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DECEM: FINANCIAL ALTERNATIVES FOR DEVELOPMENT AID (7)

*The tax on luxury*²

Luxury has existed for ages. Luxury allows for differentiation, grants status, and deserves the pride of its owner, in expense of what others think, in expense of others' admiration or scorn, others who will see luxury as an object of desire or an unnecessary complement in a society where there are alternatives valued at their fair price.

An economically unequal society that spans a variety of purchasing powers allowing for the existence of a market economy in which product specialization, added value, and customer service overlap to offer the consumer a product tailored to his needs and income

The welfare state requires taxation to cope with public spending that confers universal access to education and healthcare, that homogenizes a society with different levels of skills and therefore compensation, and enables to hedge against an individual's risk of disgrace, an individual that feels reassured in a solidary system based upon redistribution. A redistribution once upon a time bound to the borders of the nation-state, that has matured towards an intercontinental model in the postwar Marshall plan, or intracontinental in the European Union of today. A redistribution which dynamics must face the challenges of globalisation and convert into a global model.

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² This is the seventh article of the decem series, a series of ten articles fundamentally innovative that aim at the proposal of alternative financial mechanisms to considerably raise the amount of funds available for development in the third world. Throughout the series, the author will stress the implementation aspects of the suggested ideas and will propose arguments for and against.

The basis of the concept of redistribution is, as a result, taxation, taxation on wealth and income, taxation on purchased products and services through a tax widely known as value added tax.

PROGRESSIVE TAXATION

Progressive taxation is feasible nowadays not only on an income basis, but also on the purchase and sale of products and services. In today's world value added tax does not exist in a number of countries and states, whereas in others it adopts a simplified version with different levels of taxation as a function of the necessity of the product or service. As a result, for basic products and services taxation will be lower than for those considered accessory³.

A higher taxation should apply to products which demand does not significantly change as their level of taxation increases. These products are known as products of inelastic demand⁴. Economists say products and services, which demand does not significantly change with an increase in their price, should be taxed. As a result, if a luxury good is inelastic, then it should be tax considerably, because a tax that increases its price will not impact its demand.



Economists Arthur Pigou (1877-1959) and Frank Ramsey (1903-1930)

In a sustainable society that penalizes excess, there exists a duality between who should and who can compensate for the collateral damage. On one hand we can suggest a payment as a function of the responsibility, according to which those individuals causing a more severe collateral damage should be responsible for the associated cost⁵. On the other hand we can suggest a payment as a function of the payment capacity, according to which those individuals of higher income should undertake the associated cost⁶. This is

³ Which can be considered a decaff version of a tax on luxury.

⁴ According to Ramsey (1927).

⁵ Consistent with Pigou's economic theory (1920).

⁶ As it happens with the income tax.

the case of the *French contribution to international solidarity*, a contribution that taxes longhaul airplane tickets, an optimal taxation that should incorporate higher taxes in products that are preferably purchased by wealthier individuals⁷.

A SUSTAINABLE SOCIETY

The society of the twenty-first century must be based on sustainability, leaving unnecessary consumption behind and penalizing excess. In a market society, excess has to coexist with other healthier consumption habits, but has to be penalized in order to compensate the collateral damage caused by a badly managed and allocated consumption. A collateral damage defined as the consequence of not allocating consumption more equally among those who waste and those who lack the most basic, when those who lack the most basic do not have the opportunity to move forward and are born to live in eternal poverty.

A sustainable society based upon consumption has to be driven by the principles of global justice and equity, that guarantee the strict fulfillment of a *global order of priorities*. In a global society we are all part of a big family known as human kind. A big family in which a member should not, by principles if there were any, devour its prey, whereas simultaneously another member starves under extreme pain and lack of food and hope. Parents would never allow such an extreme imbalance. Our political class, our economic class, are the leaders of society and, as such, have the responsibility of legislating and ruling for global justice. The members of that big family have to demand responsible leaders, leaders with no favorable treat towards one or another family member, able to establish global operating rules capable of assuring a transition towards a global society based upon justice and equity.

Luxury is oftentimes unnecessary and counter-productive, leading to an over expense, and to an unequal allocation of consumption that deserves a profound reflection in the first world. Sometimes conceived as necessary, luxury should be taxed appropriately with a progressive tax on sales that taxes more heavily those goods and services likely to be purchased by the better off, not forgetting the framework that leads to this conclusion: a world of extreme inequality hungry for a significant increase in the accumulation of funds devoted to development aid in the third world.

BRIEF HISTORY OF THE TAXATION ON LUXURY GOODS

Like other taxation approaches that fluctuate with time and which popularity varies cyclically, taxation on luxury goods already existed as a way to raise public funds and has undergone an evolution throughout the last three centuries.

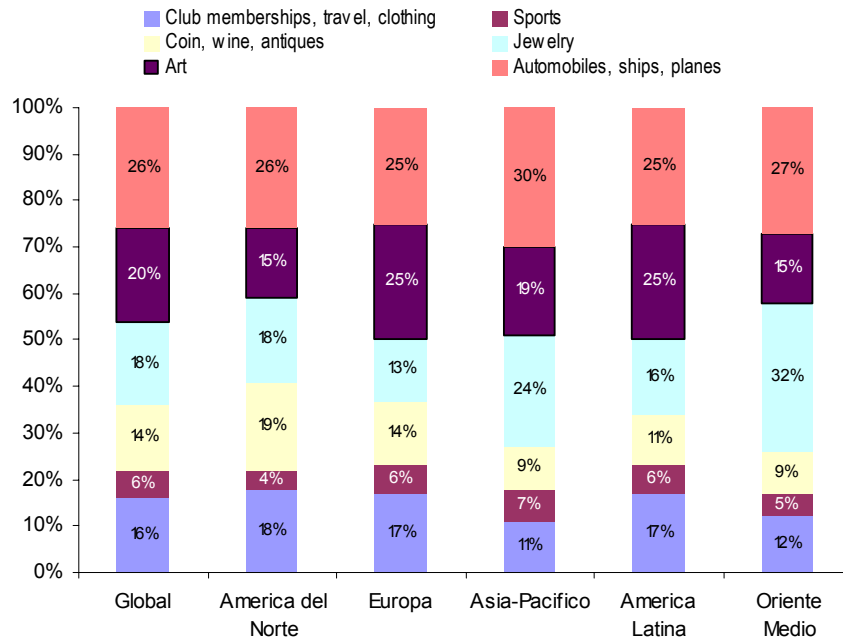
At the end of the eighteenth century a number of European nations sought a taxation on goods which demand was inelastic to price, particularly basic goods widely consumed for

⁷ A recent analysis conducted by Gillen, Morrison and Stewart (2002), who collected 254 statistical data on demand in 21 studies, justifies the argument that the demand for longhaul business trips is highly inelastic, whereas the demand for short distance leisure trips is very price-sensitive.

which there was no substitute. According a recent study⁸, during the period spanning the years 1788 and 1792, taxation on inelastic goods in England represented 45% of all public funds, while taxation on elastic goods with respect to income represented 19% of public funds. The same study points out that the definition of what was considered luxury and what was considered necessity was not based upon real research of what the population consumed, but rather upon normative assumptions. Typically the acquisition of imported goods was considered superfluous, a *voluntary* consumption.

Adam Smith and other economists of his time suggested that the right form of taxation consisted in taxing luxury in lieu of more basic goods. Originally taxation on luxury was utilized with the sole objective of manipulating consumption on luxury imports, such as textiles, in order to foster the consumption of substitute products manufactured locally.

Luxury Expenses of the Wealthy



Source : World Wealth Report 2007, Capgemini and Merrill Lynch

A recent report⁹ points out that the wealthy typically consume luxury products and services to a greater extent than goods in other categories such as jewelry or art¹⁰. A dynamics, that of acquiring luxury goods, that is increasing worldwide, which confirms the intuition that taxation on luxury is feasible and necessary. In this line of reasoning the above figure shows an expense distribution of personal wealth in excess of one million dollars, allocated by region.

⁸ *The Political Economy of British Taxation, 1660-1815*, Maxine Berg, Economic History Review.

⁹ *World Wealth Report 2007*, Capgemini and Merrill Lynch.

¹⁰ Art in particular would escape this kind of taxation, since art is oftentimes understood as an investment not very strongly correlated with the economic cycles of other asset classes, such as equities, fixed income and real estate. Art is not an expense related to the consumption of luxury.

A CONCEPT OF GLOBAL JUSTICE

The West has been able to establish a definition of welfare that guarantees universal access to basic services defined as rights in the universal declaration of human rights, a definition of welfare that incorporates the concept of minimum income, underneath of which the human dignity no longer holds. This minimum income is translated in a majority of countries¹¹ into a definition of minimum wage and maximum number of working hours that allow to earn sufficient income to fulfill a person's basic needs.

It is time to extrapolate the concept of welfare to a level beyond that considers the welfare of all and each of the citizens of the planet. The extremes that we live today are opposing poles with no attraction. The extremes we live are shameful, weak and can be avoided, in a society that is proud to be solidary and incapable of facing the do-nothing policy of a political and economic class anchored in ideas of the past, a political and economic class that has not shown to be prepared for the challenges at the beginning of the twenty-first century.

The world is a same place. In a same place there should not coexist the capricious and unnecessary expense with the extreme lack leading to the acute suffering and the premature death. We have to bring the suffering of the poor world to the first world, so that the consumer is aware of the necessity of taxing luxury. We are unable to accept that there exists extreme suffering because we are incapable of bearing it, because we would die in life and would live dying, were we aware that we could save a life, and however we did not.

An involuntary genocide that demonstrates our inability to react. An involuntary genocide penalized in the West, which mention scandalizes the welfare society, that does not assume responsibilities, that gives excuses on a footnote and justifies its lack of resources based upon the principles of economic theory, based upon financial architectures with no ethics. We cannot continue a dynamics leading to the destruction based upon the principle of ignorance, a weak virtue, an inconsistent kindness.

A TAX PENALIZING EXCESS

The maintenance of a welfare state requires the accumulation of economic resources from the taxation of wealth, income and purchase and sale of goods and services, applying the principle of redistribution through a taxation regime known as progressive.

The attainment of a society driven by the principles of global justice and equity implies the penalty of excess, in a market economy that operates in a democratic regime that by definition must consider an individual's freedom of consumption as a function of his purchasing power.

It is not obvious to determine what is and what is not a luxury good or service. Nor is it clear whether an additional taxation on a luxury good or service will diminish its demand. It is necessary to reach a consensus as to what goods or services are considered luxury, to

¹¹ There exists in Ireland a type of basic income that is granted to homeless or jobless individuals.

then establish a subset which demand does not decrease significantly with additional taxation. From a point of view of efficiency, it is logic to tax more heavily goods that do not experience big drops in demand when the price increases, so that tax collection increases and consumption does not suffer.

Excess is harmful for society as a whole. Excess does not only manifest in aspects such as pollution or abuse of power. The wealthy have the opportunity and the duty of investing and spending their money ethically. The wealthy should set the standard and become the reference to follow, for a bad spending of money is irresponsible, for a bad administration of money is not admissible in a global society that needs socially responsible investors, that needs consumers that spend efficiently. The penalty of excess is as a result necessary and leads to the gradual increase of development aid in the poor world.

A tax on luxury is not only a way to apply the principle of redistribution between rich and poor countries. It is also a way to redistribute between the rich and the poor within each developing country, a concept of local redistribution that perhaps today does not hold in developing countries with the rigor of the industrialized nations, developing countries with an almost non-existent middle class.

Mi casa es su casa. My world is your world. My actions, my attitudes, are no longer independent from the rest of the surrounding world. They are part of a global mechanism that must turn sustainable.