

Daniel Waldenström¹ Inheritance and Wealth Taxation in Sweden

and wealth inequality, and then discusses what we know about the relationship between wealth taxation, wealth accumulation and offshore tax evasion. Finally, a concluding discussion summarises the issues covered and highlights questions for further inquiry.

THE RISE AND FALL OF SWEDEN'S INHERITANCE AND WEALTH TAXES⁴

Inheritance taxation has long-standing traditions in all Western economies. In the pre-industrial era, these taxes existed because probate inventories of deceased individuals offered a reliable and easily observable tax base.⁵ Later inheritance taxes were primarily motivated by redistribution, linked to the growth of government and emergence of the welfare state.

Sweden got its first “modern” inheritance and gift tax in 1885. Inheritances were taxed at a flat rate of 0.5% at this time, but the tax rate increased over the twentieth century to 5-10% in the interwar era, 5-20% in the 1930s and 1940s and 5-60% in the first postwar decades. Figure 1 shows average effective inheritance tax rates for different size classes of estates held in the form of a closely held corporation.

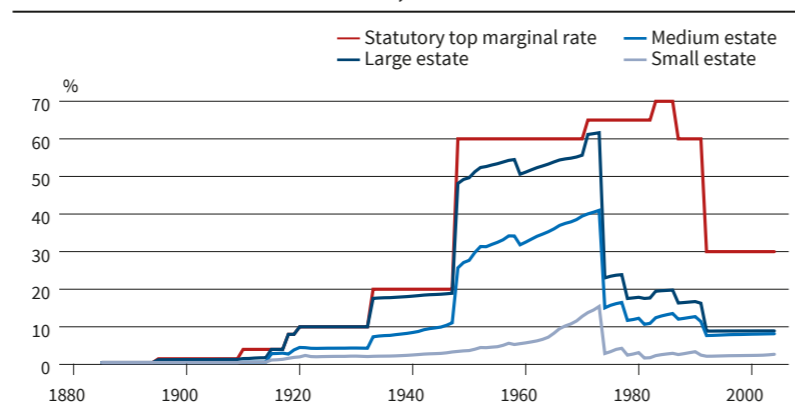
From the 1970s onwards, exemptions were introduced in the taxation of business equity in non-listed firms. Effective tax rates dropped as a result, especially on large inheritances, and a gap in tax rates vis-à-vis other assets (property, listed shares) emerged. This gap is shown in Figure 1 when comparing the effective tax rates with the statutory top tax rate.

In 2004, Sweden abolished the inheritance and gift tax. There are several potential forces that could explain this decision, according to an analysis by Henrekson

⁴ The historical descriptions of this section draw heavily on Du Rietz, Henrekson and Waldenström (2015), Henrekson and Waldenström (2017), and Du Rietz and Henrekson (2015).

⁵ Probate inventories were made early on because of the need to clear all debts of the deceased before any bequests could be transferred to heirs. For this reason, most European countries have probate archives going back a long time, sometimes to the seventeenth century or even earlier.

Figure 1
Effective Inheritance Tax Rates in Sweden, 1885–2004



Note: The graph shows the statutory top marginal inheritance tax rate and three average effective inheritance tax rates that a child with one sibling pays when inheriting half of a non-listed corporation worth 1,000 average annual worker salaries ('Large estate'), 100 worker salaries ('Medium estate') or 10 worker salaries ('Small estate'). The effective tax rates account for all relevant deductions and valuation rules. Source: Du Rietz et al. (2015). © ifo Institute

INTRODUCTION

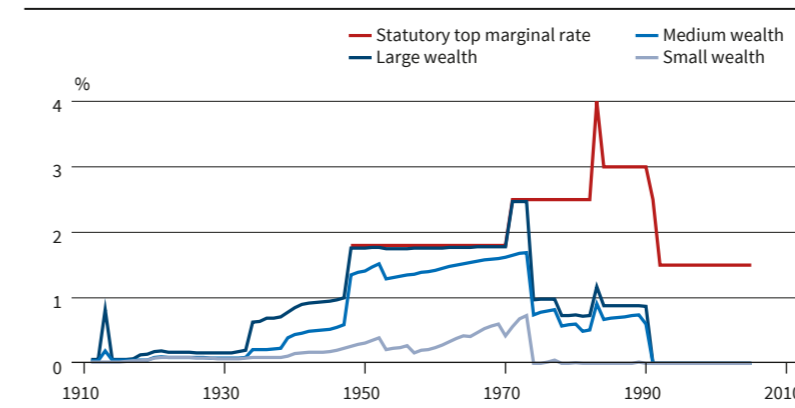
This article discusses the experiences of inheritance and wealth taxation in Sweden. It focuses on inheritance and wealth taxation for a number of reasons. The macroeconomic importance of wealth, not least inherited wealth, has increased in the Western world in recent years, as shown by growing national wealth to income ratios and increasing inheritance flows.² Inequality in incomes has trended upwards, and this increase has been linked to a capital income growth at the top of the income distribution. In addition, the theoretical body of literature on optimal tax has undergone profound changes and a new strand of papers now show that capital taxes can serve important functions in modern tax systems.³

Sweden is one of the world's most egalitarian welfare states with low levels of inequality and a high tax-to-GDP ratio. However, when it comes to the taxation of wealth and capital income, Sweden does not stand out internationally. For example, its capital tax revenues are at about 5% of GDP, which is in line with the average figure among rich countries. Capital incomes are taxed at a flat rate, without any concessions for holding time, but also with no increasing rates for higher income levels. In the mid-2000s, Sweden stopped taxing inheritances and gifts (in 2004) and household net wealth (in 2006). In other words, despite being a hallmark egalitarian welfare state, Sweden's taxes on wealth, capital income and inheritances are internationally low.

This article aims to offer a perspective on the Swedish taxation of inheritance and wealth. It begins with a description of the introduction and abolishment of these taxes, spanning over a century of historical and economic development. It subsequently examines the distributional consequences of inherited wealth, looking at both income

¹ daniel.waldenstrom@psemail.eu
² Trends in wealth-income ratios are documented by Piketty and Zucman (2014) and for Sweden by Waldenström (2016, 2017), and the evolution of inherited wealth is studied for France by Piketty (2011) and for Sweden by Ohlsson, Roine and Waldenström (2014).
³ See Bastani and Waldenström (2018) for an overview of the theoretical literature on optimal capital taxation.

Figure 2
Effective Wealth Tax Rates in Sweden, 1911–2004



Note: Average effective wealth tax rates are for owners of a non-listed corporation worth 1,000 average annual worker salaries ('Large wealth'), 100 worker salaries ('Medium wealth') or 10 worker salaries ('Small wealth'). The effective tax rates account for all relevant deductions and valuation rules. Source: Author's computations based on data from Du Rietz and Henrekson (2015). © ifo Institute

and Waldenström (2017). For example, the combination of a low basic deduction for bequests to become taxable and rising house prices during the 1990s meant that a large fraction of heirs, about one-third in 2000, was eligible to pay the tax. At the same time, new tax exemptions for business equity meant that most large bequests became effectively tax exempt, which thus meant that a growing number of taxpayers at the low end of the distribution had to pay the tax, while fewer and fewer at the top had to do so. In addition, there was general consensus that inheritance tax avoidance was widespread, which further undermined the conceived effectiveness of the tax.

Wealth taxation emerged in Sweden at the beginning of the twentieth century. After several decades of taxing a fraction of the wealth as part of the taxable income, Sweden got a separate wealth tax in 1948.⁶ The evolution of average effective wealth tax rates is shown in Figure 2 for different levels of household wealth. The figure shows that tax rates were low until the 1930s after which they were raised in several steps to reach their historical highs in the 1970s and 1980s of around a tenth of a percent. Concessions for corporate wealth taxation in the 1970s generated a gap between the taxation of closely held business equity wealth and other wealth. After 1950, the wealth tax was between 1% and 3% on large fortunes, and if one assumes a 3% real rate of

⁶ Naturally, the wealth tax is not the only tax on household wealth. The property tax affects the main non-financial assets of households whereas the capital income tax is a tax on cash returns on financial wealth (and actually almost exactly equivalent to a wealth tax on the stock of financial wealth). However, this analysis will only consider the specific net wealth tax.

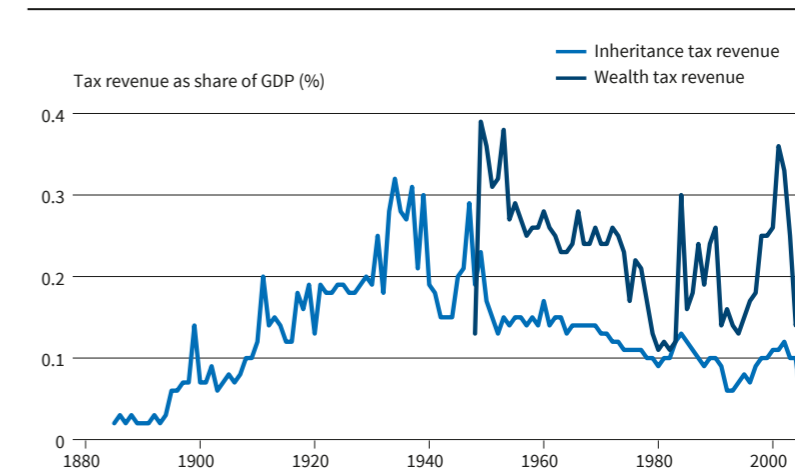
return on the wealth, this thus represents an equivalent of a tax on capital income between 33% and 100%. However, for lower levels of taxable wealth, the tax was markedly lower.

The abolishment of the wealth tax occurred in 2006, as one of the first decisions made by a new right-wing government. Several factors were behind this move. One recurrent criticism was that the special treatment of business equity had made the tax regressive, taxing middle-class wealth (mainly housing and some financial assets) while exempting the wealthiest individuals

who owned large, closely held firms (or dominant positions in listed companies). Another common criticism was that the wealth tax spurred tax avoidance and evasion, especially in the form of capital flight to offshore tax havens. It should be noted that even although the wealth tax was abolished, Sweden taxes both property and various forms of capital income, which means that wealth and its returns are still taxed in Sweden.

Figure 3 presents the evolution of revenues from the taxation of inheritances and gifts (and estates in 1948-1959) and of household net wealth. The inheritance tax revenues represented about 0.1% of GDP during the postwar period, whereas the wealth tax generated about double as much revenue. It is worth noting that the relative size of annual inheritance flows increased in the 1990s and 2000s, connected with a contemporaneous increase in the aggregate wealth to GDP ratio. The fact that tax revenues did not rise in the same manner could be an indication of aggravating problems with inheritance and wealth tax avoidance.

Figure 3
Revenues from Inheritances and Wealth Taxes in Sweden



Source: Du Rietz (2015) [inheritance tax] and Du Rietz and Henrekson (2015) [wealth tax]. © ifo Institute

INHERITED WEALTH AND INEQUALITY

The importance of inherited wealth to the overall economy is not negligible. Recent estimates for Sweden by Ohlsson, Roine and Waldenström (2014) suggest that a substantial share of private wealth, maybe 50%, is in fact inherited, while the rest has been accumulated by individuals over their life cycle. This fraction is relatively close to what is found for other developed economies.⁷ The annual flow of inheritances as share of national income has varied over time, but is approximately one-tenth today in Sweden after having been half of that just thirty years ago. In France, results in Piketty (2011) show that inheritance flows are also increasing, but their relative size is greater than in Sweden.

When it comes to the distributional consequences of inherited wealth, they are more difficult to estimate since that requires high-quality microdata on individuals linked across generations. Such data are available for Sweden, and some recent studies address the role of inheritances for different inequality outcomes. For example, Elinder, Erixson and Waldenström (2016) use inheritance tax registers for the 2000s to analyse how inheritances are distributed among heirs. Figure 4 shows one of their main findings, namely that average bequest amounts increase the level of labour income and net wealth of heirs. Heirs thus already tend to have a high economic ability and face beneficial economic circumstances. At the same time, inheritances also matter for poorer heirs, and relative to their pre-inheritance income and wealth, their importance is actually larger than for more wealthy heirs. In other words, while inheritances magnify the absolute economic differences among heirs, they reduce the relative differences between them.⁸

The influence of parental wealth on intergenerational income mobility is studied by Björklund, Roine and Waldenström (2012). Using a large sample of Swed-

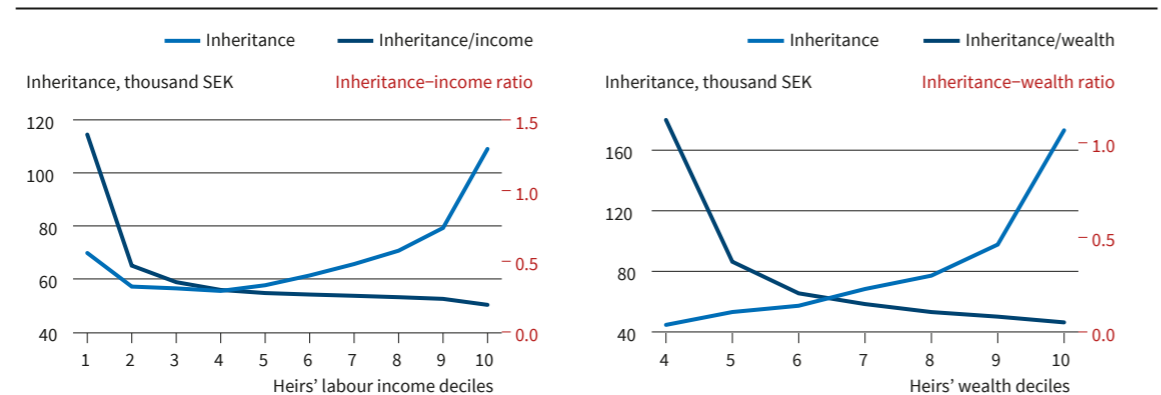
ish father-son pairs observed in the 1970s (fathers) and 2000s (sons), they examine the generational correlations for different levels of father income, and whether including capital income into the income measure matters. Figure 5 shows that adding capital incomes increases income transmission, but only among top-income fathers. Among the very top earners, sons' incomes are almost perfectly aligned with those of their fathers according to the estimated intergenerational elasticity of 0.9. Seeking explanations to this pattern, the authors reject the notion that education, non-cognitive or cognitive skills are important influences. By contrast, parental wealth accounts for a great deal of this variation: This, in turn, supports the idea that inherited wealth plays a key role in top income mobility.

A related question concerns the role of inheritances for the intergenerational mobility of wealth. Adermon, Lindahl and Waldenström (2018) examine another Swedish multigenerational dataset with observations of both wealth and inheritances. They use different methods to estimate the possible relationships, one based on subtracting the value of past bequests from children's wealth, and another based on included bequests as a mediating variable in intergenerational wealth regressions. All methods point in the same direction, namely that a considerable share of recorded wealth mobility - perhaps up to half - can be attributed to inheritance and gifts. Figure 6 shows the result from one of the approaches, namely the alignment between parental and child wealth when children's wealth either includes all inherited wealth or when it does not. There is a clear positive link between the total wealth of parents and their children, but most of it vanishes when the value of inheritances are taken out.

Taken together, these Swedish studies suggest that inherited wealth has clear effects on how important the family background is for a person's economic life chances. Bequests seem to increase generational correlations, especially at the top of the distribution, while mattering relatively more for less wealthy heirs.

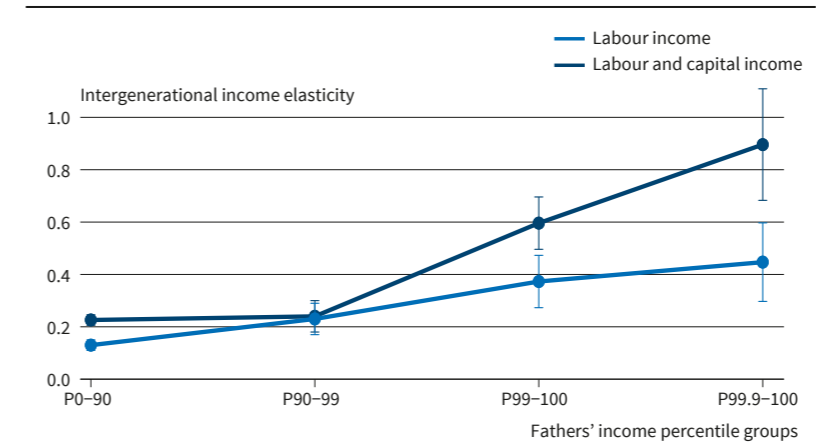
⁷ See Wolff (2015) and Piketty and Zucman (2015).
⁸ This result is not unique for Sweden; it has also been found for the US and Denmark, as discussed by Wolff (2015) and Boserup, Kreiner and Kopczuk (2016).

Figure 4
The Distributional Role of Inherited Wealth in Sweden



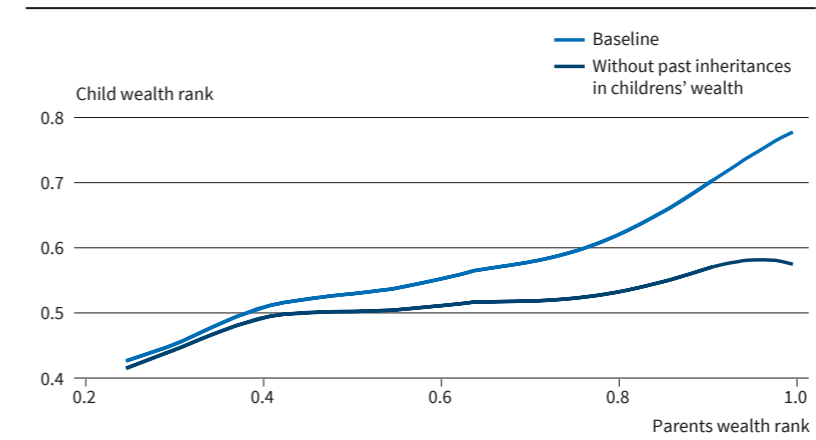
Note: Observations are averages in the years 2002–2004. Data come from the Swedish Tax Agency and the wealth register at Statistics Sweden. Source: Elinder, Erixson and Waldenström (2016). © ifo Institute

Figure 5
Intergenerational Income Mobility: The Role of Wealth



Note: Data consist of approximately hundreds of thousands of father-son relationships where income is measured in the 40's for both generations. Source: Björklund, Roine and Waldenström (2012). © ifo Institute

Figure 6
Parent-Child Wealth Correlation: The Role of Inheritances



Note: The figure shows smoothed line fits across wealth ranks of children and their parents in Sweden. Child wealth without past inheritances equals child wealth less the net present value of all past inheritances. Source: Adermon, Lindahl and Waldenström (2018). © ifo Institute

To the extent that inheritances affect the distribution, taxation will work to counteract these effects.

WEALTH TAXATION, ACCUMULATION AND OFFSHORE CAPITAL

Our knowledge of the role of the Swedish wealth taxes for wealth accumulation and wealth inequality is limited, largely due to a scarcity of detailed microdata on asset ownership. Two recent studies of Nordic wealth tax data attempt to study the effects of wealth taxation on efficiency and avoidance. Jakobsen et al. (2018) analyse wealth taxation in Denmark during the 1980s and 1990s using a relatively rich register database that allows them to examine several aspects of real and avoidance-related effects. They find that the wealth tax had negligible effects on the accumulation behaviour among most groups in society, but the effects were sizeable at the top of the distribution. Seim (2017) analyses a similar elasticity of taxable wealth in Sweden, also using administrative data but over a shorter time

period and with smaller asset coverage (especially concerning equity in closely held firms and funded pensions). The main finding is that wealth taxation in Sweden had relatively small effects on wealth accumulation, but notable effects on reporting and avoidance behaviour.

A recurrent question when it comes to the abolition of the Swedish wealth tax in 2006 is whether this had any impact on wealth inequality. Unfortunately, answering this question is obstructed by two circumstances, one being that most of individual wealth data ceased to be collected after the tax repeal, and another being the almost simultaneous occurrence of the financial crisis of 2008-2009. Lundberg and Waldenström (2018) use capital income tax data and property holdings from tax assessments to estimate Swedish wealth inequality before and after the repeal of the wealth tax. Their main finding is that wealth gaps increased towards the end of the 2000s. A possible explanation for this is that the tax repeal was capitalised in asset values, benefitting the relatively rich.⁹ Asset decomposition analyses also show that the poor seemed to empty their

bank holdings during the crisis, which widened gaps in financial assets.

Tax-driven capital flight to offshore tax havens has been another, lively debated, aspect of Sweden's wealth taxation. The discussion has concerned both its order of magnitude and the distributional profile of the hidden offshore wealth. Recent scholarly efforts have shed some light on both of these questions, but it is fair to say that a lot of uncertainty remains. Roine and Waldenström (2009) used two complementary macro-statistical models, one based on calculating the gap in financial savings between national and financial accounts and the other based on accumulated net errors and omission in the balance of payments. These sources are uncertain by construction, and they have also been shown to be sensitive to adjustments in the computation of the national accounts and the financial

⁹ For an individual with a taxable wealth of 10 million SEK, the wealth tax in 2006 was 127,000 SEK. Assuming a lifetime real return of 3%, the net present value of all future wealth-tax payments is 4.25 million SEK (127,000/3%), which thus would imply a mechanical tax-reform effect of an increase by 40% for previously taxed fortunes.

accounts. Their estimate for 2016 is that Swedes hold an equivalent of 130 billion euros in offshore tax havens, which represents about 10% of total domestic financial assets. A study by Alstadsæter, Johannesen and Zucman (2017) makes similar estimates for Sweden, but uses differences in national balance sheets across countries to back out hidden wealth. Their estimate for 2007 is a level of 3% of households' financial assets, which lies in between the other flow-based estimates.

As for the distributional effects of the offshore wealth, Roine and Waldenström (2008) estimated the impact on the income distribution by adding an assumed return from the offshore wealth to the disclosed domestic incomes of the top income percentile. The result was a 25% increase in the top percentile income share. Roine and Waldenström (2009) performed a similar exercise, but for the wealth distribution and found that the top wealth percentile share increased by between 25% and 50%. A more recent estimate was made by Alstadsæter et al. (2017) using information on named tax evaders who were linked to administrative wealth registers in Sweden. This showed that the majority of these individuals did indeed belong to the top wealth groups in Sweden; about 80% of them were in the top 0.01 percentile. While showing the distributional impact of the wealth tax, this also suggests that it had a substantial impact on avoidance behaviour among taxpayers who belong to the top wealth groups in society.

CONCLUDING REMARKS

This chapter discusses the Swedish experiences with taxing inheritance and wealth. It focuses on describing the main features of these taxes and their development over time, as well as their implications for economic efficiency and equity. Although these taxes have not constituted large shares of total tax revenues, their levels of effective tax rates have been quite high in certain periods, which had a notable impact on certain groups in society. This article also discusses the role of inheritances on economic inequality, and finds substantial effects especially on income and wealth mobility across generations. However, in the cross-section, inheritances both magnify the absolute dispersion in the population and reduce the relative differences between top and bottom.

The future of inheritance and wealth taxation in developed economies looks uncertain. In recent years, most countries have dismantled their wealth taxes, and although most countries still tax inheritances, their number is steadily decreasing. Recent theoretical and empirical studies point to a distinctive role of inheritance taxation in an optimal tax system with relatively small distortions, while promoting equality of opportunity. Understanding the role of these taxes may therefore not only require insights into their economic desirability, but also into the determinants of their political feasibility. Thus gaining a deeper understanding of the

political forces behind capital taxation is a topic worthy of future research.

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