

Wealth taxes on individuals may skew corporate decision-making

Study finds wealth taxes are linked to higher dividends and lower investment by some companies.



March 15, 2023

Individual wealth taxes, a perennial option for governments seeking new additions to their taxation toolbox, may have an unexpected and potentially damaging impact on corporate

decision-making, the experience in Europe has shown.

A [new study](#) by IESE professor [Gaizka Ormazabal](#), together with Raül Barroso of IESEG School of Management and Donald N'Gatta of MDE Business School, looks at the impact of wealth taxes on dividends and investment in Europe, where this type of levy is relatively common. The findings provide cause for caution.

Wealth taxes in Europe are normally levied as a percentage of an individual's total net wealth, which is calculated as the person's taxable assets — from real estate and bank accounts to securities — minus their debts, which are frequently mortgages and other loans.

Many corporate executives hold a percentage of their wealth as stock in their company. When the value of those stocks increase, so does the holder's wealth tax obligation — and the taxes must be paid in cash annually.

How to meet those obligations? One way is through higher dividend payments from the stocks.

The study showed that closely held companies, particularly family firms, were more likely to raise dividends when majority stockholders were facing a sharp increase in wealth taxes. Dividends in companies with executives facing a spike in wealth taxes were approximately 3.5% higher than in companies where this was not the case.

This can eventually harm the companies — and stock market reaction seemed to support this concern. Large dividends are normally applauded by investors, but market reaction to higher payouts was decidedly more muted when they appeared to be linked to wealth tax obligations. The study found that stock price increases were about 50 basis points lower in these unusual tax situations than could be otherwise expected with a big dividend announcement.

And the higher dividend payouts in these companies were in turn associated with declines in subsequent investment, with its probable impact on the long-term health of the company. Firms with very strong dividends were very likely to invest heavily in the following years, but companies impacted by the wealth tax did not follow this behavior. That was another indication that the high dividend payout responded to executives' tax needs.

All of this is not to say that wealth taxes should be eliminated or avoided; in fact, they may have benefits in terms of social equity. But policymakers should be aware of their potential impact on corporate decision-making and the long-term health of certain types of companies.

About the study

The paper, "[Individual Wealth Taxes and Corporate Payouts](#)," is published in the American Accounting Association's *The Accounting Review*. The researchers evaluated publicly available data on 4,381 companies based in 26 European countries that have, or had, wealth taxes between the years 2000 and 2017.



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