COMBINING INCOME AND WEALTH INTO A SINGLE INSTRUMENT: A REVIEW OF *TAXING INEQUALITY*

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Ari Glogower's *Taxing Inequality* is an ambitious, thought-provoking piece.[1] He makes three major arguments: (1) that the economic power theory justifies taxing wealth in addition to income, (2) that separate taxes on wealth and income are inferior to a combined tax that incorporates both into a single instrument, and (3) that the best way to accomplish this goal is to include in income an amount equal to an annuity-equivalent portion of the taxpayer's wealth. Although it departs from the structure of the article, I will address (2) before considering (1) and (3) together.

Glogower's second argument is quite compelling. He states, "proposals in the literature for separate taxes on both income and wealth do not account for the relationship between the two as factors in economic well-being."[2] Wealth and income are both relevant to well-being or ability-to-pay and meaningfully interact with each other. This is not an idle thought experiment. Existing tax systems already incorporate wealth and income (although not by adding a "wealth annuity" to labor income in the way Glogower envisions). For example, property taxes in some jurisdictions have so-called "circuit-breakers" which reduce a property tax bill if it exceeds a certain percentage of the taxpayer's income.[3] Indeed, the federal income tax indirectly incorporates wealth (again not by incorporating wealth in the tax base the way Glogower envisions) by taxing actual returns to capital.[4] There is a tight connection between income taxes on returns to capital and wealth taxes. Instead of attempting to measure and tax capital income, one alternative would be to assume that wealth earns a fixed return each year. For example, a 25% income tax on a presumed rate of return of 4% would be equivalent to a 1% wealth tax. The Netherlands

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1 Ari Glogower, *Taxing Inequality*, 93 N.Y.U. L. REV. 1421 (2018).

2 *Id.* at 1421–22.

3 *See generally* KAREN LYONS ET AL., CTR. ON BUDGET & POLICY PRIORITIES, THE PROPERTY TAX CIRCUIT BREAKER: AN INTRODUCTION AND SURVEY OF CURRENT PROGRAMS 2–8 (2007), https://www.cbpp.org/research/the-property-tax-circuit-breaker (describing the mechanics of circuit-breaker programs).

4 *See* I.R.C. § 61(a)(4), (5), (7) (2012) (defining gross income to include interests, rents, and dividends).

currently uses this approach to taxing capital income.[5]

Having established the premise that taxing wealth as well as income may be desirable, Glogower astutely notes that taxing both in a single instrument can provide greater flexibility than employing separate instruments. As he points out, the progressivity of the overall fiscal system can be undermined if wealth and income are taxed separately.[6] The advantage of a combined instrument must be balanced by the potential increase in administrative and efficiency costs. If we accept the premise that tax instruments should incorporate both income and wealth, the much more difficult question is how.

Glogower finds the current federal income tax treatment of wealth insufficient and believes that—because of differences between labor and capital income—a portion of wealth should be included in the combined tax base. He correctly observes that an important difference between income and wealth is that the former is a flow while the latter is a stock. His clever move is to convert wealth into a flow by calculating an annuity-equivalent amount and including it in the tax base. As Glogower writes, "In effect, the wealth annuity accounts for a taxpayer's capital income earned during the taxing period (as under the current income tax) and also a portion, but not all, of the taxpayer's wealth stock."[7] There is much to recommend in Glogower's annuity approach. By converting wealth into a flow, his approach makes wealth easier to compare to labor income. His approach is also sensitive to the taxpayer's age. One million dollars of wealth for a thirty-year-old is not the same as the same amount of wealth for an eighty-year-old.[8]

Although there is much to recommend Glogower's annuity-equivalent approach, there are many other possible methods for wealth and income to be combined into a single instrument. If we accept the premise that wealth should intermediate income in some way, it is not clear that using an annuity-equivalent approach is best. I find myself agnostic regarding the

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5 *See* Art. 5.2 WET INKOMSTENBELASTING [WET IB] [INCOME TAX LAW], https://wetten.overheid.nl/BWBR0011353/2018-01-01#Hoofdstuk5_Afdeling5.1_Artikel5.2; Sijbren Cnossen & Lans Bovenberg, *Fundamental Tax Reform in the Netherlands*, 7 INT'L TAX & PUB. FIN. 471, 471 (2001) ("Henceforth, the taxable return on personally held assets . . . is set at a presumptive percentage of 4% of the value of these assets net of liabilities, regardless of the actual returns.").

6 *See* Glogower, *supra* note 1, at 1460–64 (finding that "separately taxing different bases under a graduated rate schedule does not yield the same tax liability as a single progressive tax on an aggregate measure of both bases" and that this can lead to taxing those with greater ability to pay at the same rate as those with less ability, frustrating the progressive tax schedule's goal of taxing greater ability to pay at higher average rates).

7 *Id.* at 1432.

8 *See id.* at 1476–83 (describing how real-world considerations like the periodicity of labor income and life expectancy can change the impact of income and wealth on economic well-being at different stages of a taxpayer's life).

annuity approach and paralyzed by the sheer number of ways that wealth and income could potentially be combined into a single instrument. Is there some more desirable way to combine the two into a single base? Could a taxpayer's wealth instead continuously determine the tax rates that apply to taxpayer income?[9] The ways in which income and wealth could be combined into a single instrument are virtually infinite. The difficult task facing Glogower in defending his annuity approach is to start with a normative justification for taxing income and wealth and then connect it to his *particular* proposal to combine income and wealth into a single instrument.

Glogower focuses on the economic power justification for taxing wealth. Glogower states, "the relative economic power theory holds that excessively unequal distributions of economic resources and market power can result in unequal divisions of political and social power as well."[10] He goes on to say that "resources *only* reflect greater economic power to the extent that they are in fact credibly expendable in the current period."[11]

Unfortunately, the relative economic theory does not provide a clear prescription as to how wealth increases power. This is where I find Glogower's article to be a bit too conclusory. For example, in the context of one of his examples, Glogower states, "[m]ore critically, the combined base measures exactly how much more powerful [the taxpayer] is as a result of her greater income and wealth."[12] In other sections, he is a little more circumspect: "From the perspective of the relative economic power theory, the wealth annuity therefore yields a more accurate measure of economic spending power during the taxing period."[13]

However, if the point is to measure the resources a person can credibly expend in the current period, it is unclear why wealth should be converted into an annuity. Consider an alternative. In the current period, a person can credibly spend their entire wealth less an amount that will fuel a baseline level of consumption for the remainder of his or her expected life. For a wealthy taxpayer, this approach would add a much larger amount of wealth to a person's income tax base each year as compared to the annuity-equivalent approach. Without a clearer understanding of how dollars convert into relative economic power, it is hard to use the relative economic power theory to specify a combination of wealth and income.[14]

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[9] For example, one could imagine a surcharge on income based on wealth holdings.

[10] *Id.* at 1445.

[11] *Id.* at 1449 (emphasis in original).

[12] *Id.* at 1474.

[13] *Id.* at 1471.

[14] It also seems that the economic power theory should be concerned with the form of wealth. Liquid assets can much more credibly be expended than wealth held in businesses or a personal residence.

In conclusion, this piece is an important contribution to the tax literature and well worth reading. Glogower's article asks us to think more capaciously about how wealth could be incorporated into an income tax. He offers the annuity-equivalent amount as one possibility. I agree that it would be fruitful to think harder about how the fiscal system should tax income and wealth. Glogower's article and the emerging optimal tax literature on wealth[15] urge us to interrogate that combination more carefully.

15 *See, e.g.*, Stefania Albanesi & Christopher Sleet, *Dynamic Optimal Taxation with Private Information*, 73 REV. ECON. STUD. 1 (2006) (finding that when income and wealth are observable, optimal taxation requires joint instruments and not separate taxes on income and wealth); Narayana R. Kocherlakota, *Zero Expected Wealth Taxes: A Mirrlees Approach to Dynamic Optimal Taxation*, 73 ECONOMETRICA 1587 (2005) (finding that optimal wealth tax rates depend on (past and current) labor income).