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Task Force 01
FIGHTING INEQUALITIES, POVERTY, AND HUNGER

The Taxation of Wealth for Eradication of Poverty and Inequality

Zimbali Mncube, Reseacher in Tax and Budget Policy, Institute for Economic Justice (IEJ) [South Africa]
Diana Mochoge, Policy Research and Advocacy Officer, African Forum and Network on Debt and Development (AFRODAD) [Zimbabwe]

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Abstract

This policy brief will discuss how tax policy can contribute to a just and sustainable planet as per the G20 theme in 2024. The brief discusses how tax policy and in particular taxing wealth can support domestic resource mobilisation. The paper discusses tax instruments such as Financial Transaction Taxes (FTTs) and net wealth taxes and their revenue potential and economic impacts. As stated in the International Human Rights framework, these tax instruments are one of the interventions required to reform the macroeconomic framework to target inequality, unemployment, and poverty. The recommendations flowing from the paper align with SDG 1 on eradicating poverty and SDG 10 on reducing inequalities. The G20 provides a critical platform for world leaders to continue discussing resource mobilisation efforts towards SDGs 1 and 10.

Keywords: Taxation, Wealth, Inequality, Financial Transaction Tax, Net Wealth Tax, Domestic Resource Mobilsation, Poverty, Resource Rent Tax.

Diagnosis of the issue

This brief aims to discuss how a progressive tax agenda can contribute to domestic resource mobilisation for eradicating poverty and reducing inequality. It presents a set of tax instruments, their impact on alleviating inequality, and revenue potential.

Economic inequality is increasingly becoming the central issue, and it affects the most impoverished globally. It has been an obstacle to addressing poverty and climate resilience within countries and between countries. The latest World Inequality Report (2022) has shown that in richer countries, over the past 40 years, wealth has been concentrated in private actors rather than the public (Chancel, L., Piketty, T., Saez, E., Zucman, G., et al, 2022). The COVID-19 pandemic has exacerbated the concentration of wealth to the top 1%. Since the mid-1990s, the top 1% has accumulated 38% of all wealth while the poorest 50% only accumulated just 2% (Chancel, L., Piketty, T., Saez, E., Zucman, G., et al, 2022).

In Sub-Saharan Africa, 18.2 million live in extreme poverty, with little access to basic services such as healthcare, education, and clean water. Over 389 million people in Sub-Saharan Africa were living in extreme poverty in 2018 (World Bank, 2022). This means they were living on less than $1.90 per day. Despite the region's economic growth over the past two decades, inequality has remained persistent, with the poorest households often experiencing little to no improvement or a decline in their income. There is a large wealth gap between the rich and poor, with the wealthiest 10% of the population owning more than half of the region's wealth. Despite this, compared to other regions, such as the Asia-Pacific and OECD, Africa has a tax structure heavily weighted towards consumption taxes. In 2021, VAT generated 27.8% of total tax revenue on average in Africa, while the

Asia-Pacific region averaged 25.6% and the OECD 20.2% (OECD, 2023). This is regressive and inflicts a significant burden on low and middle-income households.

Overall, the Southern part of Africa is the most unequal with Namibia, Comoros, South Africa, Angola, Botswana, Lesotho, and Swaziland being in the top ten of the most unequal countries in Africa. However, inequalities have been slightly reducing in Southern Africa over the last decade whereas inequalities have increased in most of the other regions of Africa, although remaining lower than Southern Africa level. This, therefore, provides a very worrying picture and shows how crucial the inclusive growth agenda is for Africa.

In a 2022 report published by the New World Wealth and Henley & Partners, Kenya is ranked 5th in Africa in terms of the number of high net wealth individuals (HNWI), with an estimated 5,000 US-dollar millionaires residing in Nairobi with less than 0.1% of the general population owning more wealth than the remaining 99.9%. However, in countries such as Zimbabwe, there have been some progressive developments in tax policy. The new Finance Act, 2023 (No. 13 of 2023), which came into operation on the 1st of January 2024, introduced a new tax, a wealth tax. The tax targets the country's super-rich to use the funds earned from the new measure to upgrade urban infrastructure and also close the inequality gap.

It is important to note that European countries, especially Scandinavian countries, have much lower Ginis which ranges between 0.24 and 0.27. Progressive tax policy is one of the contributory factors to such low Gini coefficients. In contrast, South African inequalities extend to all forms of assets, with the richest 10% owning 99.8% of bonds and stock – which accounts for 35% of wealth. The top decile also owned 60% of housing wealth and 64% of pension assets. Housing wealth amounted to 29% of wealth and

pension assets to 33% (Charttejee, Czajka, and Gethin, 2020). Moreover, just 3,500 individuals have 15% of the country's wealth; the top 1% own 55% of the nation's wealth, while 50% of the population lives from hand to mouth, with virtually no savings cushion (Chatterjee, Czajka, and Gethin, 2020).

Overview of Wealth Tax Instruments for Domestic Resource Mobilisation

This section discusses the various tax instruments that should be considered as part of an agenda to enhance domestic resource mobilisation raise revenue for climate justice and eradicate poverty and inequality. These are not exhaustive and can be promoted by the G20 and taken up by developing countries in a manner that suits their contexts and administrative capacities.

Financial Transaction Tax

A financial transaction tax has been on the G20 agenda since 2011 without considerable action. In 2023, Kumar and Gallagher (2023) estimated that foreign exchange transactions exceeded $7.5 trillion per day as of April 2022. The scale of daily financial transactions is a boon for resource mobilisation through instruments such as the FTT. A FTT is important not just for its revenue but, more fundamentally, for its potential to curb speculative flows, short-term trading, and market failures. An FTT would "dampen the transaction volumes of financial products that are excessively complex and opaque or are purely based on "irrational exuberance", inflated expectations or behavioural biases" (Shiller, 2006; Pekanov, and Schratszenstallar, 2019: 05). Thus by increasing transaction costs, an FTT would reduce excessive trading and improve productive investment (Wamhoff, Roque, and Schieder, 2019).

The International Trade Union Confederation (ITUC) first called for an FTT to be taken up in 2010 at the Summit for the General Assembly on the MDGs. The ITUC (2020) showed that an FTT could generate from $200 billion to $900 billion annually, depending on the specific types of taxes and the rates at which they are set. According to Kumar and Gallagher (2023) an FTT levied at 0.05% could generate $900 billion annually, and even taking into account the decline in financial transactions, it could still generate between $603 - $675 annually. According to Pekanov and Schratzenstaller (2019) at a rate of 0.1% on the trading of stocks and bonds instruments and 0.01% on transactions of derivatives, the FTT could raise $237 billion per year at a conservative estimate and $418 billion on a more optimistic estimate.

This year presents an opportunity for the G20 to put back FTT on its agenda. In 2011 over 1000 leading economists from 53 countries signed a letter supporting the call for a FTT (The Guardian, 2011). The G20 Brazilian Presidency has supported progressive taxation through a proposal for a FTT policy adoption at the G20 can also lead to member states and regional bodies advocating for its adoption in international multilateral forums.

Taxing Wealth

The world's richest individuals enjoy favorable taxes while the working class continues to shoulder tax increases. For example, billionaires have effective tax rates equivalent to less than 0.5% of their wealth (EU Tax Observatory. 2023). On the other hand, an average tax paper paid 13% in tax in the US in 2021. A wealth tax on the richest individuals is one of the proposals that need to be considered to raise revenue for poverty reduction, expand social protection and healthcare, and support a just transition.

Although the use of net wealth taxes has decreased in Europe, those remaining still generate meaningful revenue. From 1965 to 2021, Spain, Sweden, Norway, and Switzerland have, on average, generated annual Net Wealth Tax revenues to the tune of 0.47%, 0.49%, 1.36%, and 4.7% of their respective GDPs. In contrast, net wealth taxes have been growing in usage in Latin America. The revenues generated in Latin American countries have been comparable to those in Europe. As a share of GDP, revenues have averaged 1% in Argentina since 1990, 2% in Colombia since 2002, 0.2% in Ecuador since 2009, and 3.5% in Uruguay since 1990 according to OECD.

The recent developments of an international framework on tax in the UN signal progress towards the right direction. It will lay the groundwork for progressive taxation and a global wealth tax. The G20 needs to support the development of a UN framework on International Tax and Cooperation and ensure that a wealth tax is one of the key issues in this convention. There is potential for a wealth tax to alleviate global inequalities and help developing countries raise revenue to support sustainable development goals. The EU Tax Observatory (2023) estimates that wealth tax on the richest 3000 globally could raise about $250 billion. While the proposal is a good starting point, it is limited to billionaires, most of whom reside in the Global North. Thus leaving much of the wealthy in the Global South still undertaxed. The G20's support of the wealth tax will ensure that countries also take it up domestically.

Property taxation

A property tax (PT) is generally levied as an annual tax on the value of real property, such as land and buildings. These taxes are considered efficient and equitable sources of revenue because property and land assets are visible and immobile. There are exceptions

to this definition as capital invested on land in general and non-residential activities like businesses, in particular, could be mobile. PT is one of the most lucrative yet still the least tapped sources of tax revenue to support the urban government in Africa. Developing countries only collect 0.5% of PT as a share of their GDP compared to 2% of developed countries (Ali, Fjeldstad, and Katera, 2017). This was due to poor tax administration, lack of capacity, and lack of will from some political and religious leaders. Property tax is equitable and efficient. It is a well-targeted tax, considering that high-income earners and the wealthy often own property. Furthermore, the taxation of property does not affect resource allocation by impacting decisions on whether to supply or invest capital.

Taxing the extractives sector: Resource rent tax

Africa has a wide range of natural endowments, including fisheries, minerals, fossil fuels, and timber. These resources provide an opportunity for governments to raise revenue. The Resource Rent Tax (RTT) is a tax extracted on economic rents in the commodities sector. An economic rent is defined as that portion of value-added that exceeds the costs of all the factors of production, including the required return on capital. It accrues to firms when outputs are priced at levels exceeding what is necessary to cover their inputs and a required profit margin. Taxing such a rent will, by definition, have no impact on investment decisions as it will theoretically only be levied on the portion of profit above the investors' required rate of return.

Governments raise revenue from extractive industries through taxation (corporate income, value-added tax, royalties, personal income tax, customs duties, and withholding taxes) and direct ownership (with State-owned companies or joint ventures). Revenue

from taxing extractives has a huge potential to transform economies and reduce inequalities in the region.

Scenarios: Potential Tax instruments and revenue

In this section, we discuss examples of progressive taxation that could raise substantial revenue for the realisation of socio-economic rights using South Africa as a case. Table 01 below illustrates examples of progressive taxes that can be implemented using the case of South Africa to show their revenue potential. If these taxes are taken up, substantial revenue could be raised to support the expansion of social protection and implement a Universal Basic Income Guarantee (UBIG), resourcing healthcare and education and improving government spending on social and economic infrastructure. This will set the economy on a path of inclusive growth and development.

TABLE 01. Proposed progressive taxes and their revenue potential

Tax	Policy measure	Revenue potential for 2023/24 (R billions)
Net Wealth Tax	Progressively levied between 3% - 7%	R 70- R160 (2018 rands)
Securities Transaction Tax	Increasing the STT from 0.25% on all security transfers to 0.3%.	R 1.41
Financial transaction tax	Lower the STT rate to 0.1% but broaden the base to include the equity, interest rate, interest rate derivatives, and commodity derivatives markets	R 41.00
Resource Rent Tax	Levied at 25%	R 38
Estate duty	Estates valued between R3.5 million and R30 million are taxed at a rate of 36%, Estates valued between R30 million and R146.8937 million are taxed at a rate of 41%, and Estates above R146.89 million are taxed at a rate of 45%.	R 1.87

Taxing financial transactions

Currently, South Africa levies a Securities Transaction Tax (STT) on the transfer value (sale/transfer/assignment/cession amount) of a transaction on a company's securities in South Africa or any other company listed on any securities exchange in South Africa at the rate of 0.25%.

The tax revenue from such could be expanded in two ways. The first is by increasing the rate. A rate of 0.3%, for example, would raise approximately R1.5 billion. Second, a broader Financial Transactions Tax (FFT) levied across a wider range of financial

instruments traded on the JSE, levied at only 0.1%, could raise more than R40 billion (Table 01). A Currency Transaction Tax (CTT) levied on the trading of rands of as little as 0.005% could raise an additional R4 billion.

Net Wealth Tax

The Southern Center for Inequality Studies (SCIS) has shown that a Net Wealth Tax has the potential to raise between R70 and R160 billion[1] when levied at progressive rates of between 3-7% (Chatterjee, Czajka, and Gethin, 2021). By their 2021 estimation, that revenue would be 1.5% to 3.5% of GDP, which would be in line with the contribution of wealth taxes in both Europe and Latin America. A recent report by Applied Development Research Solutions (ADRS) and IEJ showed that a wealth tax can partly be used to support a basic income grant, providing much-needed poverty alleviation and economic stimulus. The study found that a 'high-ambition' basic income grant scenario can raise average GDP growth from 2.2% in the baseline year of 2023 to 3.5% on average by 2030 (IEJ, 2024). Progressive taxation is, therefore, not only important to support and protect livelihoods but can play a key role in contributing to the growth of the economy.

Dividend tax and estate duty

In SA, the dividend tax is levied on dividends issued by companies is currently 20%. This is well below both personal and CIT rates. This means that persons and companies wealthy enough to invest in shares, or who inherit them, are taxed on the income they receive from owning these shares well below the tax rate faced by those working for a living. Increasing this rate from 20 to 25% would have raised approximately R8 billion in 2023 (DNA Economics, 2021).

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Similarly, estates with a value of R3.5 to R30 million are also taxed at 20%, while estates with a value of more than R30 million face a tax rate of 25%. This means that those benefiting from such inheritance are again being taxed less than those earning modest wage income. A DNA Economics (2021) report from 2021, showed that aligning this tax rate with income brackets would raise R2 billion in revenue in 2023.

The tax instruments above have varying degrees of complexity. Thus it is important to look at National bodies' tax administrative capacity before discussing which tax would be the most ideal. The tax instruments alone would not assist in fighting the challenges in this subtopic but need to be coupled with supportive industrial policy and a supportive macroeconomic framework.

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