

The Rise and Fall of Swedish Wealth Taxation*



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Abstract: We study the evolution of modern Swedish wealth taxation from its introduction in 1911 until it was abolished in 2007. The rules concerning valuation of assets, deductions/exemptions and tax schedules to characterize effective wealth tax schedules are described. These rules and schedules are used to calculate marginal and average wealth tax rates for three differently endowed owners of family firms and individual fortunes corresponding to a large, medium-sized and small firm. The overall trend in the direct wealth tax was rising until 1971 for owners of large and medium-sized firms and for individuals of equally-sized wealth consisting of non-corporate assets. Average direct wealth tax rates were low until 1934, except for 1913 when a progressive defense tax was levied. There were three major tax hikes: in 1934, when the wealth tax was more than doubled, in 1948 when tax rates were doubled again and in 1971 for owners of large firms and similarly sized non-corporate fortunes. Effective tax rates peaked in 1973 for owners of large firms and in 1983 for individuals with large non-corporate wealth. Reduction rules limited the wealth tax rates from 1934 for fortunes with high wealth/income ratios. The wealth tax on unlisted net business equity was abolished in 1991. Tax rates for wealthy individuals were decreased in 1991 and in 1992 and then remained at 0.5-1 percent through 2006, depending on whether the reduction rule was applicable. Tax rates for small-firm owners and small individual fortunes were substantially lower. Aggregate wealth tax revenues were rela-

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tively small; they never exceeded 0.4 percent of GDP in the postwar period and amounted to 0.16 percent of GDP in 2006.

Keywords: Wealth tax; Tax avoidance; Entrepreneurship.

1. Introduction

Modern wealth taxation was introduced in Sweden in 1911 by the *1910 Ordinance of Income and Wealth Taxation*, SFS 1910:115. A primary goal of the ordinance was to take advantage of the greater ability to pay tax that possession of wealth gave the taxpayer (SOU 1969:54, p. 78). A second motive was to compensate for the erosion of other tax bases and growing government financing needs. Likewise, several types of wealth taxes were introduced during and between the world wars in order to fund the military. From the early 1930s the wealth tax was also motivated as a means of redistribution (SOU 1969:54, p. 8-9).

The purpose of this article is to provide an analysis of the evolution of Swedish wealth taxation from 1911 until 2007 when it was abolished.¹ We calculate long-term series of average wealth tax rates for each year during the full period under study. We cover different representative levels of wealth as well as account for institutional factors affecting tax rates such as deductions, exemptions and valuation rules. The tax rates paid for nearly a century are presented both for owners of individual fortunes and for owners of family firms of three different sizes.

In order to avoid any misunderstandings it is appropriate to state what this paper does *not* do. We do not assess any behavioral effects of wealth taxation. We merely calculate wealth tax rates for three hypothetical entrepreneurs and holders of equally-sized non-corporate wealth over time. Nor do we assess any effect the wealth tax may have had on wealth mobility, or on the propensity to become (or stop being) an entrepreneur.² Instead it is our hope that the present study

1. In fact, the wealth tax was abolished in 1994 by the then non-socialist government. The abolishment was to come into effect January 1, 1995, but the repeal was annulled by the newly elected Social-Democratic government in the late fall of 1994.
2. For a discussion of wealth mobility in Sweden, the reader is referred to Hochguertel and Ohlsson (2012) and Björklund, Roine and Waldenström (2012). Nykvist (2008) estimates the effect of personal wealth on the propensity to become self-employed. Du Rietz, Henrekson and Waldenström (2012) offer an equally exhaustive characterization of Swedish gift and inheritance taxation. For a seminal study of behavioral effects of inheritance taxation in Sweden, the reader is referred to Ohlsson (2012).

can provide the platform for studies of the effect of wealth taxation on behavior.

The paper is organized as follows. In section 2 we present the rules governing the valuation of assets and liabilities, and in the third section we present the different wealth tax schedules from 1911-2006. Only some key tables are presented in the paper. For an exhaustive description of all applicable tax rates (presented in 33 tables), the reader is referred to Du Rietz and Henrekson (2014). In section 4 we examine the impact of the wealth tax by computing average wealth tax rates – including the income wealth tax when applicable – for synthetically constructed family firms and individuals. Most of the focus is on computing the average tax rate on owners of family firms of three different sizes. In Section 5 we discuss why the wealth tax was abolished. Section 6 consists of a brief summary and our main conclusions.

2. Valuation rules

2.1. General principles

The Swedish wealth tax applied exclusively to households and the amount due was based on net wealth. The net wealth of dependent children living with their parents was included in household wealth.³ The capital values of insurance and pension rights were excluded from the tax base. For certain types of assets, special valuation rules applied. Real estate was valued at the tax-assessed value (*taxeringsvärdet*), which was supposed to be roughly 75 percent of the market value. The value of co-operative building society apartments was set to the member's share of the society's wealth. Periodic payments were valued according to capitalized values determined by the tax authority. Personal property (*lösöre*) was to correspond to the market value, and a business was valued as its market value, estimated by trustees. Some asset categories were listed at a fraction of their market value. For example, stocks registered on a stock exchange were (in some periods) listed at less than their full market value.⁴ From 1978 unlisted shares (on the so-called O-list, an informal listing) and other OTC-shares were assessed at only 30 percent of their quoted or book value. Forest holdings (*skogskonto*) were taxed based on half their market value. The inventories of small firms and stock-in-trade were at times also valued below market value.

3. Children were defined as dependent if they were below the age of 21 until 1968, below 20 from 1969 until 1973, and below 18 from 1974.
4. At 80 percent from 1997 until 2006; at 75 percent from 1978 through 1996; and at 100 percent prior to 1978.

The principal valuation rule for the wealth tax was that companies should be valued at expected sales value, for example at the quoted share value (market cap) on a stock exchange. For stocks in closely held (private) firms without dividends the value of equity was set to the difference between assets and liabilities at book value. For other Swedish stocks, values were often based on the capitalized value of dividends, the so-called earnings value (SOU 1969:54, p. 54).

2.2. Total tax caps

Reduction rules were introduced to mitigate the effect of the wealth tax for individuals with low current income in relation to wealth. The first reduction rule was introduced in 1934, jointly with the 1934 separate wealth tax. If taxable wealth exceeded 25 times taxable income from labor and capital, taxable wealth was lowered to that limit. The reduction rule was important for many wealthy persons because it often reduced their taxable wealth and thus their wealth tax significantly. To prevent the tax caps from becoming overly generous, a minimum tax floor was introduced, stipulating that the wealth tax could never be reduced below the tax due on half of taxable wealth.⁵ This minimum tax floor was temporarily lowered to 40 percent in 1938-1939. During WWII and just afterwards, from 1940 through 1947, no reduction rule applied (SOU 1969:54, p. 79-81).

In connection with the 1947 state income tax reform, the maximum taxable wealth in the earlier wealth reduction rule was changed to 30 times taxable income. Also, a new provisional *total* tax cap rule was introduced. This rule, effective from 1948, limited the sum of local and state income taxes and wealth tax for individuals to at most 80 percent of income subject to state income tax.⁶ However, this total tax limit was restricted in that the tax reduction could not exceed the amount of the state income tax (SOU 1969:54, p. 82-83).

From 1971 and onwards, there was an average total tax cap, inclusive of wealth tax. The cap amounted to 80 percent of state taxable income below SEK 200,000, and 85 percent on exceeding income (SOU 1977:91, p. 231-233). The main objective of the 80/85 percent rule was the same as for the earlier reduction rules, to ease taxation on low-yield assets. Beginning in 1984 the average total tax cap was lowered to 75/80 percent. After the 1990/91 tax reform there was also a cap

5. For example, if a taxpayer's wealth was SEK 4 million, but (s)he had no current income; taxable wealth was reduced to SEK 2 million. If a taxpayer's current income was SEK 100,000, taxable wealth was reduced to SEK 100,000 \times 25 = SEK 2.5 million.

6. A similar tax cap also applied from 1941 until 1944 and then again in 1947, but this cap only limited the state income tax (SOU 1969:54, p. 82).

limiting total tax payments, including wealth tax, to 55 percent of taxable income (labor plus capital income). This cap was raised to 60 percent in 1995 and remained at that level until the repeal of the wealth tax (SOU 2002:47, p. 441).

Most importantly, throughout the entire 1948-2006 period, the wealth tax could not be reduced below the amount due on 50 percent of taxable wealth (SOU 1969:54, p. 83). This rule provided a well-defined floor for wealth tax payments.

To consider the effect of the reduction rules in a tractable manner we make the following two, in our view reasonable, assumptions: (i) the reduction rules only applied to owners of medium-sized and large firms and equally wealthy individuals; and (ii) when the reduction rules applied, the individuals in question paid the minimum wealth tax, i.e., the tax on half their taxable wealth. The reduction rules could significantly lower the wealth tax due, but not necessarily sufficiently to avoid having a total tax load exceeding 80 percent of total taxable income (85 percent after 1971 for high-income earners; less after 1984, see above). For the owners of the large and medium-sized firm and persons with comparable non-corporate wealth, we will calculate total wealth tax in both sets of circumstances, i.e., when no reduction rule applied and when the tax floor was binding. That combination gives for each year a well-defined interval for the actual payment of wealth tax for a particular individual at that wealth level.

2.3. Valuation reliefs for net business equity of unlisted firms

Throughout the 20th century the corporate tax code granted relief in the valuation of business capital in the form of favorable rules for valuation of machinery, inventories and stocks-in-trade (Du Rietz, Johansson and Stenkula 2014, p. 12). However, in the wealth tax code such relief was not introduced for small closely held (private) companies until 1971 (SOU 1971:46, p. 127). The owner obtained a 25 percent reduction on the part of net corporate assets exceeding SEK 500,000, but for corporate assets below this level there was no reduction. Eligibility for such valuation relief was well-defined: At least 75 percent of the firm had to be owned by the entrepreneur alone or together with a maximum of eight other persons and total net assets had to be below SEK 2 million (SOU 1971:46, p. 128-134).

In 1974, the 1971-1973 tax relief was modified and extended by an option allowing stocks-in-trade and inventories to be undervalued. The new valuation rules stipulated that the lower value of either acquisition cost or replacement value were to be used as a basis for taxation. An additional 5 percent was then deducted for obsolescence, and finally the remainder was written down by a further 60 percent (Englund 1975, p. 62). In the tax rate computations below we have inter-

preted the deliberate underestimation of stocks-in-trade and inventories from 1974 until 1977 to have resulted in an assessment at 40 percent of net business equity.

In 1978, the valuation relief for unlisted businesses became more generous. Unlisted firms were valued at 30 percent of booked net equity value. This valuation rule was in force until the wealth tax for unlisted corporate equity was repealed in 1991.

3. Tax schedules

To understand how the wealth tax normally worked in practice, one must consider the structure of marginal and average tax rates, tax brackets, the scope for deductions, the valuation rules for assets and the rules for reductions of the wealth tax. The reader who wants the full details is referred to Du Rietz and Henrekson (2014), which contains 33 tables covering all tax rates, brackets and other rules during the 1911-2006 period.

3.1. The combined income and wealth tax: 1911-1919

In 1910 the combined income and wealth tax was introduced, and was in effect from 1911 through 1919. The marginal tax rates in the combined income and wealth tax in the 1911-1919 period varied between 1.7 and 6 percent (Table 1). Part of a taxpayer's net wealth was added on top of global (labor plus capital) income. The share of wealth that was added to the income tax base varied over time. It was 1/60th from 1911 through 1938 and 1 percent from 1939 through 1947, but had once been temporarily as high as 10 percent due to the 1913 defense tax. For high-income earners the wealth tax at times was so large that the income-taxed imputed income from wealth covered several tax brackets. In those cases the amounts in each bracket were determined at different marginal tax rates. This was particularly true following the 1913 defense tax.

State taxable income, SEK	Tax SEK	Average tax rate, %	Marginal tax rate, %
0	0	0	0
800	3.2	0.4	3.2
900	5.4	0.6	2.2
1,100	8.8	0.8	1.7
1,400	14	1.0	2.13
1,700	20.4	1.2	2.53
2,000	28	1.4	2.4
2,500	40	1.6	2.8
3,000	54	1.8	3.0
3,600	72	2.0	3.0
4,500	99	2.2	2.4
6,000	132	2.2	3.0
8,000	195	2.4	3.5
12,000	335	2.8	4.0
20,000	655	3.3	4.5
30,000	1,105	3.7	5.0
50,000	2,105	4.2	5.5
80,000	3,755	4.7	6.0
104,500	5,225	5.0	5.0

Table 1. The combined state income and wealth tax, 1911-1919

Source: Genberg (1942, p. 21-22) and SFS 1910:115 and our own calculations; see Du Rietz, Johansson and Stenkula (2013).

Note: Between 1911 and 1919, 1/60th of the tax payer's wealth was added to state taxable income. For income above SEK 104,500, the marginal income tax rate is lower due to an average tax cap. The appropriation and defense taxes are not included in the figures. For income below SEK 6,000, only average tax rates are reported in SFS 1910:115. As the average tax rates increase with income, the marginal tax rates are higher than the average tax rates up to the tax cap.

The income wealth tax was levied from 1911 to 1948. The marginal tax rates were increased several times (especially in 1920 and 1939). As a result of WWI, several additional temporary taxes were introduced to finance military expenditures. These taxes were constructed in a way similar to the regular income and wealth tax, i.e., part of the net

wealth was included in the income tax base and thus increased the effective income tax. The temporary war taxes affected only individuals with high income or large wealth, but the tax schedules were highly progressive with the result that those affected were often hit hard.⁷ These temporary surtaxes, particularly the business cycle tax (*krigskonjunkturskatten*; literally “the war boom tax”), were also in part motivated by the recognition that many firms made extraordinarily large profits of a windfall character during the war.

The first of these surtaxes was the temporary 1913 progressive defense tax which was due in 1914, but calculated on the basis of 1913 income. The defense tax was levied on individuals with an income of at least SEK 5,000 or with taxable wealth exceeding SEK 30,000. Ten percent of personal wealth was added to taxable income (compared to 1/60th in the ordinary income and wealth taxation (Söderberg 1996, p. 11; SOU 1969:54, p. 77-79). The marginal tax rate was 2.5 percent for an income of SEK 5,000 and the top tax rate was 13.5 percent, which applied to income exceeding SEK 225,000 (SEK 10.5 million in 2013).

Furthermore, and in a similar vein, an extra income and wealth tax was levied in 1918 and 1919, as well as a supplementary tax on incomes above SEK 100,000 in 1918. This amount corresponded to 49 average annual wages for a full-time production worker, henceforth APW (SEK 2,054 in 1918). These surtaxes were similar to the 1913 defense tax in being designed to apply exclusively to very large incomes and fortunes (Söderberg 1996, p. 11). The 1918 supplementary tax had several upper bracket thresholds.

3.2. The combined state income and wealth tax: 1920-1938

The 1919 combined state income and wealth tax was implemented in 1920. It replaced the 1910 income and wealth tax along with earlier temporary defense taxes, and was in effect through 1938 (Du Rietz, Johansson and Stenkula 2013). The state income tax schedules were revised and made flexible. The structure of the new state tax system – tax brackets, base amounts and marginal tax rates – was fixed, but the effective total tax rates were flexible. Politicians would henceforth annually determine the withdrawal percentage of the tax (*uttagningsprocenten*), thus allowing for easy upward and downward adjustments in the state income and wealth tax rates.

The system was progressive, with base marginal income tax rates running from 3 to 15 percent. To calculate the total tax rates, the base tax rates were multiplied by the withdrawal percentage for the year in question. There was a tax cap, which restricted the average tax to

7. Söderberg (1996, p. 11) and SOU 1969:54, p. 77-79.

about 12 percent of taxable income. The lowest tax bracket was very wide (the threshold for the upper limit was more than three times the 1920 APW) and thus included the vast majority of taxpayers.⁸ As a result, even though the new income tax schedule comprised 13 different tax brackets with rising marginal income tax rates, the tax schedule was proportional for low- and middle-income earners.

Several new additional temporary state income taxes were introduced alongside the 1920 ordinary state income and wealth tax. Wealth taxation was thus raised by the 1920 local progressive income tax (1920 års kommunala progressivskatt), which had the same base as the ordinary income and wealth tax (SOU 1969:54, p. 78). The marginal tax rates varied from 0.5 to 8 percent. The 1920 local progressive income tax was replaced by the 1928 local progressive income tax. The organization of the local tax system was changed, so that 1/4th of the 1920 local tax was transformed into a separate state income tax called the state equalization tax (*statliga utjämningskatten*). Revenues from this new state tax were used to compensate municipalities having weak tax bases or high expenditures. The tax was slightly progressive, but the tax rates were modest (the top marginal tax rate was 1.5 percent). This changed when it was doubled in 1934.

The depression in the early 1930s led to shrinking tax bases and the need to finance increased public expenditures. This was partly compensated for in 1932 by another temporary tax – the state extra income and wealth tax. This extra income tax was slightly progressive, but only affected taxpayers having taxable income above SEK 6,000 (about 3.5 APWs). The top marginal tax rate was 4 percent. The extra income tax rates were doubled in 1936.

3.3. The separate wealth tax in 1934 and 1938

A separate wealth tax was introduced in 1934, alongside the income wealth tax and applied until 2007. This wealth tax levied specific marginal wealth tax rates in different brackets *directly* on net wealth (not taxing added wealth by marginal income tax rates), normally resulting in higher wealth taxes. Initially, the exemption was high, SEK 50,000, which was more than the net worth of many small and medium-sized firms (see section 5 below). The tax rates varied between 0.1 and 0.5 percent. As noted in section 2.2, the introduction of the separate wealth tax in 1934 also entailed a reduction rule.

Effective from 1938, tax rates were slightly increased (to a maximum of 0.6 percent). The exempted amount was more than halved to

8. In 1920, about 98 percent of all persons declaring a taxable income paid the lowest marginal state tax rate or no state income tax at all (*Statistical Yearbook of Sweden 1923*).

SEK 20,000 in the separate wealth tax that was then an integral part of the ordinary tax system by virtue of the 1938 particular tax on wealth, applicable in the 1939-1947 period; see Table 2.

Taxable wealth, SEK	Tax, SEK	Marginal tax rate, %
20,000	0	0.1
40,000	20	0.2
80,000	100	0.3
150,000	310	0.4
300,000	910	0.5
1,000,000	4,410	0.6

Source: Genberg (1942, p. 24) and SOU 1969:54, p. 80.

Table 2. The 1938 separate tax on wealth, 1939-1947

The 1939-1947 defense tax increased the wealth tax rate for larger firms despite the reduction of the part of wealth added to income from 1/60th to 1 percent and the fact that the progressive local tax, the state equalization tax and the extra state income and wealth tax were all repealed (Du Rietz, Johansson and Stenkula 2013). However, only taxpayers having taxable income exceeding SEK 6,000 (between two and three APWs during this period) paid the temporary income and wealth taxes in the 1920-1938 period. The tax rates in the ordinary income and wealth tax that affected almost all taxpayers were increased in 1939 by the 1938 income and wealth tax (SFS 1938:369) to compensate for the repeal of the temporary taxes. With the 1938 income tax – the last combined income and wealth tax – high-income earners were taxed substantially more heavily than the average person.

3.4. The combined state income and wealth tax: 1939-1947

The 1938 income and wealth tax applied from 1939 until 1947 and consisted of a flexible tax rate (the “bottom tax”/*bottenskatt*), which was determined annually by Parliament, and a fixed tax rate (the surtax/*tilläggsskatt*). That is, this income and wealth tax was partly constructed in the same way as the one it replaced. The bottom tax was only slightly progressive, while the surtax was highly progressive, but only levied on income exceeding roughly three APWs. All these changes resulted in increased progressivity of the income tax. The part of wealth that was added and subject to state tax was reduced from 1/60th of a taxpayer’s wealth, in effect from 1911 through 1938, to 1 percent from 1939 through 1947.

Although the equalization tax and the extra income tax were abolished to simplify the tax system, a new defense tax (*värnskatt*) was introduced in 1939. This was a highly progressive combined income and wealth tax payable by most taxpayers. It was raised in 1940 and in 1942, and in effect through 1947. The reasoning behind this tax was analogous to that behind the WWI defense tax. The new income and wealth tax (1939-1947), the defense tax (1939-1947) and high inflation and wage increases all combined to cause a sharp increase of marginal income tax rates for most taxpayers (Du Rietz, Johansson and Stenku-la 2013, p. 17-18).

3.5. The separate wealth tax: 1947-2006

The combined income and wealth tax was motivated by the notion that current income from wealth could be taxed more heavily than labor income (current capital income was taxed jointly with labor income) and therefore additional income could be imputed and taxed. It was also judged that the combined system adhered more closely to the ability to pay principle. The system was abandoned for two reasons: (i) greater simplicity and (ii) an increasing awareness of its disincentive effects when marginal tax rates were becoming much higher.⁹ In 1910 the highest marginal tax rate was a mere 12 percent, while it exceeded 70 percent by the mid-1940s (Du Rietz et al. 2013).

By the 1947 *Royal Ordinance* (Table 3), wealth taxation was defined in a separate law, independent of the income tax law. The system was abandoned for two reasons: (i) greater simplicity and (ii) an increasing awareness of its disincentive effects when marginal tax rates were becoming much higher.¹⁰ In 1910, the highest marginal tax rate was a mere 12 percent, while it exceeded 70 percent by the mid-1940s (Du Rietz et al. 2013).

The tax rates were increased sharply through the 1947 wealth tax schedule, applicable from 1948, when compared to the 1938 separate tax on wealth, with tax rates ranging from 0.6 to 1.8 percent. With the introduction of the new state income tax in 1948, the old combined income and wealth tax as well as the income wealth tax were discontinued.¹¹

9. SOU 1969:54, p. 78-80.

10. SOU 1969:54, p. 78-80.

11. SOU 1969:54, p. 54ff.

Taxable wealth, SEK	Tax SEK	Marginal tax rate, %
30,000	0	0.6
100,000	420	1.0
150,000	920	1.2
200,000	1,520	1.5
300,000	3,020	1.8

Source: SOU 1951:51, p. 225.

Table 3. The 1947 wealth tax, 1948-1952

In the 1950s and 1960s unreduced direct wealth tax rates continuously increased through bracket creep. This occurred in spite of the fact that the top marginal tax rate remained at 1.8 percent until 1970, when it was temporarily raised to 2.5 percent. A final, temporary, wealth tax hike was implemented in 1983. Marginal tax rates ranged from 1.0 to 4.0 percent. In 1984, the top marginal tax rate was reduced from 4 to 3 percent and further to 2.5 percent in 1991 and 1.5 percent in 1992.

The taxation of wealth before 1948 was a complex combination of wealth and income taxation, making it impossible to fully define its aggregate importance. However, that was possible in the 1948-2006 period, when a pure wealth tax was in effect. With the exception of a temporary surge in wealth tax revenue around 1950, wealth taxation was of minor importance as a source of revenue for the government. Revenue from wealth never exceeded 0.4 percent of GDP.

4. The evolution of the wealth tax rate for Swedish family firms and individuals

4.1. Family firms

In order to depict how the Swedish wealth tax rates evolved, we present estimated average wealth tax rates for synthetically constructed family firms and individuals over the entire life-span of the law, from its inception in 1911 until its repeal in 2007. Throughout the analysis, we assume that the firm has only one owner whose total wealth is invested in his/her firm. We calculate annual average wealth tax rates as a percentage of net business equity during the entire period.

The tax rates are applied to three different stylized family firms: one large, one medium-sized and one small firm. The large firm has a net worth assumed equal to 1,000 average annual wages for a full-time production worker (1,000 APWs), and therefore has a starting wealth in 1911 of SEK 986,000, which increases to SEK 261 million in

2006. The large firm owner is assumed to have had a salary of 3.0 APWs but lower than the top marginal tax rate. The medium-sized firm is assumed to have a nominal equity equal to 100 APWs, and thus has an initial wealth of SEK 98,600 in 1911, which increases to SEK 26.1 million in 2006. The marginal tax rate of the owner of the medium-sized firm is assumed to be the same as for an employee earning 1.67 APWs.¹² The small firm is assumed to have nominal net business equity of 10 APWs or SEK 9,860 in 1911, and SEK 2.61 million in 2006.¹³ In the base case, the marginal tax rate is assumed to be equal to the marginal tax rate for the owner of the medium-sized firm (at 1.67 APWs).

Figure 1 depicts the long-run evolution of the unreduced direct wealth tax rate paid by the owner of a large family firm with equity of SEK 261 million in 2006 (almost 30 million euros at the time). The assessed tax rate varied greatly over time, increasing in the postwar era and peaking in the early 1970s, and then falling to zero in 1991. Until 1934, the wealth tax hovered between 0.1 and 0.2 percent. The one exception was the year 1913 when the defense tax temporarily sharply increased the wealth tax to 0.82 percent.¹⁴

12. An annual income of 1.67 APW is used to attain consistency with other studies in the overall project (e.g., Du Rietz et al. 2014), and because this is one of three income levels used by the OECD when comparing effective marginal tax rates across countries, e.g., OECD (2011). The other two levels used by the OECD are 0.67 and 1 APW.
13. The size of our synthetically constructed firms is chosen so as to be fully comparable with the analysis in our companion paper on Swedish inheritance and gift taxation (Du Rietz, Henrekson and Waldenström 2012). In that paper we assume that there are two heirs, each inheriting 50 percent of the firm.
14. The owner of the large firm (is assumed to have) had a salary of SEK 3,185 (three APWs) and firm equity of SEK 1,061,500 in 1913. Wealth subject to income taxation amounted to SEK 106,150 (10 percent of 1,061,500). The wealth tax on this amount was SEK 8,047 + SEK 636 in ordinary income and wealth tax, thus totaling SEK 8,683. Hence, the total average tax for the two tax types combined was $8,683/1,061,500 = 0.82$ percent. The assumed salary of three APWs is arguably on the low side for a large firm owner. On the other hand, it is not unreasonably low considering that retained earnings were taxed much more lightly; there was no capital gains tax and the 1913 extra defense marginal tax schedule was highly progressive and applied alongside the ordinary 1911-1919 tax schedule.

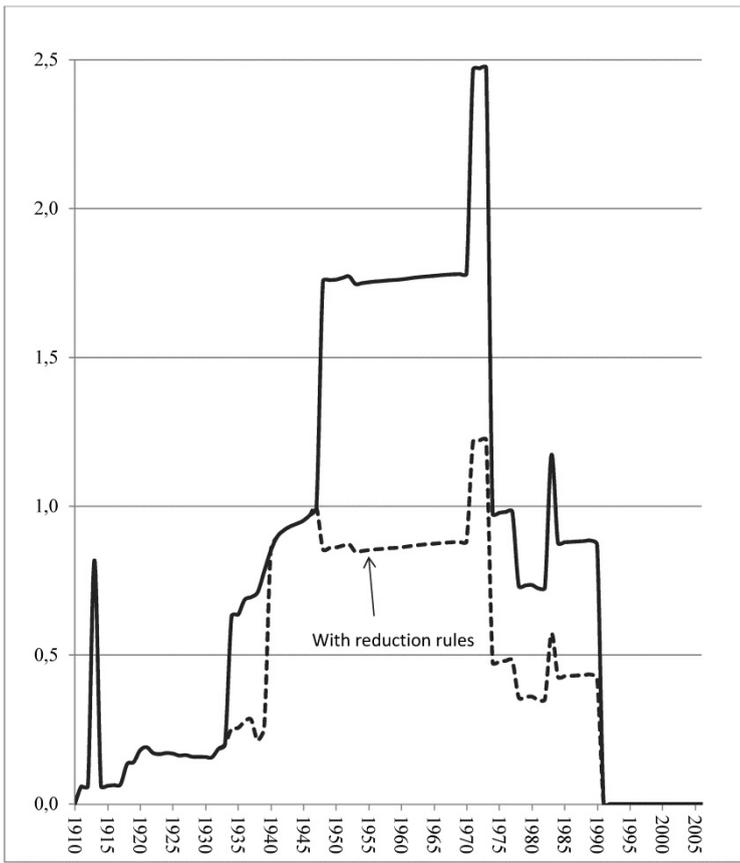


Figure 1. Effective wealth tax rate and total wealth tax, with and without reduction rules, for an owner of a large firm, 1911-2006 (% of firm net equity)

Source: Calculations made by the authors.

Note: The net worth of the large firm is 1000 APW (corresponding to SEK 261 million in 2006).

A permanent rise in unreduced wealth taxation occurred in 1934 with the introduction of the separate wealth tax, in effect tripling the entrepreneur's wealth tax rate to 0.6 percent. The 1938 income and wealth tax, effective from 1939, and the defense taxes in 1939-1947 resulted in a gradual increase of the direct wealth tax rate by another 0.3 percentage points. The next tax hike occurred in 1948 when the direct wealth tax rate was increased from 1.0 to 1.8 percent. Large firm owners, however, by using the rule that reduced taxable wealth to at most 25 times taxable income, but at least 50 percent of taxable wealth in 1934-1937 and 40 percent of taxable wealth in 1938-1939, avoided wealth tax increases until 1940, when the reduction rule no longer applied.

The repeal of the reduction rule more than tripled the effective tax rates.

The wealth tax schedule effective from 1971, led to a further substantial increase of the average direct tax rate from 1.8 to almost 2.5 percent. The top marginal tax rate was increased from 1.8 percent in the period 1948-1970 to 2.5 percent in 1971-1973. The unreduced wealth tax rate then increased sharply to 2.47 percent, while the reduced wealth tax rate stabilized at 1.2 percent of firm equity.

In 1974, tax authorities allowed a greater undervaluation of firms' stocks-in-trade and inventories, leading to the unreduced wealth tax rate being more than halved from 2.5 to 1.0 percent.¹⁵ The wealth tax on corporate equity dropped further in 1978 to 0.7 percent when only 30 percent of the net worth (*substansvärdet*) of firms was subject to wealth taxation, but then with increased tax rates in 1983 rose temporarily to 1.2 percent. It decreased to 0.9 percent in 1984, when the top marginal tax rate was reduced from 4 to 3 percent. The reduced wealth tax rate also dropped in 1974, from 1.2 to 0.5 percent, and then to 0.4 percent in 1978. It remained roughly at that level until the wealth tax for unlisted corporate equity was abolished in 1991.

Turning to the medium-sized firm (with an equity of SEK 26.1 million, or almost 3 million euros in 2006), Figure 2 shows the average tax rate paid by the owner of such a firm. The long-run trend resembles that of the large family firm, but at a lower level. Before the introduction of the separate wealth tax in 1934, the medium-sized firm owner paid below 0.1 percent in wealth tax with the exception of 1913 when the defense tax was levied. In 1934, the average full direct tax rate increased to 0.2 percent, and then to 0.4 percent in 1939. It gradually increased until 1948 when it more than doubled again, to 1.35 percent. The tax rate continued upward to 1.52 percent in 1952, and peaked two decades later in 1973 at 1.7 percent. It fell considerably in the 1974-1977 period to barely 0.8 percent as a result of the lower valuation of inventories and stocks-in-trade. In 1978 it decreased to 0.6 percent with the 30 percent valuation rule, and then fell to zero in 1991.¹⁶ Thanks to the reduction rule, the wealth tax rate did – analogous to the large firm – hardly increase in 1934, only somewhat in 1939, but then climbed steeply from 1940 through 1947 when no reduction rule applied.

15. The impact of this alleviation was not uniform across industries. Service sector firms with small stocks and limited inventories were relatively disfavored.

16. Proposition 1991/1992:60, p. 1.

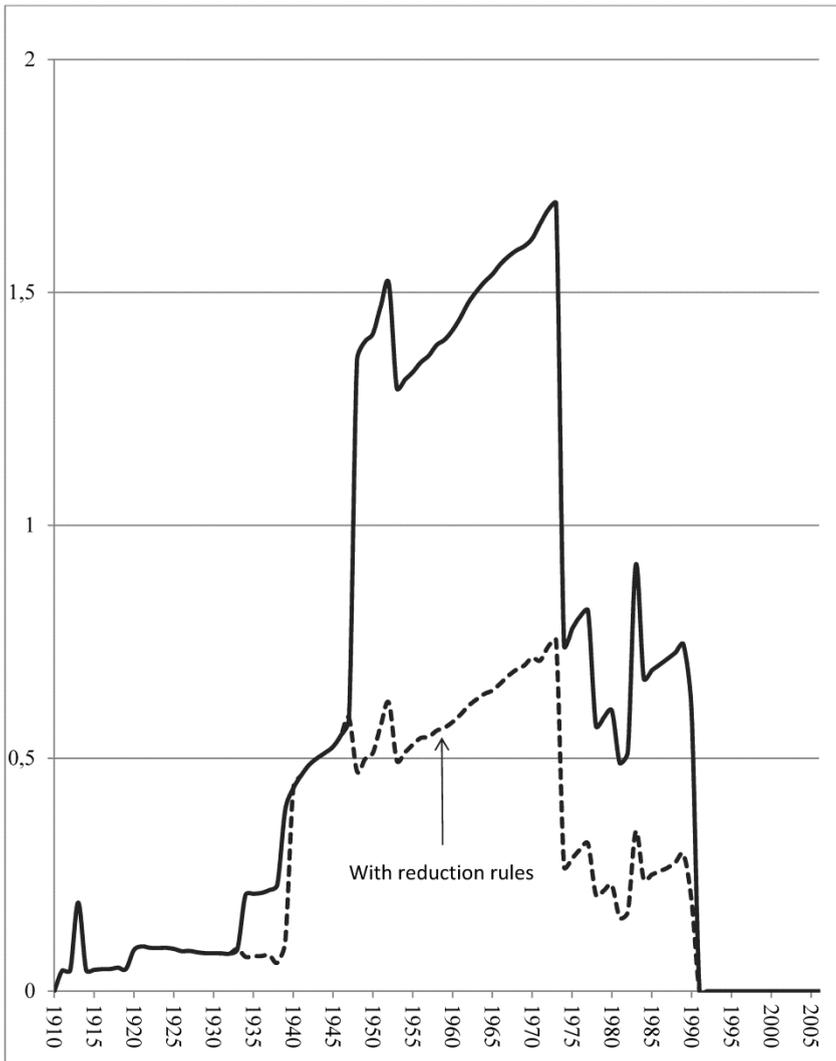


Figure 2. Effective wealth tax rate and total wealth tax, with and without reduction rules, for owner of a medium-sized firm, 1911–2006 (% of firm net equity).

Source: Calculations made by the authors.

Note: The net worth of the medium-sized firm is 100 APWs (corresponding to SEK 26.1 million in 2006).

In 1948 the reduction rule resulted in an effective direct wealth tax rate of 0.47 percent, a sharp drop when compared to the unreduced tax rate of 1.35 percent. During the 1950s and 1960s, both the unreduced and the reduced direct wealth tax rate increased slowly, but the

reduced rate level remained at less than half the level of the full tax rate.

Figure 3 shows the average direct wealth tax rate paid by the owner of the small firm (with an equity of SEK 2.6 million 2006). The average direct tax rate began at 0.02 percent in 1911, increased to just below 0.1 percent between 1919 and 1939, to 0.2 percent from 1940 through 1947 and to around 0.3 percent in 1948. The 1948-1953 tax schedules continued to increase the wealth tax rate until it peaked in 1951 and 1952 at 0.4 percent, because the size of the exemption (SEK 30,000) was unchanged through 1952.

Between 1954 and 1973, the average wealth tax rose from 0.23 to 0.73 percent as an increasingly larger fraction of firm equity exceeded the exemption level. In addition, the net business equity of the small firm owner did not exceed SEK 500,000, which excluded the owner from the 1971-1973 small-firm asset relief. From 1974, the lower valuation rules for corporate equity diminished the wealth tax drastically to zero for small-firm owners, apart from a low positive rate in 1976, 1977, 1980 and 1989.

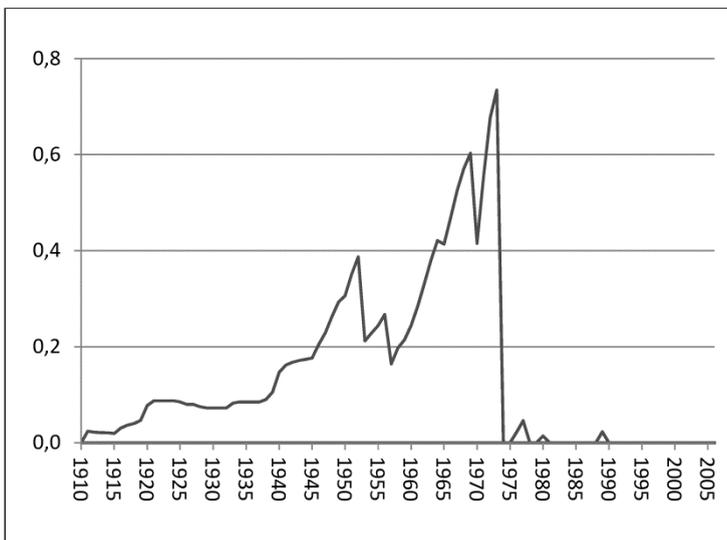


Figure 3. Direct wealth tax for an owner of a small firm, 1911-2006 (% of firm net equity)

Source: Calculations made by the authors.

Note: The net worth of the small firm is 10 APWs (corresponding to SEK 2.6 million in 2006). Reduction rules are assumed not to be applicable.

When calculating the wealth tax rate, one important aspect is how the entrepreneur finances wealth tax payments. Selling off assets or stock to pay the direct tax minimizes additional taxes incurred. In practice, however, that may not always have been feasible or desirable. One option for entrepreneurs to finance wealth tax payments was by means of additional dividends. This was more expensive than selling off stock, since dividends were taxed jointly with labor income until 1991; owners had to pay labor income tax on these dividends before the remainder could be used to meet wealth tax obligations. Family firm owners could extract an extra salary payment from the company to pay the tax. But that would give rise to additional taxation at an even higher rate, since in addition to the ordinary labor income the firm would have to pay payroll taxes.

However, it should be noted that before any dividend payments could be made from a firm, corporate tax had to be paid on the profits. From 1951 until 1990 the statutory corporate tax rate was never below 46 percent, and in the 1970s and 1980s it was on average roughly 55 percent (Davis and Henrekson 1997).

Finally, owners could simply take loans to finance tax payments, at least in theory. Debt financing was a favorable mode of payment because it did not give rise to the extra income taxes associated with dividends. However, this strategy was normally not an option until the mid-1980s, because of the strict quantitative regulation of credit markets.¹⁷ In other words, in addition to the wealth tax owners potentially faced high indirect wealth-related taxes. During the 1970s and 1980s, when the marginal dividend tax was at 70 percent or above, and as much as 85 percent in the 1977-1981 period, these indirect taxes were almost prohibitive.

For calculations including these indirect effects in the case when wealth tax payments are met by extra dividend payouts the reader is referred to Du Rietz and Henrekson (2014). For the large firm these calculations show that from the late 1940s until 1990 the effective unreduced wealth tax financed through dividends was invariably above 3 percent, and for most of these years it hovered between 4 and 6 percent (between 2 and 3 percent when the reduction rule applied). Due to the fact that entrepreneurs, in practice, were forced to withdraw funds from their firms to pay wealth tax (unless they were willing to

17. Even if there had been no quantitative restrictions preventing such lending, it would have been difficult to find a credit institution willing to grant loans to be used to pay taxes likely to arise every year for the foreseeable future. Moreover, entrepreneurs are unlikely to be willing to use personal borrowing to meet tax payments year after year, thereby gradually increasing their financial risk.

sell part of the firm to pay the tax), running large family firms became extremely unfavorable from the 1960s through the 1980s.

Finally, when we look at the wealth tax rates of all three firm types together, both clear similarities and differences become apparent. First, they all follow largely the same time trend in taxation, starting off from a relatively low level in the years before WWII. After the war, tax rates increased sharply until 1973. In 1974, these high levels dropped due to the comprehensive valuation reductions.

In terms of tax levels, the experiences of the three differently sized family firms diverge significantly. Comparing the large and the medium-sized firm, the effective total tax rate of the large firm owner was roughly twice the effective rate for the owner of the medium-sized firm for a long time. But as a result of lowered exemption levels, the effective wealth taxation of the large and medium-sized firm owner almost converge in the late 1970s. In contrast, for the small-firm owner the direct wealth tax rate for most years was relatively low. The main exception is the decade 1963-1973, when it consistently exceeded 0.4 percent. In 1974, the small firm tax rate fell to zero.

4.2. Private individuals

Figures 4, 5 and 6 present the wealth tax rates paid by the three individuals whose level of wealth corresponds to the corporate wealth of the owners of the large, medium-sized and small family firm, respectively, as discussed in the previous subsection. We only calculate the direct wealth tax for individuals. In order to pay the wealth tax incurred, individuals may have had to pay capital gains tax when selling assets in order to meet tax payments. To the extent this is true we tend to underestimate the total effective tax.¹⁸

In 1978 listed stock was valued at 75 percent of the quoted value, motivated by the latent capital gains tax. This was raised to 80 percent in 1997. Real estate was taxed based on the assessed value, measured at 75 percent of the market value. On these grounds, we assume that the average valuation of non-corporate assets was 100 percent before 1978, and 75 percent from 1978 onwards.

Figure 4 shows that wealthy individuals – with fortunes equal to the owners of family firms – faced the same direct wealth tax rates as

18. Until 1966 the long-term capital gains tax (holding period > 5 years) was zero. From 1967 to 1975 about 25 percent of long-term capital gains can be estimated to have been taxable (Du Rietz, Johansson and Stenkula 2014). Formally, 10 percent of the proceeds of sales of long-term shares were included in personal income. From 1976 to 1990, 40 percent of long-term gains were taxable (holding period > 2 years). Short-term capital gains were always fully taxable at the labor income tax schedule.

the corresponding firm owners in all years through 1973. If the maximum reduction rules applied, the wealth tax rate fell to approximately 0.2-0.3 percent in the period 1934-1939. In 1940 it then rose sharply to 0.9 percent when no reduction rule applied and further to 1.2 percent from 1971 until 1977, finally peaking at 1.47 percent in 1983. The tax rate fell to 0.6 percent in 1991-1992 and stayed at that level through 2006. With the introduction of the valuation relief for unlisted net business equity in 1974, effective wealth taxation of the two types of wealth holders began to diverge. The beneficial treatment of unlisted firm equity was reinforced through the tax rules introduced in 1978. Such beneficial treatment was not extended to non-corporate wealth. As a result, wealthy individuals paid between two and almost three times more than the medium-sized or large firm owners. The difference was even greater for small wealth holders.

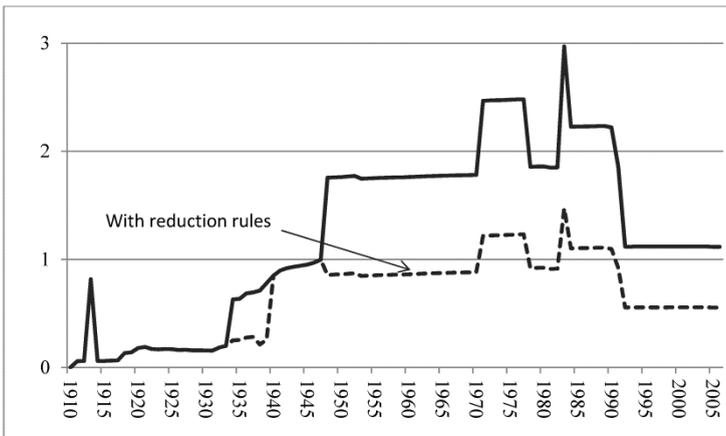


Figure 4. Effective wealth tax rate for an individual having wealth equal to the large-firm owner, 1911-2006 (%)

Source: Calculations made by the authors.

Note: The person's wealth is 1,000 APWs (SEK 261 million in 2006).

Figure 5 shows that an individual having non-corporate wealth at the level of the owner of the medium-sized firm faced the same direct wealth tax rate as did the firm owner in all years through 1970. From 1971 moderately wealthy individuals paid a higher wealth tax, while from 1974 their direct wealth tax was three times higher than for firm owners of equal wealth.

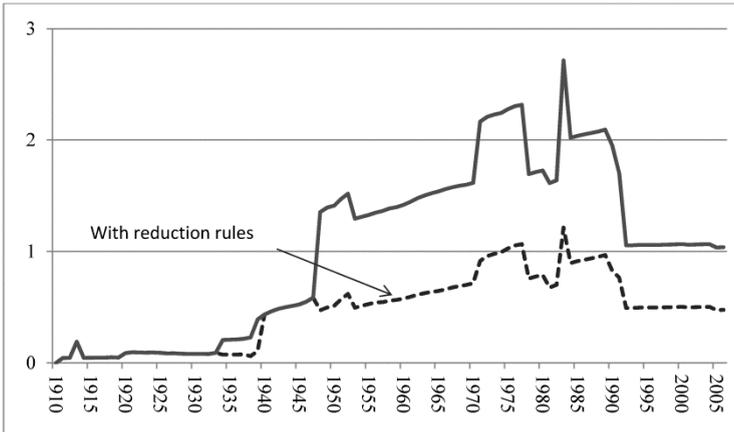


Figure 5. Effective wealth tax rate for an individual having wealth equal to the medium-sized firm owner, 1911-2006 (%)

Source: Calculations made by the authors.

Note: The person's wealth is 100 APWs (SEK 26.1 million in 2006).

Figure 6 shows that an individual having wealth of the same level as the owner of the small firm faced the same direct wealth tax rate as did the firm owner in all years through 1973. From 1974, the direct wealth tax for the small firm owner fell to zero (but for a few years), while our corresponding individual continued to pay wealth tax at a rate of nearly 1 percent until 1978 when the tax rate was reduced to 0.6 percent. In 1979-1980 the tax rate increased to 0.7 percent. Temporarily, in 1981-1982, the tax rate almost fell to 0.2 percent due to increased bracket boundaries. During the period 1990-2004 the tax rate varied between 0.4 and 0.5 percent, falling to between 0.2 and 0.3 percent in 2005-2006.

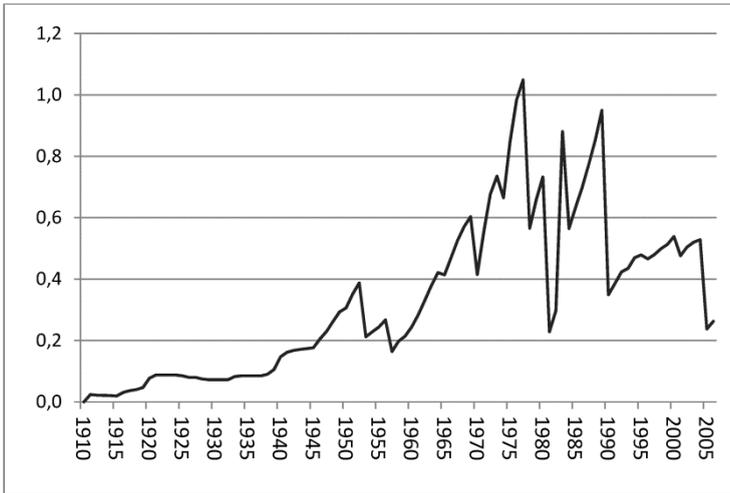


Figure 6. Effective wealth tax rate for an individual having wealth equal to the small-firm owner, 1911-2006 (%)

Source: Calculations made by the authors.

Note: The person's wealth is 10 APWs (SEK 2.61 million in 2006).

5. Why was the wealth tax abolished?

Before addressing the question in the heading above, it should be noted that a decade ago the inheritance and gift tax was abolished by a socialist government, while the wealth tax was retained. A priori, puzzling in 2004 over which one of those taxes to abolish, one would have expected the reverse. The law professor and tax expert Sven-Olof Lodin (2009), who had a unique insight into the discussions at the time, maintains that this was because the Prime Minister asked Lars Ohly (then leader of the Left Party) to choose which of the two taxes he wanted to abolish. He chose the inheritance tax. This privilege was bestowed upon Ohly because the Social-Democrats led a minority government that was dependent on the support of the Left Party, which had already made it clear they could support the abolishment of only one of the two taxes. Faced with this choice, Ohly opted for the inheritance tax.

There is little, if any, evidence that this decision resulted from the Left Party seriously weighing and comparing the ideological and redistributive aspects of the two types of taxes. A more likely explanation is that the *Zeitgeist* at that point in time attributed more symbolic weight to the wealth tax. And it appears that no influential politician

(on the left) took the trouble to argue that for anyone concerned with the issue of redistribution it would be far wiser to retain the inheritance and gift tax.

But as we have noted, the wealth tax only outlasted the inheritance tax by two years. So why was the wealth tax eventually abolished? First, one should note that despite high statutory tax rates and rapidly increasing wealth levels, especially following financial market deregulation in the 1980s, wealth tax revenue remained low. This is in itself a strong indication that people could with impunity evade the tax by taking appropriate measures.

What at first sight may seem paradoxical is that the most important of these measures were provided by the politicians themselves in order to alleviate perceived problems in key areas caused by wealth taxation. The first measure was the reduction rule, introduced in 1934, which could and did cut wealth tax payments by half for the very wealthiest. A second set of measures were the various forms of valuation relief for unlisted firms' net business equity introduced in the 1970s, and the full exemption of such assets from 1991. A third measure was the exemption of land and forest holdings from 1991. In 1997 controlling owners of listed firms (defined as having at least 25 percent of the votes) were exempted.¹⁹ Throughout the tax's century long lifetime, art objects, antiques, gold, silver, and uncut gems were exempted.

In 1989 all foreign exchange controls were lifted, making it difficult to prevent people from transferring wealth to tax havens, either illicitly or when taking residence in another country. Several studies found that a sizable share of large fortunes was being placed outside of Sweden in countries like Luxembourg and Switzerland. In those cases the government not only lost income from wealth taxation, but also tax revenue on capital gains, dividends and interest income. The Swedish Tax Authority (*Skatteverket*) reported that in the early 2000s the value of assets illicitly transferred offshore may have amounted to more than SEK 500 billion, and the accumulated assets of Swedish billionaires living abroad were at least as large (Edin, Hansson and Lodin 2005, p. 179). The magnitude of these outflows was a major motivation for the repeal of the wealth tax in 2007 (Regeringens proposition 2007/08:26, p. 34). Three years earlier a major government commission had concluded (SOU 2004:36, p. 260): "If the wealth tax is abolished it is possible that wealthy Swedes having unreported assets

19. Regeringens proposition 1996/97:117, p. 36-47.

abroad repatriate their assets to Sweden and that wealthy individuals move (back) to Sweden.”²⁰

The many opportunities for tax planning that were opened up – in most cases in order to alleviate the effect of what was considered to be an excessively high standard wealth tax rate – and the new opportunities to transfer assets abroad, were said for people having great wealth to in effect make the wealth tax largely “voluntary”.²¹ By contrast, it was deemed to be much more difficult for people with moderately high income and wealth to evade wealth taxation.

Thus, the numerous forms of relief and exemptions introduced over the years not only lowered wealth tax revenue, they also increased the distortive effects of the wealth tax. Most important among these effects were capital outflow and an unsustainable valuation and growth of asset classes exempted from wealth taxation. These asset holdings were often financed by borrowing, which in turn resulted in increased financial fragility.

These problems were in plain sight and there was no lack of awareness of them. For instance, the Tax Base Commission (*Skattebasutredningen*) in their 2002 final report (SOU 2002:47) presented the stark choice. They suggested that either the base for wealth taxation be broadened to *all* important asset classes combined with a much lower tax rate than the prevailing 1.5 percent, or if that was not possible it should be abolished.

Looking back, it is clear that the government did not try to argue and explain to the electorate why it would be favorable to substantially reduce the wealth tax rate and apply it to a much broader asset base. Instead, while the distortionary effects resulting from evasive behavior were growing, the system remained unreformed. Strong evidence that the distortive effects increased rapidly is given by the fact that between 2001 and 2006, when aggregate household net wealth increased by roughly 60 percent, total wealth tax revenue fell from SEK 8.4 billion to SEK 4.8 billion. Hence, the lack of reform around the turn of the millennium eventually made full abolishment the only option.

A reformed wealth tax could arguably have performed a redistributive role in society. However, whether that is possible given today’s integrated financial markets is open to dispute. The now unfolding tale of the 2012 reintroduction of a wealth tax in Spain may offer us some insights in the years to come.

20. In Swedish: “Om förmögenhetsskatten avskaffas är det möjligt att svenskar med oredovisade tillgångar i utlandet flyttar tillbaka kapitalet till Sverige och att förmögna personer flyttar (tillbaka) till Sverige.”

21. See, e.g., Eklund (1998, p. 40-49) and SOU 2004:36, p. 458.

6. Concluding remarks

We have provided an exploratory analysis of the system for taxation of wealth in Sweden. The analysis begins in 1911, when the income wealth tax was introduced. It ends in 2006, the last year wealth was taxed.

Until 1934, with the exception of 1913, taxes were low even for entrepreneurs owning very large firms and for individuals with the largest fortunes. In 1934, wealth tax rates were sharply increased for owners of large firms and rose gradually through the war years and up to 1948 when tax rates were once more sharply raised. A third wealth tax hike occurred in 1971, and effective tax rates peaked in 1973 for entrepreneurs and in 1983 for other individuals. Thereafter, new valuation rules concerning net business equity in family firms lowered tax rates. Additional tax reliefs were enacted in 1991 and 1992 that led to further tax reductions. This trend continued until the final abolishment of the entire wealth tax on January 1, 2007.

When considering wealth tax effects, the total effects are arguably more important than the direct wealth tax effects. The wealth tax had to be paid annually. Firm owners often had to finance wealth tax payments through additional dividend payouts that were taxed at high marginal income tax rates. The total effective wealth tax was in such cases much higher than the direct wealth tax. It peaked at high levels in the 1970s and 1980s.

The taxation of wealth before 1948 was a complex combination of wealth and income taxation, making it impossible to truthfully measure its aggregate importance. That is possible from 1948 when a pure wealth tax was in effect. With the exception of a temporary surge in wealth tax revenue around 1950, wealth taxation was of minor importance as a source of revenue for the government. Wealth tax revenue typically varied from 0.5 to 1 percent of total tax revenue from the early 1970s until 2006. As a share of GDP it averaged just 0.2 percent, never exceeding 0.4 percent.²²

We also end by a brief, and admittedly speculative, discussion of why the wealth tax was eventually abolished rather than reformed. Around the turn of the millennium several government commissions identified the harm caused by the wealth tax system, and also suggested reforms. It seems that there was a lack of political entrepreneurship explaining why a thoroughly reformed wealth tax system based on a lower tax rate and an extensive broadening of the tax base was the *only* viable alternative to a total abolishment.

22. Source: *Statistical Yearbook of Sweden 1949-2008*, Rodriguez (1980) and Statistics Sweden.

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