FABIAN SOCIETY FRIEDRICH EBERT STIFTUNG

# APPENDIX

## **A Unique Contribution**: Reducing budget deficits and tackling inequality with a one-off wealth tax **| Nick Donovan**

This appendix sets out several stylised case studies, which illustrate certain features of the one-off levy. All names are fictitious and are not intended to represent real people. For illustrative purposes we have made the following assumptions about key features of the levy:

- The assumed average annual rate of return is 5%.
- The personal chargeable wealth allowance is £10,000,000.
- The higher rate chargeable wealth threshold is £20,000,000.
- The lower rate is 5%.
- The higher rate is 10%.

For simplicity it is assumed that inflation is zero throughout the period.

Figures in green are ignored in the calculations.

## Case study 1: Roddy Winshaw

Roddy Winshaw is a Canadian investment banker who has been living in the UK for five years. Alongside his large salary and annual bonus he's received numerous share options. He has a large buy-to-let property empire. He also owns two holiday homes, one of which he lets friends and family use for free some of the time, and one of which he occasionally uses but makes available on the open holiday lettings market at other times. He owns his house outright (and jointly with his wife, who has very little wealth of her own).

Roddy is a low risk taxpayer.

### Income

| | **Salary & bonus** | **Rental income** *- buy to let empire* | **Occasional letting income** *- holiday home* |
|---|---|---|---|
| *2010* | N/A | N/A | 0 |
| *2011* | 1,500,000 | 1,000,000 | 0 |
| *2012* | 1,500,000 | 3,000,000 | 15,000 |
| *2013* | 1,500,000 | 3,000,000 | 5,000 |
| *2014* | 1,500,000 | 3,000,000 | 0 |
| *2015* | 1,500,000 | 3,000,000 | 7,500 |

### Assets

| **Asset** | **Value** | |
|---|---|---|
| *Family home* | £ | 10,000,000 |
| *Holiday home exclusively used by family* | £ | 5,000,000 |
| *Holiday home occasionally let* | £ | 2,000,000 |
| *Share options* | | N/A |

### Tax calculation

Roddy's salary (and bonuses), and occasional letting income, are both ignored in the following calculation of deemed investment wealth. The income in the form of his salary and bonuses is excluded as it is employment income, and the income from the holiday home is ignored because the asset is valued in the calculation of untenanted real property. Only the income from the last four years is considered. Roddy's share options, which are in any case often difficult to value until they are exercised, are ignored as they are related to his employment activity.

| Calculation | £ |
|---:|---:|
| ***Deemed investment wealth*** | |
| *Top income in 4 yrs* | 3,000,000 |
| *Deemed investment wealth (£3,000,000/5%)* | 60,000,000 |
| | |
| ***Deemed chargeable wealth*** | |
| *Deemed investment wealth* | 60,000,000 |
| *Untenanted real property* | 17,000,000 |
| | |
| ***Total*** | 77,000,000 |
| | |
| *Personal allowance* | 10,000,000 |
| | |
| *Relevant deemed chargeable wealth* | 67,000,000 |
| | |
| *Tax due at lower rate* | 500,000 |
| *Tax due at higher rate* | 5,700,000 |
| | |
| ***Total tax due*** | 6,200,000 |

## Case study 2: Dorothy and Mark Winshaw

Dorothy is a member of an old British aristocratic family that lives in a stately home, Winshaw Towers, owned by a charitable trust which opens the house to the public. She pays rent to the trust for her apartment in the house; it used to be market rent but the trustees have omitted to put her rent up in line with market rent increases in recent years. She owns a number of extremely valuable 'Old Master' paintings and pieces of antique furniture, and a large tract of agricultural land, all of which were left to her upon the death of her father two years ago. The agricultural land is mostly leased to a large corporate agricultural concern, and she uses the remaining plots to operate, as a lone trader, a small organic farm raising speciality pig breeds. She also owns (subject to a mortgage) a flat in Bristol which she bought for her son when he was at university there; it is now let on the open rental market. She receives intermittent cash payments from a Swiss bank account, which she is conscious has something to do with an arrangement set up by her late uncle Godfrey and cousin Mark, but she doesn't know much about it. She declares the payments on her income tax return as miscellaneous income.

Dorothy's cousin Mark made a huge fortune in the late 90s doing shady arms deals and declared almost none of the income; instead he placed it in an originally more modest but elaborate offshore family trust structure originally established by his late father. Mark spent much of his life not resident in the UK but is now living out his retirement in a smart but unobtrusive house he owns in a Yorkshire village near Winshaw towers. Mark has an extremely expensive lifestyle funded by a very high income from the family trust. Alongside Dorothy a few other members of the family also receive payments from the offshore trust structure.

Dorothy is a low risk taxpayer. Mark is a high risk taxpayer.

### Income (Dorothy)

| | *Income from Swiss account* | *Rental income - Bristol flat* | *Agri-business rent* | *Trading income from organic pig farm* |
|---|---|---|---|---|
| *2010* | 175,000 | | 150,000 | 20,000 |
| *2011* | - | | 150,000 | 20,000 |
| *2012* | 850,000 | | 150,000 | 20,000 |
| *2013* | 250,000 | | 150,000 | 20,000 |
| *2014* | - | 24,000 | 150,000 | 20,000 |
| *2015* | 400,000 | 24,000 | 150,000 | 20,000 |

Dorothy is not a high risk taxpayer because she isn't settlor of the offshore account, but a beneficiary. Her income as a sole trader running a pig farm is excluded from the calculation of deemed investment wealth, as it is trading income.

### Assets (Dorothy)

| ***Asset*** | ***Value*** |
|---|---|
| *Property (Apartment in stately home)* | 250,000 |
| *Fine art and antiques* | 25,000,000 |

As the trustees did not increase the rent of Dorothy's apartment in line with market values part of the value of her apartment has been attributed to her. This is the capitalised difference between the market rent and the rent she has actually paid. For example, if her rent was in effect subsidised by, say, one quarter, then one quarter of the value of the apartment would be attributed to her. Her inherited collection of antique furniture, rare books and 'Old Masters' are excluded from the calculation of deemed chargeable wealth as no leasing market exists for them, and they are incapable of yielding a passive income.

### Tax calculation (Dorothy)

The income from the Swiss bank account has been lumpy, with a large payment of £850,000 made in 2012. This affects the calculation of deemed investment wealth. It would be open to Dorothy to make a claim to for her asset (the share of the offshore trust which would be attributable to her) to be valued instead but her family are reluctant to have the sources of their wealth investigated and therefore have encouraged her not to claim.

| Calculation | £ |
|---:|---:|
| ***Deemed investment wealth*** | |
| *Top income in 4 years* | 1,000,000 |
| *Deemed investment wealth (£1m/5%)* | 20,000,000 |
| | |
| ***Deemed chargeable wealth*** | |
| *Deemed investment wealth* | 20,000,000 |
| *Untenanted real property* | 250,000 |
| ***Total*** | 20,250,000 |
| | |
| *Personal allowance* | 10,000,000 |
| | |
| *Relevant deemed chargeable wealth* | 10,250,000 |
| | |
| *Tax due at lower rate* | 500,000 |
| *Tax due at higher rate* | 25,000 |
| | |
| ***Total tax due*** | 525,000 |

## Assets (Mark)

Mark is a high risk taxpayer because he transferred assets into a bank account in a secrecy jurisdiction within the relevant twenty year time period. Therefore his assets are valued directly rather than imputed from his income.

| Asset | Value |
|---:|---:|
| *Property* | 9,000,000 |
| *Offshore wealth* | 200,000,000 |
| | |
| *Total* | 209,000,000 |

## Tax calculation (Mark)

Mark's main asset is the wealth he placed in the offshore structure originally established by his father. He is not taxed on the full amount but receives relief, related to the amount of tax paid by Dorothy and other beneficiaries of the family trust. The relief is designed so as to prevent double taxation of the same wealth.

| Calculation | |
|---|---|
| *Chargeable wealth* | 209,000,000 |
| *Personal allowance* | 10,000,000 |
| *Relevant chargeable wealth* | 199,000,000 |
| *Tax due at lower rate* | 500,000 |
| *Tax due at higher rate* | 18,900,000 |
| *Minus relief (to avoid double counting)* | -3,000,000 |
| ***Total tax due*** | 16,400,000 |

## Case study 3: Phoebe & Michael Owen

Phoebe is an extremely successful derivatives trader, receiving a high salary and bonuses for her employer, which is a financial institution. Phoebe's husband Michael is an entrepreneur, owning all of the shares in a fast-growing start-up company which he manages. He receives a modest salary from the company, and took a large dividend two years ago, but he is hoping to take most of his reward in the form of a capital gain when he sells out to an investor. They live in a house in Chelsea which they own jointly, subject to a joint mortgage. Phoebe also owns rental property in France. She is not a particularly careful investor, spending a large amount of her money on art, and holding a lot of cash. She also has a substantial amount of assets in a registered pension fund.

Both Phoebe and Michael are low risk taxpayers.

**Income (Phoebe)**

| | *Salary* | *Interest from cash* | *Rental income* |
|---|---|---|---|
| *2010* | 500,000 | 5,000 | 200,000 |
| *2011* | 500,000 | 5,000 | 200,000 |
| *2012* | 500,000 | 5,000 | 200,000 |
| *2013* | 500,000 | 10,000 | 200,000 |
| *2014* | 500,000 | 5,000 | 200,000 |
| *2015* | 500,000 | 5,000 | 200,000 |

Phoebe's salary and other income before the relevant four year period are disregarded.

### Assets (Phoebe)

| Asset | Value |
|---|---|
| Art collection | 3,000,000 |
| Pension fund | 1,250,000 |

Phoebe's art collection is excluded from the calculation of chargeable wealth. Her share of the property, which she holds jointly with Michael, is taken into account in the calculation of his wealth as his chargeable wealth is the higher of the two.

### Tax calculation (Phoebe)

As Phoebe's wealth is below the threshold of the personal allowance she pays no tax.

| Calculation | |
|---|---|
| **Deemed investment wealth** | |
| Top income in 4 years | 210,000 |
| Deemed investment wealth | 4,200,000 |
| **Deemed chargeable wealth** | |
| Deemed investment wealth | 4,200,000 |
| Private pension | 1,250,000 |
| | |
| **Total** | 5,450,000 |
| | |
| Personal allowance | 10,000,000 |
| | |
| Relevant Deemed Chargeable wealth | N/A |
| | |
| Tax due | ZERO |

### Income (Michael)

| | Salary | Dividend |
|---|---|---|
| 2010 | 50,000 | |
| 2011 | 50,000 | |
| 2012 | 50,000 | |
| 2013 | 50,000 | |
| 2014 | 50,000 | 4,000,000 |
| 2015 | 50,000 | |

**Assets (Michael)**

| *Asset* | *Value* |
|---:|---:|
| *Property* | 10,000,000 |
| *Mortgage* | - 2,500,000 |

**Tax calculation (Michael)**

Michael's income included a 'lumpy' payment of a £4m dividend in one year. Taking this as the highest income and imputing the deemed chargeable wealth from this one year's figure would have yielded a valuation of his company of £80m. Michael opts for a full valuation of the company's worth – which is subsequently valued at £7.75 million.

Jointly owned property is deemed to be included within the chargeable wealth of the person whose wealth is the greatest, and therefore the value of Phoebe and Michael's home, minus their mortgage is included in the calculation of Michael's chargeable wealth, not Phoebe's.

| ***Calculation*** | **£** |
|---:|---:|
| *Cash valued assets* | 7,750,000 |
| *Untenanted real property* | 10,000,000 |
| *minus liabilities* | -2,500,000 |
| ***Total*** | 15,250,000 |
| *Personal allowance* | 10,000,000 |
| *Relevant deemed chargeable wealth* | 5,250,000 |
| ***Tax due*** | 262,500 |

## Case study 4: Findlay Onyx

Findlay is a successful pop singer who earns millions of pounds a year in royalties. Aside from a much-publicised purchase of a luxury yacht worth tens of millions of pounds, he is a conscientious saver and invests most of his income in a portfolio of investment assets, which are by themselves a substantial additional source of income alongside his royalty income. He is from the US originally, and has only been living in the UK for two years. He has, however, set up home here with his British boyfriend. His income is not currently being paid to him in the UK, and since he is claiming the remittance basis of taxation, he pays a relatively small amount of UK income tax on the money that he brings into the UK.

Findlay is a long term resident because he intends to stay in the UK, and is a high risk taxpayer, because he pays tax on the remittance basis.

**Income**

| | *Royalty income* | *Investment income* |
|---|---|---|
| *2010* | 9,000,000 | 7,000,000 |
| *2011* | 9,000,000 | 7,000,000 |
| *2012* | 9,000,000 | 7,000,000 |
| *2013* | 9,000,000 | 7,000,000 |
| *2014* | 9,000,000 | 7,000,000 |
| *2015* | 9,000,000 | 7,000,000 |

As Findlay is a high risk taxpayer his wealth is not deemed from his income, but instead valued in full.

**Assets**

| ***Asset*** | ***Value*** |
|---|---|
| *Investment portfolio* | 140,000,000 |
| *Song rights* | 180,000,000 |
| *Luxury yacht* | 30,000,000 |
| *Property* | 17,000,000 |
| *Mortgage* | -12,000,000 |

**Tax calculation**

Findlay's song rights are an asset held for the purpose of a trade and are excluded from the calculation of the market value of relevant assets. (If someone else bought them, for example as Michael Jackson bought the rights to The Beatles' songs – then they would be an asset from which passive income could be derived, and would be included in that person's chargeable wealth.)

| ***Calculation*** | £ |
|---|---|
| *Chargeable wealth* | 175,000,000 |
| | |
| *Personal allowance* | 10,000,000 |
| | |
| *Relevant chargeable wealth* | 165,000,000 |
| | |
| *Tax due at lower rate* | 500,000 |
| *Tax due at higher rate* | 15,500,000 |
| | |
| ***Total tax due*** | 16,000,000 |