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Reducing Inequality: Taxation and Philanthropy in China and the United States

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Inequality is a growing area of concern in both China and the U.S. Unequal distribution of wealth has affected how the very rules of both societies are shaped, and has created disproportionately greater opportunities for those with substantial wealth. This paper considers taxation and philanthropy as possible means for reducing inequality. In analyzing policies on taxation and philanthropy, this paper concludes that despite limitations and unintended consequences, under the current systems in China and the U.S. taxation and philanthropy can and should be more effectively used to reduce inequality.

Keywords: Capital, Income Inequality, Taxation, Philanthropy, China, United States

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Introduction

Over the last fifteen years economist Thomas Piketty and his colleagues have compiled an extensive data set that analyzes worldwide trends in inequality since the eighteenth century. Their findings, published in the book *Capital in the Twenty-First Century* in April 2014, have already garnered tremendous attention. Piketty's research has redirected public interest to the issue of wealth distribution—ending what author Moses Naim termed "our peaceful coexistence with inequality" (Naim, 2014)—and provided ammunition to activist movements such as Occupy Wall Street. Soon after the book's publication Pope Francis publicly declared that "inequality is the root of social evil" (Frye, 2014), and academic journals have published significantly more articles about inequality (Naim, 2014).

In short, Piketty's main assertion is that the share of wealth held by the world's richest has sharply risen in recent decades—based on his assumption that inequality grows when the rate of return on capital exceeds economic growth (rendered as $r > g$). While capital is often concentrated in the hands of relatively few, income from labor is more evenly dispersed throughout the population as a whole. Given that wage growth is directly dependent on economic growth, then, economic inequality is bound to worsen if economies expand at slower rates than capital earnings. The impact, he posits, is a return to a system based on inherited wealth—and the stasis that it will create (Piketty & Goldhammer, 2014).

With regard to solutions, Piketty recognizes that taxing capital income heavily enough to reduce private returns to less than the growth rates would stunt economic growth. Instead he proposes a comprehensive international agreement to progressively tax capital, in order to avoid wealth concentration at the uppermost echelon of society. He acknowledges the political difficulties of such a plan, but insists that with the proper checks and balances in place, it would be feasible. Piketty's research has received widespread acclaim, and also fielded a number of challenges. Some have contested the theoretical framework, and suggested that rates of return on capital do not exceed economic growth in the long term (Milanovic, 2014). Most critiques have centered on his policy suggestions, however, arguing that a progressive wealth tax is politically infeasible at best, and potentially harmful—undermining investment in human capital and the creation of new businesses (Cowen, 2014).

In *Capital in the Twenty-First Century*, Piketty and his colleague approach China's rising inequality with some degree of optimism. As they point out, between 2000 and 2010 the top 1% of China's share of national income was less than that in India, Indonesia, Britain, Canada, South Africa, Argentina, and the U.S. Furthermore, as a regional power China faces relatively little pressure to cut taxes or significantly change its progressive tax system, and has remained untouched by the stampede toward complete deregulation (Piketty & Goldhammer, 2014). China strictly regulates foreign investment and outgoing capital. However, China's wealthiest 1% have accumulated an increasing share of capital in recent years, and stark inequalities do exist. Additionally, Piketty and his colleague complained of limited availability of data in China, and propose that corrupt officials may have overstated growth rates of economy — which would have obscured the true picture of inequality.

Wealth inequality in U.S. and China

Piketty's research has meaningfully impacted the discourse on the capitalist system, and drawn much deserved attention to the problem of growing inequality in the United States. While income has traditionally been used as the standard measure of well-being and progress, there are many instances of those with approximate incomes experiencing different levels of well-being and stability. The debate about economic inequality is now rightfully including analysis of capital and wealth. Research show that in the U.S. people underestimate the level of wealth inequality, and across the political and economic spectrum, show consensus in desiring a more equal wealth distribution than what currently exists (Norton & Ariely, 2013).

Wealth inequality in the U.S. has been linked to growing indebtedness through mortgage and credit card obligations, the collapse in value of assets during the Great Recession, and stagnant real wages (Saez & Zucman, 2014). In this country wealth inequality is also manifestly connected to issues of racial discrimination and other forms of oppression (Oliver & Shapiro, 2006). In fact, wealth inequality has widened considerably along racial and ethnic lines since the end of the Great Depression (Kochhar & Fry, 2014). In 2013 the net worth of white households was thirteen times greater than that of black households (compared to ten times greater in 2007), and ten times greater than that of Hispanic households (compared to eight times greater in 2007) (Kochhar & Fry, 2014).

In discussing wealth inequality, it is likewise important to consider the opportunity gap. People make decisions about education, investment and employment based not only on resources available to them, but also on the expectations of what such decisions may lead to. Unequal distribution of wealth affects how the very rules of our society are shaped—through lobbying and campaign contributions, for instance—and thereby creates disproportionately greater opportunities for those with substantial wealth. As a recent example, during the economic recovery in the wake of the Great Recession, minority households' median income has decreased much more than white households' has. This is owed in part to the fact that whites are much more likely than minorities to own financial assets, which have recovered in value more quickly than has housing (Kochhar & Fry, 2014).

The U.S. debate about economic inequality has mirrored an ongoing, worldwide conversation. In China, the landscape is certainly different, but wealth inequality is a growing area of concern. In 2001 Kanbur and Zhang identified that China was entering its third "peak of inequality" since the Communist Revolution, following those coinciding with the Great Famine of the late 1950s and the Cultural Revolution in the late 1960s. According to the authors, a key dimension of inequality in China was that between inland and coastal provinces (Kanbur & Zhang, 2005). Several years later, Zhang, Yang and Wang (2010) found that China had passed the Lewis turning point (the point at which surplus labor is fully absorbed into the market-based sector) and had moved from a period of unlimited supply to an "era of labor shortage." In light of this shift, the authors argued, China would likely reorient its development strategy toward more capital intensive and skill-based labor practices. Such a shift often leads to a wider inequality and opportunity gaps, as unskilled and uneducated workers are proverbially left behind.

Today China continues to experience income and wealth inequality alongside rapid economic growth. Currently its Gini coefficient is estimated to be in the range of 0.53-0.55 (Xie & Zhou, 2014). Its transition from a socialist planned economy to an increasingly market-based system has differentiated among its people based on productivity, human capital, effort, entrepreneurship, and wealth holdings, as well as by occupation and region (Shi, Li, Sato, & Sicular, 2013). However, researchers debate whether China's wealth inequality in recent years has increased or declined. Ward (2014) found that wealth inequality has declined in China, likely due to economic reforms and an expanding social welfare system. Other researchers hold that disparities have widened (Fan, Kanbur, & Zhang, 2011; He & Huang, 2012; Shi, Li, Sato, & Sicular, 2013).

In contrast to the U.S., where race and ethnicity play a key role, China's wealth inequality is rooted primarily in the rural-urban divide (Yang, Huang, & Liu, 2014). The household registration system, which divides the population according to urban and rural residency, has contributed to social stratification by imposing institutional barriers to obtaining education, employment, and health care (Hu, Lu, & Huang, 2014; Yang, Huang, & Liu, 2014). Rising inequality in China is also related to income from property and assets. The government has worked toward privatizing urban housing, developing urban residential real estate markets, and expanding capital markets. Chinese property prices are rising faster than wages and profits in the manufacturing sector. In effect, the return on capital investments for an elite group of real estate owners is growing faster than China's GDP (Shi, Li, Sato, & Sicular, 2013).

Research Purpose and Method

In addition to social welfare system, taxation and philanthropy are two alternatives to reduce income inequality and have received increasingly attention around the world (Piketty & Goldhammer, 2014; Lu, 2015). In this paper we will look at various forms of taxation in the U.S. and China, as well as in Japan, Germany and Sweden—nations representing the other major social welfare regime types—in order to analyze connections between these respective tax systems and economic inequality in each country. We will also consider Piketty's proposed global wealth tax and its possible application and ramifications in the U.S. and China, and explore the reasons why other countries have chosen to adopt, and abolish, taxes on wealth. Finally, we will consider impacts of philanthropy on economic inequality, and the mechanisms by which it may affect inequality moving forward. We utilize secondary data to conduct the analyses.

As social welfare systems aim to redistribute wealth in the interest of social well-being, presumably the differences in taxation and charitable giving reflect disparate ideological and political systems. The U.S. social welfare regime is liberal, dominated by market logic and featuring modest, means-tested benefits (Esping-Andersen, 1990). Germany is a conservative-corporatist regime: social welfare is based on occupation and status, and benefits have limited redistributive effects. On the other end of the ideological spectrum, Sweden is a social-democratic state, where left-wing party and class coalitions bolster traditions of universal entitlement (Esping-Andersen, 1990). China and Japan, as well as other East Asian regimes, are typically considered conservative-corporatist, with some features resembling the liberal model (Esping-Andersen 1990,1999; Lee & Ku, 2007; Lu, Lin, Vikse, & Huang, 2013). Holliday (2000) argued that the social welfare system in East Asian regimes focuses on productivism—the relationship between social and economic policy. As productivity has been viewed as a reflection of national power, social welfare is considered, most importantly, to be an investment towards economic growth (Holliday 2000, Holliday and Wilding 2003).

The information on tax and philanthropy came from various government websites and reports, majority came from tax and revenue departments. It is also important to note that there may be slight variation in tax liability, and the income subject to tax. In each of these countries residents are taxed on their worldwide income, which includes wage and salary income, pensions, fringe benefits and most allowances, but some minor variances do exist (Ernst & Young, 2015). These countries also vary in the number of brackets used. For income taxation, for instance, China and the U.S. each use seven brackets, while the German system defines only four. The variances of taxation and charitable giving deductions in these countries reflect the regimes' differences and may shed a light on potential direction for some countries.

Current Taxation and Charitable Deduction

Progressive personal income taxation is one way that nations address inequality. As previously discussed, China's personal income tax is highly progressive, in part to offset the regressive impact of its indirect taxation (e.g. value-added tax, business tax and consumption tax). As detailed in table 1, China's lowest tax rate is only 3%, compared to 5% in Japan, 10% in the U.S. and Sweden, and 14% in Germany. China's top rate is 45%, the second highest after Sweden's 58%. China, Japan and Sweden feature the widest range of tax rates (3-45%, 5-40%, and 10-58% respectively). In contrast, German and U.S. tax rates range only between 14-45% and 10-39.6%, respectively. The Swedish tax system is often considered to be among the most progressive, given that its 58% top rate actually targets a relatively large number of taxpayers. Although the lowest tax rates in the U.S. and Sweden are relatively high at 10%, it is important to consider how these countries' social welfare systems alleviate the impact of taxation on their lowest-income individuals and families.

Capital gains taxes are levied on the profits realized on the sale of stocks, bonds, precious metals and property. According to Hungerford (2013), capital gains income was the largest contributor to increasing income inequality between 1991-2006. With regard to capital gains taxation, China and the U.S. stand out as shown in Table 2. China does not explicitly tax capital gains, but applies a flat 20% tax on income derived from the transfer or sale of property and on financial securities income (Ernst & Young, 2015). The U.S. capital gains tax is dependent on whether investments are shorter or longer than one year—if shorter, gains are taxed according to income tax brackets, and if longer-term, gains are subject to 0%, 15% or 20% rates. The U.S. capital gains tax rates rank 6th highest among OECD countries (Ernst & Young, 2015). Japan and Germany also tax capital gains based on whether they are short- or long-term, but do so at lower, flat rates. In Japan short-term gains are those acquired within 5 years, and in Germany those acquired within 10 years (after which point they are untaxed). Sweden taxes all capital gains at 30%.

Piketty has suggested that a global wealth tax might remedy the problem of growing inequality. Of these five countries, only Sweden and Germany have implemented taxes on wealth, and none currently have one in place (see Table 3). Germany abolished its wealth tax in 1997, and Sweden abolished its own in 2007. The modern wealth tax was established in Sweden in 1911 with the aim, among others, to redistribute wealth (Henrekson & Du Rietz, 2014). However, over the decades it was in effect, wealth tax revenue remained low and capital outflow increased, indicating that many were able to evade the tax with impunity (Henrekson & Du Rietz, 2014). Before its abolition, Sweden's wealth tax rate was 1.5% on wealth totaling more than 1.5 or 3 million SEK (depending on whether taxpayers filed individually or jointly). In Germany the government repealed the wealth tax based on a Constitutional ruling focused on distorted valuation methods. Prior to this repeal, German wealth totaling more than 1 million DEM had been taxed at 1.0%.

Estate, or inheritance, tax rates vary widely among these countries as shown in Table 4. The U.S. rather heavily taxes inheritance, initially at a rate of 18% and at a top rate of 55%. Germany and Japan have lower initial rates (7 and 10%, respectively) and top rates (30 and 50%, respectively) than the U.S. Both Germany and Japan rely on a unified inheritance and gift tax, which is imposed on any transfer of property at death or by gift. Finally, China and Sweden do not tax inheritance at all. Sweden abolished its inheritance and gift tax in 2004, and Macau and Hong Kong did so in 2001 and 2006, respectively, bringing them in line with mainland China.

The last factors we consider are charitable limits and tax benefits (see Table 5). The limit on deductions for charitable donations is highest in the U.S., at 50%--meaning that a deduction for charitable contributions can be up to 50% of one's taxable income. This relatively high cap is followed by Japan (40%) and China (30%). Germany and Sweden limit charitable deductions at respectively 20% and 25% of taxable income. Although these rates are much lower, the top tax benefit rates are highest in Germany and Sweden. The value of tax expenditures as a percentage of deductions is less valuable in lower tax brackets; in this sense, tax benefits for charitable donations are ultimately regressive.

Discussion

Before discussing the broader policies targeting economic inequality, it is important to recognize the responses of those who suffer its worst consequences. In both China and the U.S. there is significant public outcry against perceived and experienced inequality—with regard to education, employment, and numerous other spheres. Over the course of each nation's history, instances of "rightful resistance" by the economically disadvantaged have shaped policy creation and implementation, as well as policy revision and abolition (O'Brien & Li, 2006). The income tax system in the U.S. is not as progressive as that in Sweden, Japan, Germany or China (Table 1), and the relatively progressive Chinese income tax system is offset by highly regressive value-added and consumption taxes. If tax reforms and the philanthropic sector are to meaningfully impact economic inequality in either country, they will need to account for the needs and goals of the public.

In China the emergence of a largely market-based economy has given rise to the privileges and perils of capitalism, including tycoons, labor exploitation, and company bankruptcy (Whyte, 2010). As previously noted, China does not tax capital gains or levy any type of estate tax (Tables 2, 4). Outcry over unfair taxation practices and their role in promoting inequality has led to significant social unrest and political instability (Liu & Tao, 2007). Rising inequality has also led to fermenting resentment and increasingly strong reactions to "moral shocks"—highly scrutinized events that raise the public's sense of outrage (Cai, 2010). Moral shocks pertaining to economic inequality, and related abuses of power, have triggered riots involving tens of thousands of participants. There is little sign of these incidents disappearing in the near future (Cai, 2010).

For this reason, to achieve the "harmonious society" it wishes to, China must develop greater legitimacy around its efforts to tame inequality. At the same time, it is questionable whether rising inequality is propelling the Chinese people toward "a social volcano" of instability, which was the subject of widespread academic and political speculation for years (Whyte, 2010). Whyte found that Chinese people tend to place faith in the future and are generally less angry than others about current inequality patterns. In fact, the modern Chinese economy is rooted in the ideas and policies of Deng Xiaoping, who in 1983 stated, "Some people in rural areas and cities should be allowed to get rich before others" (Deng, 1987). Perhaps it is the perpetuation of this attitude that has resulted in China's continued lack of any capital gains or estate taxation (Tables 2, 4) and continued reliance on highly regressive indirect taxation (Xu & Yue, 2013).

In the United States, public disapproval of growing economic inequality culminated in the 2011 Occupy Wall Street movement. Prior to this, policymakers and journalists had infrequently made reference to the issue of economic inequality, except a brief focus on exorbitant CEO compensation (Kenworthy & Smeeding, 2013). According to polls, American public opinion regarding economic inequality remained stable over the last two decades: between 57% and 66% of Americans desired more equitable wealth distribution, while 28-35% expressed satisfaction with the status quo. While specific events have triggered slightly different responses (most notably the recent recession), overall there have been no significant shifts in this public stance on inequality or its political remedies (Shaw & Gaffey, 2012). Even if attitudes did shift, however, it is questionable whether poor or middle-class Americans' views would meaningfully effect change at the policy level. Gilens (2005) showed that when Americans at different income levels held disparate policy preferences, outcomes only reflected the preferences of the most affluent.

Taxation

Compared to most developed countries, the U.S. spends a relatively small share of its GDP on public social welfare programs; most of its spending on social programs consists of private expenditures on pensions and health insurance, and has very limited redistributive effects (Garfinkel, Rainwater, & Smeeding, 2010). Likewise, the Chinese welfare system features decreasing subsidies and limited government transfers alongside increasing social insurance expenditures (Gao & Riskin, 2006; Lu, Lin, Vikse, & Huang, 2013). As social welfare programs have had limited impact on curbing inequality in each country, then, we shift our attention to two alternative mechanisms: taxation and philanthropy.

As Saez & Zucman (2014) point out, it is difficult to justify the preferential tax rates on capital income that exist in many countries, given the steady rise of wealth inequality and high savings rates among those nations' wealthiest individuals and corporations. In the U.S., long-term capital gains are taxed at rates between 0-20%, compared to a significantly higher 39.6% tax rate for the highest income level (Tables 1, 2). As wealth inequality continues to increase, so does the growing indebtedness of low income and middle class Americans—owed to higher mortgages, consumer credit and student loans (Saez & Zucman, 2014). The result is that the top 0.1% wealth share in the U.S. has risen to the highest levels since the Roaring Twenties, while low- and middle-class wealth has steadily eroded (Saez &

Zucman, 2014). Although the middle-class share of wealth rose significantly during the twenty-first century, it has dramatically declined since the mid-1980s (Saez & Zucman, 2014).

Although the federal tax system in the U.S. is progressive, and as previously shown a viable tool to reduce inequality, its redistributive power has changed over time (Burman, 2014). After the Great Depression, progressive estate taxes and income taxes were implemented in order to reduce the concentration of wealth (Piketty & Saez, 2003; Kopxzuk & Saez, 2004). In the wake of Reagan's 1981 income tax reforms, which greatly lowered the top marginal tax rate, the ability of federal taxes to redistribute wealth was meaningfully hampered (Kenworthy & Smeeding, 2013). As shown previously, this top U.S. marginal tax rate (39.6%) is significantly lower than that of Sweden (58%), Germany and China (45%), and Japan (40%). Also beginning in the 1980s, financial deregulation occurred steadily, which led to a sharp rise in pay for financial traders and analysts (Kenworthy & Smeeding, 2013). In 1997 President Clinton enacted a cut in taxes on capital gains, which further undermined the progressivity of the tax system (Burman, 2014).

While the U.S. has seen an expansion of tax credit programs for low- and middle-income families, such as EITC and the child tax credit, the benefits have been limited, particularly following the comprehensive program of tax cuts in 2001 (Burman, 2014). Overall, U.S. policymakers in recent decades have done little to address or ameliorate the tremendous wealth gap through targeted tax policies (Kenworthy & Smeeding, 2013). According to estimates by the Congressional Budget Office (CBO), the U.S. Gini coefficient was not significantly impacted by tax or transfer policies between 1979-2007 (Congressional Budget Office, 2010), and as previously mentioned the level of wealth inequality in the U.S. is now roughly equivalent to that precipitating the Great Depression.

In China, rising incomes and a higher fraction of wage earners in the labor force have made the income tax a more progressive tool for remedying inequality (Piketty & Qian, 2009). Personal income taxes in China were put into place between the early 1980s and mid-1990s, but during this period taxpayers were limited (Shi, Sato & Sicular, 2013). In 1994 China reformed its tax system, most notably by making indirect taxes—including the value added tax (VAT), business tax, and consumption tax—a dominant share of collected tax revenue (Xu & Yue, 2013). While progressive income and corporate income taxes offset some of the regressivity of its indirect taxation, China's predominant reliance on this latter form makes its system regressive overall (Xu & Yue, 2013). Since the mid-2000s adjustments to personal income tax exemptions have aimed to alleviate income inequality (Shi, Sato & Sicular, 2013). The Chinese income tax system remains highly progressive; its bottom rate (3%) is much lower than that of Japan (5%), the U.S. and Sweden (10%), and Germany (14-24%), and its top rate (45%) is higher than that of the U.S. (39.6%) and Japan (40%), and equivalent to that of Germany (Table 1). In addition, China's corporate income tax has grown as a share of overall tax revenue in recent years (Xu & Yue, 2013). Additionally, rural tax and fee reforms were implemented in 2000 to substitute formal taxation for regressive local levies and gradually eliminate agricultural taxes (Shi, Sato & Sicular, 2013). However, China has struggled to set an effective tax rate scale and further reforms are the subject of ongoing policy discussion (Shi, Sato & Sicular, 2013).

Additionally, the redistributive power of taxation is geographically dependent in China; higher levels of industrialization in coastal and urbanized regions have contributed to much lower levels of taxation (Liu & Tao, 2007). One of the key barriers to implementing rural tax reforms in particular is local governments' reliance on higher-level government transfers, which hampers the effective provision of public goods and services and undermines tax competition (Liu & Tao, 2007). Another unique challenge to reforming taxation in China is the decentralization of its fiscal system, compared to a rather centralized governance structure. This leads to widening regional gaps, as agricultural regions burdened by bureaucratic expenses have limited funds for public investment (Zhang, 2006).

Two of the most common objections to enacting more progressive taxation, including on capital gains, are that it produces costly behavioral responses (e.g. deterring work, saving, or investing), and that it is ineffective because of tax avoidance mechanisms and loopholes. In response to the first claim, Thomas Hungerford (2013) analyzed the effects of past tax policies, came to the opposite conclusion: he found that lowering marginal tax rates and capital gains tax rates had not significantly impacted economic growth, savings, investment, or productivity, but rather had been associated with an increasing concentration of wealth in the top income brackets. Likewise, Mirrlees et al. (2011) found that raising tax rates on the wealthiest individuals led to very small average behavioral responses.

With regard to the second objection, it is true that tax policy reforms to combat inequality are notoriously difficult to implement without unforeseen consequences. In 1993, the Clinton administration capped the amount of executive compensation that was tax deductible at $1 million, with the exception of "performance-based" income. In response, corporate accountants found ways to circumvent this policy by reclassifying income, and firms accelerated their shift toward compensating executives through stock options (Kenworthy & Smeeding, 2013). There are many ways to skirt tax liability, and complex tax shelter arrangements can entail significant economic costs (Burman, 2014). For this reason, eliminating tax loopholes, in particular the lower tax rate on capital gains, are essential to effectively reducing wealth inequality (Burman, 2014). In China, serious problems have resulted from local levies and taxation practices, which are rife with cronyism and corruption (Shue & Wong, 2007).

While progressive income taxation has proven effective in limiting inequality, to some degree at least, other forms of taxation should also be explored. Piketty's suggestion of a global tax on wealth has been hotly debated. Wealth taxes have been implemented in a number of countries to date. Switzerland, the Netherlands, and Norway, for instance, still tax wealth (Glennerster, 2012), while Germany and Sweden have discontinued wealth tax policies (Table 3). Supporters point to the increasing concentration of wealth worldwide, and argue that wealth taxation can generate significant revenue, reinforce the productive use of assets (Shakow & Shuldiner, 2000), and promote social mobility (Council of Europe, 2013). On the other hand, those who have chosen to abolish taxes on wealth have cited several reasons for doing so. In some cases wealth taxation led to capital outflow, as wealthy individuals and corporations developed tax avoidance mechanisms and chose to invest abroad—which meant that governments lost revenue from taxes not only on wealth, but also on capital gains, dividends and interest (Henrekson & Du Rietz, 2014). In Germany the complexity of wealth taxation required an influx of bureaucratic infrastructure, which was expensive and difficult to implement and maintain, and arguments were made against double taxation (Heckly, 2004). A number of the countries that initially tried to implement taxes on wealth ultimately turned to inheritance taxation instead.

Inheritance, or estate, taxes have served an important function in reducing inequality, but can also have limited impacts, and at times negative impacts, in some circumstances. For instance, research shows that while estate taxes do not have significant negative impacts on the saving and investment decisions of individuals and small businesses, they do affect the decisions of larger firms (Cagetti & De Nardi, 2009). According to Yunker (2010), however, while estate taxation can slow the rise of capital wealth inequality, it is ineffective at reducing wealth inequality once it has reached a high level. In terms of its mixed public support, one study showed that when Americans were informed of how few families are affected by the estate tax, and how wealthy those families were, support dramatically increased (Kuziemko et al., In Press). The U.S. estate tax rates (18-55%) are relatively high, compared to those in Japan (7-30%) and Germany (10-50%), and China and Sweden do not tax inheritance at all.

Philanthropy

Philanthropy is another possible remedy for the vast wealth inequality worldwide, and this paper focuses on its development and impacts toward that end in China and the U.S. Overall, Americans engage in more charitable giving than any other nation, and its wealthy are the most generous of their peers worldwide (Charities Aid Foundation, 2006; Giving USA, 2015). In 2014 charitable giving amounted to over 358 billion dollars in the U.S.: 72% came from individuals, compared to 15% from foundations, 8% from bequests, and 5% from corporations (Giving USA, 2015). In China, the charitable sector has grown significantly. Some have suggested that its rise and expansion was largely in response to the vast wealth inequalities between rural regions and rapidly developing urban centers (Lee, 2009). Others point to government attitudes, economic development, Charity laws and regulations, and substantial national disasters throughout the years (Deng, 2014). For example, in 2008 Sichuan earthquake brought the role of the charitable sector to the forefront, particularly in cases when local governments were unable to effectively handle crises and their aftermath (Lee, 2009; Deng, 2014). The Sichuan earthquake also energized a previously fragmented civil society by providing a public stage for nonprofits to demonstrate their worth (Shieh & Deng, 2011).

Several years earlier President Hu Jintao had proposed that China develop a "harmonious society," focused on redressing economic, social and geographic inequalities (Chodorow, 2012). An important aspect of this concept was the idea that civil society could play a key role in reducing inequalities, perceived to be the root of social conflict. As Dong (2012) argues, fostering the development and growing the capacity of the charitable sector may be a key step toward alleviating poverty, redistributing capital wealth, and subsequently reducing wealth inequality in China. The government has continued to call for reductions of inequality, but as previously shown, has avoided imposing higher levels of progressive taxation in the interest of economic growth. Compared with the U.S., which limits deductions for charitable donations at 50%, China caps deductions at 30% and offers tax benefit rates that are no higher than its income taxation levels (Table 5). While philanthropy has been highlighted as an alternative solution to the same outcome, it is still unclear to what extent the charitable sector can effect redistribution and impact wealth disparities in China (Chodorow, 2012).

Its reach and impact has vacillated alongside changing policies over the last several decades. In 1999 the central government issued the Public Welfare Donation Law, which loosened its control over which organizations were eligible for tax-free charitable donations. Again in 2007, the government reformed charitable giving regulations by allowing public welfare groups to receive tax-deductible donations, and expanding allowable deductions from 3% to 12%. Now, while the government continues to control which organizations are eligible for receiving charitable donations, the pool has expanded significantly to include public institutions, foundations, civil "non-business units" (Chodorow, 2012). As of January 2015, a draft of the new "Charity Law" apparently includes structure and guidance for obtaining charity certification and tax status, and expands the definition of charity to include most activities in the public's interest.

However, there are also limitations and questions surrounding philanthropy in China. The legal framework surrounding charitable organizations is still insufficient: it consists of disparate laws that fail to facilitate growth of the sector, in large part because it allows for the continuation of inefficient, bureaucratic modes of governance (Lee, 2009). There is also no history of donative-style charity, and cultural practices of giving to the needy during the premodern and Maoist eras still influence the public's vision of charity (Hsu, 2008). The relationship between philanthropy and government has a tense history—whether owed to, or reflected in, the tight restrictions and complex registration processes that were previously discussed. This dominating role of government in managing the charity sector is notably divergent from the modern charity paradigm (Lee, 2009). As argued by He and Meng (2011), it is important for the government to play more of a catalytic role in philanthropic and nonprofit capacity building in order to expand its reach and impact.

Conclusion

Despite the objections, limitations, and unintended consequences described above, under the current systems in China and the U.S. taxation and philanthropy can certainly be used as tools to reduce inequality. Progressive taxation, elimination of tax loopholes, and increasing tax rates on capital gains reduce inequality. Vast sums of money are donated for the benefit of the most vulnerable, and as the philanthropic sector grows—particularly in China—its impact may vastly increase. While this paper does not explore other factors in depth, it is also important to note that inequality hinges on reforms in other spheres as well: education policy, labor policy (in China particularly, labor migration policies), and policies determining the structure and direction of industrial development (Gustafsson, Shi & Sicular, 2008). Finally, as suggested by Saez and Zucman (2014), better data collection on wealth—particularly 401(k) and bank account balances—should be a priority, in order to inform policymaking and shed light on the extent of economic inequality.

Table 1: Income Tax by Countries

Income tax					
	China	**US**	**Japan**	**Germany**	**Sweden**
Tax Bracket	Marginal Tax Rate				
1	3	10	5	14 - 24	10
2	10	15	10	24 - 42	22
3	20	25	20	42	30
4	25	28	23	45	33
5	30	33	33		53
6	35	35	40		58
7	45	39.6			

* All rates are based on 2014.
* China's tax rate is focus on the wage income while others apply to all incomes.
* All the countries have different tax deductions and exemptions.
* Japan and Germany have extra tax after income tax.

Table 2: Capital Gain Tax by Countries

<table>
<tr><th></th><th>China</th><th>US</th><th>Japan</th><th>Germany</th><th>Sweden</th></tr>
<tr><td>Time Range</td><td colspan="5">Tax Rate</td></tr>
<tr><td rowspan="7">Short Term</td><td rowspan="10">0% for stocks, 20% for interests</td><td>10%</td><td rowspan="7">30%</td><td rowspan="7">25%</td><td rowspan="10">30%</td></tr>
<tr><td>15%</td></tr>
<tr><td>25%</td></tr>
<tr><td>28%</td></tr>
<tr><td>33%</td></tr>
<tr><td>35%</td></tr>
<tr><td>39.60%</td></tr>
<tr><td rowspan="3">Long Term</td><td>0%</td><td rowspan="3">15%</td><td rowspan="3">0%</td></tr>
<tr><td>15%</td></tr>
<tr><td>20%</td></tr>
</table>

* This table applies to 2014 year.

Table 3: Wealth Tax by Countries

Wealth Tax	Sweden	Germany	Japan/US/China
Exemption	1.5 or 3million SEK	1 million Mark	N/A
Rate	1.50%	1.00%	

6.845 SEK = 1 USD on Jan 01 2007. 1 USD = 1.74 Mark on average 1997.

* Single persons and persons with joint taxation have different wealth tax liability thresholds.
* Sweden abolished its wealth tax in 2007.
* Germany suspended its wealth tax in 1997, and increased its inheritance/gift and real estate transfer taxes.

Table 4: Estate Tax/Inheritance Tax Exemptions and Rates in 2013[1]

Country	US[2]	China[3]	Germany[4]	Japan[5]	Sweden[7]
Estate/Inheritance Tax Exemption	$5,250,000	¥0	€ 541,000	¥50,000,000	€ 0
Initial Rate	18%	0%	7%	10%	0%
Top Rate	55%	0%	30%	50%	0%

[1]USD$1=Chinese Yuan (RMB)$6.203 =Euro 0.731 = Japanese Yen 101.514 on July 1, 2014.
[2]The United States' federal estate tax applies to property owned at the time of death. Several states collect inheritance tax from the beneficiaries who receive property or money from the estate of the deceased.
[3]China does not levy an estate/inheritance tax.
[4]Germany has a unified inheritance and gift tax. The tax is imposed on any transfer of property at death or by gift, depending on the tax class of the beneficiary. The data in the table shows the tax imposed on spouses and on registered same-sex partners under German law.
[5]Japan has a unified inheritance and gift tax. The basic exemption is ¥50 million plus ¥10 million multiplied by the number of beneficiaries.
[7]Sweden repealed its unified inheritance and gift tax law in 2004.

Table 5: Deduction of Charitable Donations by Countries

	US	China	Japan	Germany	Sweden
Limits on Charitable Deductions	50%	30%	40%	20%	25%
Tax Benefits for Cash Donated by Tax Bracket					
1	10%	3%	5%	14%-24%	10%
2	15%	10%	10%	24%-42%	22%
3	25%	20%	20%	42%	30%
4	28%	25%	23%	45%	33%
5	33%	30%	33%		53%
6	35%	35%	40%		58%
7	39.60%	45%			

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