 2021 suggests the number of ultra-high-net-worth individuals (UHNWIs) in Singapore - those with at least US$30 million in net assets - rose 10 per cent last year to over 3,700. That is the third-highest growth recorded globally, and has proven a boon for the wealth management business.

Some see this as an opportunity - even a moral imperative - to extract more dollars from the rich. "We take pride, as we say in our pledge, to build a society based on justice and equality," says Christopher Gee, a senior research fellow at the Institute of Policy Studies who is upfront about his support for wealth taxes. "If we hold to that, then we need to put the prevention of inequality as a goal."

Parliamentarians are also weighing in. Last year, Foo Mee Har of West Coast Group Representation Constituency (GRC) mooted reinstating estate duty; this year, she suggested a one-off tax.

"The defining feature of a one-off wealth tax is that it would be a one-off exceptional response to a particular crisis," she tells The Business Times (BT). "Since it is one-off, it does not distort behaviours."

She adds: "It may not be unreasonable to expect selected entities or individuals, who have enjoyed outsized windfalls because of Covid-19, to do more for the common good."

Where did all those taxes go?

Thirty years ago, 12 countries in the Organisation for Economic Co-operation and Development (OECD) levied net wealth taxes. One by one, they peeled away. Austria (1994), Denmark and Germany (1997) went first, followed by the Netherlands (2001), Finland, Iceland, Luxembourg and Sweden (2006-07), and finally France (2018). Spain repealed the tax in 2008, but reinstated it in 2011.

Now only three (Norway, Spain and Switzerland), and roughly a dozen others worldwide, are left standing.

Why did wealth taxes fail? As it turns out, taxing the rich is not unlike a never-ending round of whack-a-mole. Tax them in one jurisdiction, and they pop up in another. Tax only some asset classes, and they buy up more of others.

A net wealth tax seeks to counter this by taxing everything, everywhere. But that could require an administrative army to hunt down and valuate, well - everything, everywhere: from private companies, to luxury handbags and watches, avant garde paintings and for the Swiss, Alpine cattle.

Especially frustrating for progressive ideals is that the rich have greater access to wealth planning services. They can avail themselves of exemptions, trusts and other means to shield themselves from the taxman, leaving the middle class to bear more of the burden.

They also tend to have more lucrative investments, which means a wealth tax hurts them less compared to those with lower returns on their assets.

These factors help explain why property tax has outlasted most other wealth taxes today, including here in Singapore. It is hard to hide or relocate a house. Valuations are generally straightforward, and ownership is transparently documented.

Properties are also big-ticket purchases, so the tax extracted is high. In the three financial years preceding its repeal in 2008, estate duty raised an average of just S$111 million annually. Property tax on private properties raised an average of S$1.83 billion annually in the same period.

And then there's Switzerland

What about the Swiss? It has been vaunted as a rare example of a wealth tax that works. In 2018, Switzerland taxed everything from livestock to beehives to yield 3.9 per cent of its tax revenues, compared to Norway's 1.1 per cent and Spain's 0.5 per cent the same year.

The reality is a little more complicated. For one, the Swiss have fairly low thresholds for taxable net worth, which means a larger share of taxpayers is affected. As at 2020, thresholds for married couples range from 50,000 Swiss francs (S$72,421) in the canton of Obwalden, to 250,000 Swiss francs in Schwyz.

That said, there are shields in place for the broad middle of taxpayers, such as low tax values for real estate. Despite the low thresholds, most Swiss taxpayers do not pay wealth taxes at all, says Jürg Niederbacher, PwC Switzerland's tax partner and leader for private clients.

That does not make wealth taxes popular among the ones who do - especially the ultra-wealthy, who pay the most. A wealth tax seems inherently more unfair than a tax on income, says Mr Niederbacher. As a result, a number of his clients are constantly seeking solutions to reduce the tax payable - such as moving between cantons, which they can certainly afford to do.

Given this, why aren't the wealthy exiting Switzerland en masse? To understand that phenomenon, Mr Niederbacher stresses, one must look at the Swiss taxation system in totality.

"A lot of very wealthy people derive most of their income from dividends, which are preferentially taxed," he says. "Switzerland is also one of the few countries where capital gains are not taxed."

In other words, the ultra-wealthy are willing to bear with wealth taxes - so long as other forms of taxation are not too onerous. Switzerland reaps value from its wealth tax, but it taxes the rich more lightly in other ways, compared to its regional peers; so the overall burden evens out. That is a balancing act governments will have to puzzle out, if they want to emulate the Swiss story.

Wealth taxes 2.0

With the deep-seated challenges of wealth taxes, should they be ruled out entirely? Not according to Sarah Perret, an economist at the OECD's Centre for Tax Policy and Administration, who joins BT from France on a Zoom call.

Ms Perret advises countries on tax reforms for a living, including as a contributor to the UK's Wealth Tax Commission. The choice of tax instrument, she stresses, all depends on the country's end goal. If the primary aim is to collect more revenues from the rich, while reducing inequality over time, then there are perfectly valid alternatives.

But if the primary aim is to actively and rapidly reduce inequality, then a net wealth tax is the most direct method - and there are ways to design them better.

First, Ms Perret suggests, countries could set higher thresholds for the taxes, to avoid burdening the middle class. France used to tax net assets above 1.3 million euros (S$2.08 million), before it repealed its wealth tax in 2018. Other countries had lower thresholds, which affected some households with moderate levels of wealth and sometimes limited cash.

Second, they could limit exemptions, to keep the tax base broad. "Some exemptions were justified, such as to encourage entrepreneurship, while others were simply due to lobbying," Ms Perret says. "But as a result, the revenues raised from wealth taxes were very limited. Wealth taxes generally accounted for less than one per cent of total tax revenues, in countries where they existed."

Importantly, the operating context has also changed. While valuation remains a challenge, significant progress has been made on the adoption of tax transparency standards led by the OECD, says Ms Perret. "In particular, the Automatic Exchange of Information (AEOI) has been a game-changer."

Under the AEOI, participating jurisdictions - including Singapore - must obtain information from their financial institutions on accounts held by non-residents, and share this with jurisdictions where the account holders are tax residents.

In 2019, nearly 100 countries exchanged information under the AEOI. Tax authorities obtained data on 84 million financial accounts, covering 10 trillion euros in assets.

But guard the golden goose

Despite the advances made, Ms Perret stops short of prescribing wealth taxes for a country like Singapore. Most countries she has worked with do not resemble the small and open city-state, whose light-touch tax regime has been a competitive advantage.

Furthermore, Singapore adopts a territorial basis of taxation, with no taxes on overseas income. If the same principle were applied to a wealth tax - which is usually levied on assets worldwide - this could leave the Republic prone to capital flight.

"Tax residents would only be taxed on assets they own domestically," Ms Perret notes. "They might then have an incentive to invest abroad instead."

As it stands, talk around town about wealth taxes has led to jitters in the wealth industry. "My biggest concern," says PwC Singapore's Mr Woo, "is that we must not harm the golden goose. We've got a pretty good ecosystem. If it ain't broke, don't fix it. Ultimately, the best way to grow revenue in Singapore is to grow the economic pie."

As a tax professional, Mr Woo has a natural interest in keeping Singapore competitive as a wealth hub. But the wealthy are important for larger national reasons, he says. They might set up family offices, growing the financial services sector; lead or invest in businesses and startups, creating jobs; or spend on big-ticket items, boosting consumption.

"Some might say - wow, rich people come in here and enjoy Singapore. But they do pay taxes," he stresses. "When they run a business, they pay taxes. When a tycoon buys a penthouse, they pay taxes. When they employ, their employees pay taxes."

He adds: "If you introduce new wealth taxes, or reinstate old ones - like bringing back estate tax - you are going to create perceptions that you're moving the goalposts. That can have ramifications."

Echoing the call for stability is Adrian Sham, tax partner at Grant Thornton Singapore, who works with high net worth individuals. He is against the idea of a "one-and-done" tax, which Ms Foo has suggested.

He points to Cyprus as an extreme example, where the government raided insured bank deposits in 2013 to meet internationally imposed conditions for a bailout. This caused howls of fury from depositors.

"One of Singapore's key selling points is its stability," says Mr Sham. "If Singapore suddenly imposes a one-off tax, that uncertainty may mean future funds do not come to Singapore."

He adds: "When the government here designs a wealth tax, it has to be something that is sustainable. If another global pandemic happens, will people move money out of Singapore as soon as that happens, to avoid a potential one-off tax?"

The ends decide the means

Ultimately, no one who spoke to BT for this story opposes higher taxes on the rich; nor do they appear fixated on rigid policy prescriptions. Across the board, they emphasise principles and outcomes over the means: progressive taxation, to reduce inequality; healthy and efficient revenue collections, to support national spending; and growth, to improve livelihoods.

In the end, the answers may lie in what the nation chooses to prioritise. A net wealth tax - with high thresholds, and few exemptions - could take a sledgehammer to inequality.

But considering potential trade-offs to growth, overall tax revenues and efficiency, Singapore might opt for a scalpel instead - through targeted new taxes, or simply by raising the rates of existing ones.

As Ms Perret points out, "There are features of Singapore's system that are striking to me, like the absence of capital gains or estate tax. I'm not saying you shouldn't have discussions about (net) wealth taxes. But there appear to be other avenues that could be considered first."

PwC Singapore's tax partner Paul Lau sums it up thus: "I don't have a specific policy answer. We should study the impact of these measures, and find a sensible, efficient way to proceed - in a fashion where investors continue to have confidence in the economy, you drive the right behaviour from entrepreneurs, and we can address socio-economic hardships through transfers.

"If indeed, you've done that study, and you land on the best way to do it - even if it's introducing a new tax - then fine," he muses. "Then it's a matter of communicating that to people, to say 'This is best for the country'."