Abolish the Billionaires?

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With the richest people in the world continuing to amass ever more wealth, few would dispute that economic inequality is on the rise, or that current disparities will keep growing in the absence of more progressive taxation. But while tax reform is certainly necessary to solve the problem, it is not sufficient.

- Emmanuel Saez and Gabriel Zucman, *The Triumph of Injustice: How the Rich Dodge Taxes and How to Make Them Pay*, Norton, 2019.
- Kenneth Scheve and David Stasavage, *Taxing the Rich: A History of Fiscal Fairness in the United States and Europe*, Princeton University Press, 2016.
- Thomas Piketty, *Capital and Ideology*, Harvard University Press, 2020; *Capital et idéologie,* Éditions du Seuil, 2019.

MILAN – The march of the billionaires has seemed unstoppable. Even as the International Monetary Fund warns of a synchronized global slowdown, the wealth of the very rich continues to grow unabated. According to Oxfam, the number of billionaires in the world has almost doubled since the 2008 financial crisis, with a new billionaire created every 48 hours. Last year, the 26 richest people on Earth had a combined net worth equal to that of the poorest half of the world's population – some 3.8 billion people.

But political attitudes toward the wealthy are changing, particularly in the United States, where great fortunes have always been considered a reward for talent, creativity, and risk-taking. In 1992, while campaigning for president against the incumbent, George H.W. Bush, Bill Clinton promised tax policies that would create more millionaires than each of the previous two administrations had done. But now, aspiring Democratic presidential candidates are proposing wealth taxes, steeper income-tax rates, and more biting inheritance taxes.

Senators Elizabeth Warren and Bernie Sanders, in particular, have advanced highly contentious wealth-tax plans. Warren wants to tax wealth above $50 million at 2% and wealth above $1 billion at 3% (and she has since suggested doubling these rates to pay for a "Medicare for All" plan). Sanders, who has explicitly stated that "billionaires should not exist," would impose even higher taxes on the extremely rich, with rates reaching 8% for wealth over $10 billion. And if American tycoons try to renounce their US citizenship to escape the levy, they would face an exit tax of 40% on their net worth (and 60% on assets worth more than $1 billion).

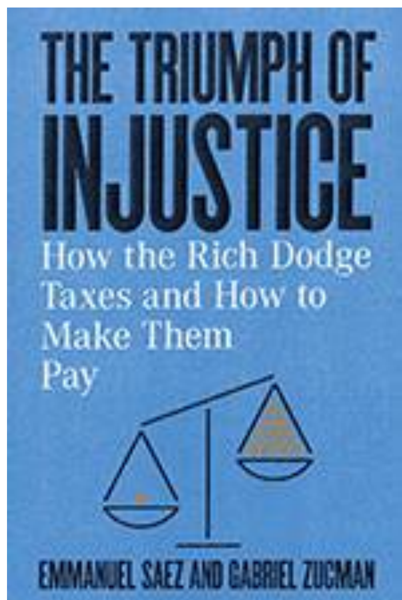
Motivating these proposals are much broader concerns about rising inequality. In the US, the concentration of wealth at the very top is symptomatic of a socioeconomic system that promotes the interests of the few, squeezes the middle class, and perpetuates undeserved privileges across generations. Of the world's 2,604 billionaires, 25% are Americans, and their share of total US wealth has almost quadrupled over the last 40 years, from under 1% in 1982 to 3.5% today.4

Three recent books seek to explain why American society has grown so unequal, and how the rich can be made to pay their fair share. Each embraces the premise that taxing the super-wealthy more heavily could restore a lost sense of social justice. And yet,

without a reimagining of America's broken social contract, such policies would not be enough to restart the engines of social mobility and promote greater equality of opportunity.

TAX INJUSTICE

Among those leading the fight against American billionaires are economists Emmanuel Saez and Gabriel Zucman of the University of California at Berkeley. The two French academics, both longtime collaborators with the inequality guru Thomas Piketty, have advised Warren on the design of her proposed wealth tax. In *The Triumph of Injustice*, they offer an historical and statistical account of the rise of America's super-rich, focusing specifically on the role played by a rigged and unjust tax system.



The book's analysis confirms financier Warren Buffet's famous observation that his tax rate is lower than his secretary's. According to Saez and Zucman, in 2018, the effective tax rate paid by the richest 400 US households was just 23% – roughly five percentage points lower than the average rate for the population as a whole. Given that the US tax code has undergone a complicated evolution over time, the reliability of these estimates – which account for capital, income, and consumption taxes – is the subject of a lively academic debate. But the upshot is clear: a US tax system that is billed as progressive is nothing of the kind.

To explain this fiscal aberration, Saez and Zucman have constructed a historical database that tracks the tax payments of households along the income spectrum going back to 1913, when the federal income tax was introduced. While the individual income tax is formally progressive – with a graduated tax rate going from 0% for the lowest earners to 37% for the highest – most billionaires do not pay income tax at all. The bulk of their earnings come from dividends, which are not only taxed at a rate of just 20%, but also are exempted from Social Security payroll taxes, which are levied on labor earnings only.

The other major source of fiscal injustice is represented by consumption taxes. In the US, sales and excise taxes exempt most services, which are consumed more voraciously by the rich than by members of the working class. Country club memberships and lawyer fees, for example, are not subject to any sales tax, whereas purchases of food, clothes, or home appliances are. And because excises are a function of quantity rather

than price, a bottle of a renowned French wine will be taxed at the same rate as boxed wine.

IN PRAISE OF PROGRESSIVITY

By taking a long historical perspective, Saez and Zucman dismantle the idea that today's tax system simply reflects an American aversion to high taxation and intrusive government. It's true that the American Revolution was triggered by King George III's efforts to impose stifling taxes on the colonies. But the broader history of taxation in America is predominantly a story of progressivity and redistribution.

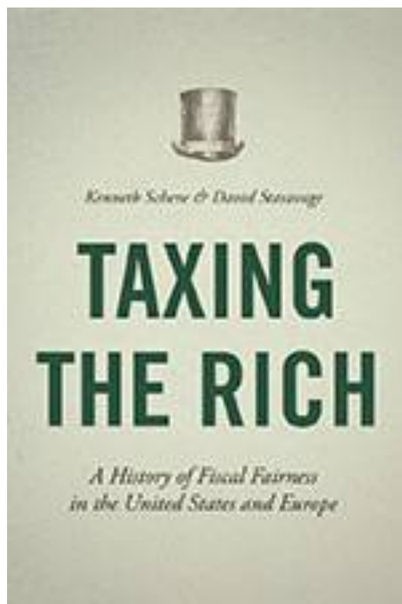
For example, in the seventeenth century, the Massachusetts Bay Colony enacted a wealth tax on most forms of property, including land, ships, jewelry, and livestock. And when sharply progressive taxation was introduced in the twentieth century, it was not a Scandinavian invention but an American one. In 1917, the US became the first country to impose top marginal tax rates as high as 67%, and in the 1930s it became the first country to levy an estate tax as high as 70%. In 1950, the average tax rate for the top 400 earners in the US was 70% – three times higher than the effective rate at which they are taxed today.

How were such high tax rates possible? For starters, egalitarianism, not elitism, is deeply woven into the American cultural and political fabric. During his travels through America in the 1830s, Alexis de Tocqueville was struck by the general equality of socioeconomic conditions, which were nothing like those of France. And a century later, Franklin D. Roosevelt made economic equality a priority for his presidency. In 1942, he declared that "no American citizen ought to have an income, after he has paid his taxes, of more than $25,000 a year," which is equivalent to just $1 million in today's money. Roosevelt even proposed a 100% tax rate on every dollar earned above that level. That was too much for the US Congress, which reduced it to 94%.

But attitudes toward tax progressivity started to reverse in the 1970s, owing to the threat of capital flight, the emergence of an aggressive tax-dodging industry, and the intensification of global tax competition. Since then, average tax rates have declined for everyone, including the poor. But the rich have benefited the most – and massively so. The top marginal federal income tax rate has fallen from 70% to 37%. The corporate tax rate has declined from about 50% to 16%. And estate taxes on large bequests have proved to be highly ineffective, owing to exemptions and deductions.

SOAK THE RICH

Against this backdrop, Saez and Zucman think it is only natural that the rich should be made to pay more in taxes to fund educational, medical, and infrastructure projects. In particular, they propose an overall tax rate of 60% on the top 1% of earners, which would boost tax revenues by an estimated 4% of GDP. They also argue that American companies should pay a global corporate tax rate of at least 25% on their profits, regardless of where their legal entities are located.



Similarly, in *Taxing the Rich*, Stanford's Kenneth Scheve and David Stasavage of New York University use the experiences of 20 countries over the past two centuries to argue that now is the time for a radical overhaul of the tax system. Blending historical, economic, and statistical analysis, they provide an overview of the standard justifications for imposing high taxes on the rich, with a focus on the three principles of fairness, equity, and compensation.

Fairness might dictate that the rich should pay a higher tax rate simply because they can, and because they have a much higher propensity to save. But Scheve and Stasavage show that, historically, higher top tax rates generally have not followed as a political response to higher pre-tax inequality. Similarly, equity seems to dictate that democracies should adopt progressive taxation because the poor outnumber the rich. But, again, in the past, progressivity has not tended to increase as a result of the extension of suffrage.

By contrast, Scheve and Stasavage show that compensation underpins the most robust arguments in favor of progressivity, which have generally been most persuasive in the face of some fundamental state-induced unfairness that cannot be removed otherwise. During the two world wars, for example, ordinary citizens expected compensation from the rich – framed as a "conscription of wealth" – for the effects of mass military conscription and wartime deprivations.

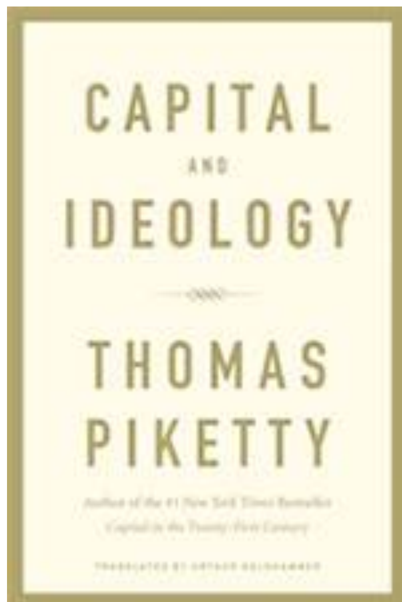
Moreover, during WWI, the US introduced a stifling tax on the munitions industry to prevent the emergence of a "shoddy aristocracy" of war profiteers. From this perspective, the high degree of progressivity that characterized the first half of the twentieth century was more a historical exception than a political victory.

Yet even in the absence of a war that enlists the masses and beefs up the upper class, inequality in the US seems to be approaching the threshold of intolerability. The meritocratic mantra that has long underpinned the American Dream and justified unequal outcomes has begun to lose its appeal as wealthy families monopolize the best educational, social, and economic opportunities. According to economist Raj Chetty of Harvard University and his co-authors, whereas 90% of Americans born in 1940 ended up better off in real (inflation-adjusted) terms than their parents at the same age, that is true of only half of those born in 1980. Having been marginalized by a system that

enriches the few while cynically promising a better future for all, voters are now demanding redistribution as compensation.

PIKETTY'S CHARGE

Today's rising public anger over inequality should not come as a surprise. As Piketty shows in his new 1,200-page tome, *Capital and Ideology*, inequality is less a product of nature than the result of conscious political choices that are supported by a well-developed ideological apparatus. Through what he calls the "sacralization of property," every unequal society creates an ideology to legitimize the prevailing distribution of resources and to justify social divisions and classes (nobility, clergy, working class, bourgeoisie) – or, in India's case, hereditary castes. The Protestant ethic, for example, treats worldly success as a form of divine reward, and has thus proven effective in justifying the inequalities of the Anglo-Saxon world.



Nonetheless, Piketty goes on to show that when the prevailing ideology is called into question, the entire socioeconomic structure can crumble, at which point a new ideology must be developed to legitimize inequality once again. To back these claims, Piketty (whose book is currently available only in French, but is forthcoming in English next spring) takes readers on a world tour through the centuries. His goal is to demonstrate how asset ownership has been justified in different societies with vastly different histories, from China, Japan, and India, to feudal and capitalist Europe, and on through the periods of colonialism, transatlantic slavery, and communism. But such sweeping ambition comes at a cost, and Piketty inevitably must simplify the discussion of ancient societies and the evolution of beliefs and socioeconomic structures over time.

Piketty is at his best when explaining how political competition has evolved in contemporary Western societies, and why the meritocratic ideology that supports the current socioeconomic model is now in crisis. In the 1950s and 1960s, he notes, left-wing parties worked hard to open up education and high-income opportunities for working-class households. But since then, they have become victims of their own success, in the sense that they have increasingly come to represent the educated and affluent middle and upper-middle classes. Those who did not manage to climb the social ladder, meanwhile, have been left behind.

Thus, in Piketty's jargon, left-wing parties became the parties of the "Brahmin left," as opposed to the conservative right-wing parties, which remained the representatives of the wealthy and the "merchant right." But as social mobility has become increasingly unavailable to a growing share of the population, populist parties have found fertile ground on which to question the predominant ideology.

Ultimately, *Capital and Ideology* turns out to be as much a political manifesto as a scholarly treatise. Piketty calls for today's flawed capitalism to be replaced with a new system of participatory socialism. To that end, he suggests a number of radical reforms, not just for the US but for the world. In his view, the ownership of property should be made temporary, particularly in the case of extremely large fortunes. In fact, he would tax billionaires out of existence – through a confiscatory wealth tax and highly progressive estate and income taxes – and funnel the revenues toward public goods, social insurance, and a basic income for the poor.

MISDIRECTED ENERGY

Critics of inequality in America have a point. There is ample empirical evidence to show that extreme concentrations of wealth distort economic policies, misallocate resources, and undermine growth. Moreover, with extreme economic power comes the risk of a "wealthification" of politics, with those at the very top of the income distribution steering policy outcomes in their favor. In the US, the wealthiest 0.01% already account for over 40% of political contributions.

Yet scapegoating a small group of individuals for all of America's misfortunes is delusional. Not all billionaires are created equal. In some cases, outsize fortunes are indeed the result of political cronyism, rent seeking, or poor regulation. But if the goal is to prevent *unmerited* wealth accumulation and its attendant effects on politics, targeted regulations and caps on individual electoral contributions would be more effective than sweeping taxation.

Besides, in many contemporary cases, billionaires' fortunes are the result of exceptional talent or achievement. Most of the Americans who populate the top of *Fortune*'s net-worth rankings are visionaries like Amazon's Jeff Bezos, Microsoft founder Bill Gates, or Michael Bloomberg of Bloomberg LP. Demonizing these entrepreneurs for their wealth is counterproductive. After all, the fact that someone can build such an immense fortune (and such large, effective philanthropic organizations) in a single generation indicates that the engine of American capitalism is working. Moreover, the continuous reshuffling at the top of the *Fortune* list is indicative of a virtuous process of wealth creation, rather than cronyism or plutocratic collusion.

This is not to suggest that the wealthy should be exempted from paying their fair share of taxes through higher progressivity and curbs on the tax-dodging industry. Many billionaires – not least Buffett and Ray Dalio of Bridgewater Associates – would agree. But we should be wary of rhetoric that conflates equality of opportunity with equality of outcomes. Piketty's extreme, confiscatory logic leads him to focus more on punishing those who are professionally successful than on empowering those who are lagging behind.

THE ROOT OF THE PROBLEM

At the end of the day, a flawed or skewed tax system is merely an amplifier of inequalities that actually stem from other forces, such as globalization and technological innovation. As such, pursuing more punitive taxation might dampen the inequality problem, but it cannot solve it. True, additional tax revenues can be used to improve

public education, infrastructure, and other goods on which lower-income households rely. But the rich will always find ways to prosper, even if it means fleeing abroad in the face of a confiscatory threat.

Addressing the ultimate causes of inequality requires a change of mindset, not just a redistribution of economic resources. The top priority, then, should be to restore meritocracy to a system that now perpetuates undeserved privileges. Private donations to top universities, for example, should be welcome, but legacy admissions should be banned if the prospective student lacks the necessary academic credentials.1

In today's America, the main sources of inequality are immaterial. Gender, age, race, and geography remain major obstacles to the free circulation of talent, ideas, and wealth. These traits are just as predictive of professional success as is one's household income at birth. Opening up the ladder of social mobility requires removing these pervasive barriers.

It is certainly time for America to reestablish some tax justice. But abolishing billionaires won't solve the problem of widening inequality on its own. That will require a new social contract.