

Chapter 3: Wealth Is Not Money

"The confusion of money with wealth... is perhaps the oldest and most persistent of economic fallacies."

— **Henry Hazlitt**, *The Failure of the "New Economics"* (1959)

The modern policy debate has learned a small trick that saves it from the strain of understanding finance: it uses the word *wealth* as a synonym for *cash*. Then it performs arithmetic on that imagined cash. Then it announces moral victory.

This is not analysis. It is theatre with numbers.

"Wealth," in the sense that matters for taxes and politics, is largely a claim on productive assets: companies, property, shares, ventures, patents, and control blocks. It is often illiquid, unevenly priced, and measured at the margin. It can make a person "worth" ten billion in headlines while leaving them with far less in spendable money. It can also vanish—partly or entirely—if the assumptions behind the valuation shift, if market sentiment turns, or if forced selling begins.

To treat that wealth as if it were a vault of banknotes is to confuse a balance sheet with a purse. And that confusion does not merely produce bad rhetoric. It produces coercive policy—because the state, having promised revenue in cash, must extract it in cash, and the asset does not oblige.

This chapter is a guide to the gap between political arithmetic and economic reality.

The Governing Claim

Treating "wealth" as spendable cash turns policy into arithmetic theatre and administration into coercion. It invites tax promises that require forced liquidity, intrusive valuation, and the punishment of investment rather than indulgence.

To see why, we must define a handful of plain concepts that are constantly smuggled past the reader.

Wealth, Liquidity, and Cash Flow: Three Different Animals

A person can be rich and cash-poor. A person can have a high income and little wealth. A person can have wealth that is entirely trapped inside a business that cannot be sold without destroying it.

Policy debates often flatten all of this into a single caricature: a wealthy person as a dragon on a pile of coins. It is a childish image, but it has an adult function. It makes confiscation feel tidy.

Asset wealth

Asset wealth is the estimated market value of what you own, net of what you owe. It is not a pile of money. It is a portfolio of claims. Many of those claims cannot be converted into money without cost, delay, or consequences.

Liquidity

Liquidity is the ability to turn an asset into spendable cash quickly, in size, without collapsing the price. A publicly traded share is more liquid than a privately held company stake. A house is less liquid than a share. A controlling stake in a company may be “valuable” but hard to liquidate without sacrificing control—often the very thing that made it valuable.

Cash flow

Cash flow is the stream of money the asset generates: dividends, rent, business earnings, distributions. A person can have enormous wealth in an asset that generates little cash flow, because the asset’s value is expected future growth rather than present income.

The political mind looks at a valuation and assumes it can be skimmed annually like income. But valuations are often the price of future expectations. Taxing expectations as if they were income is not redistribution; it is a demand that tomorrow pay today’s promises.

Price-at-the-Margin: Why Headlines Are Fragile

Markets do not value entire fortunes as a single block. They value marginal trades: the next buyer and seller determine the price. This matters because it means the headline valuation of a large holding is not a reservoir of cash. It is a number derived from small trades.

If a founder owns 40% of a company and the share price implies a net worth of \$10 billion, that does not mean they can sell \$200 million of stock each year without moving the price. Large, repeated, price-insensitive selling is not a neutral act. It changes the market.

Forced selling is not merely a payment method. It is a distortion.

A policy that relies on steady annual liquidation of large holdings is, in effect, a permanent sell programme imposed by law. It may be dressed as fairness. But the market experiences it as pressure. That pressure increases volatility, widens spreads, and can depress valuations—especially in companies where the taxable wealth is concentrated.

The political story says “we’re taking from billionaires.” The economic reality says “we’re repricing capital.”

And capital, inconveniently, is where everyone’s future sits: pensions, retirement accounts, endowments, insurance portfolios, and the savings of ordinary people.

"It is the aim of good government to stimulate production, of bad government to encourage consumption." — Jean-Baptiste Say, A Treatise on Political Economy (1803)

Control Blocks: When Selling Destroys the Thing Being Taxed

Many large fortunes exist as control blocks—stakes that confer voting control, strategic direction, and the ability to hire or fire management. The value of control is not the same as the value of a small shareholder’s stake. It often includes a premium, because control allows decisions that affect the company’s future.

But control is fragile. Sell enough, and you lose it.

A tax that forces annual sales of a control block is not merely a tax on “wealth.” It is a forced dilution of ownership and influence. That may be exactly what some advocates want. But then it should be said honestly: the policy is not simply raising revenue; it is restructuring corporate governance by compulsion.

The moment policy begins to treat control as a taxable reservoir, it turns taxation into industrial policy.

Valuation: The Quiet Hell Beneath the Slogan

A wealth tax looks simple only if you assume all assets have clean market prices. Most do not.

Privately held companies do not trade daily. Venture stakes do not have transparent markets. Intellectual property is notoriously hard to price. Real estate values can be contested. Art, collectibles, and complex partnership structures exist precisely because they evade simple valuation.

An annual wealth tax therefore requires either:

1. **Mark-to-market** valuation where a market does not exist, or
2. **Appraisal regimes** that become contentious, intrusive, expensive, and politically gamed.

Either way, administration becomes a struggle. The state needs revenue. The taxpayer has incentives to contest valuations. An entire industry emerges to argue about what is “really” worth what. Compliance costs balloon. Enforcement becomes more aggressive. And because the tax is annual, the fight is permanent.

The slogan promised simplicity. The reality delivers bureaucracy.

Why This Matters Morally

The moral case for treating wealth as money is always stated as compassion. But the effects tend to be institutional.

A society that begins to tax illiquid, hard-to-measure assets annually is a society that must either accept poor compliance and lower revenue than promised, or escalate coercion to force liquidity and enforce valuations. It will demand disclosures, audits, appraisals, reporting regimes, and penalties that expand state discretion. That discretion does not remain politely targeted. It spreads. It becomes a tool of politics.

The price of “simple fairness” becomes a state with more surveillance capacity and more control over private economic life.

That is the real trade: not merely rich versus poor, but freedom versus administrative compulsion.

Primary Example (13): The Wealth Tax

Claim: “A small annual wealth tax raises large revenue without affecting how the wealthy live, because it taxes idle hoards.”

Hidden assumption: Wealth is liquid, easily valued, and convertible to cash without affecting prices or governance.

Behavioural response: Taxpayers sell assets, borrow against them, restructure holdings, shift residence, move assets into vehicles designed to reduce taxable base, and litigate valuations.

Second effects: Persistent sell pressure and repricing of concentrated equities; higher volatility and wider spreads; growth of avoidance and appraisal industries; diversion of talent

and time from production to defence; increased political risk premium on investment.

Who pays: Not only high-wealth taxpayers, but savers through repriced capital, workers through reduced investment, and the public through administrative bloat and weaker long-run growth.

Better test: If revenue requires annual forced liquidity from illiquid assets, the policy taxes capital formation.

A wealth tax is often defended with the claim that it does not change behaviour because the rich “will still be rich.” This is a clever evasion. Behaviour does not need to change at the level of lifestyle to change at the level that matters: investment, risk-taking, ownership structure, and location of activity.

The policy is not merely about who owns yachts. It is about where capital is priced and deployed.

And because capital pricing governs productivity, the poor—whom the policy is meant to help—can end up paying through slower wage growth and fewer opportunities.

Capital Gains: The Mirage of “Just Tax It When They Sell”

When wealth taxes become administratively ugly, the debate often shifts to capital gains taxation. Here the confusion takes a different form. Capital gains are treated as “income” that can be tapped whenever needed. But capital gains have a notorious behavioural response: **lock-in**.

If you tax realised gains heavily, people delay realising them. They hold assets longer than they otherwise would. This is not because they are morally defective. It is because selling triggers the tax.¹²

Lock-in has several consequences. It reduces market liquidity. It discourages reallocation of capital from lower-productivity uses to higher-productivity ones. It can trap capital in legacy firms and slow the diffusion of innovation.

In other words: a tax designed to harvest “wealth” can also preserve stagnation.

Primary Example (15): Capital gains lock-in

¹² **Dai et al. (2008)**, “Capital Gains Taxes and Asset Prices: Capitalization or Lock-in?” *Journal of Finance*. This study confirmed the “lock-in” effect empirically, showing that higher capital gains taxes reduce selling pressure, reduce trading volume, and distort asset prices by preventing reallocation to higher-value uses.

Claim: “Tax capital gains more; it targets unearned windfalls and does not harm the real economy.”

Hidden assumption: Investors will sell and reallocate capital normally regardless of tax on realisation.

Behavioural response: Investors defer sales, favour borrowing against appreciated assets rather than selling, and seek structures to avoid realisation.

Second effects: Lower liquidity and slower capital reallocation; increased leverage as borrowing replaces selling; preservation of inefficient holdings; reduced entrepreneurial recycling of capital into new ventures.

Who pays: The broader economy through slower dynamism; future workers through slower productivity growth; the public through lower-than-expected revenue as realisations decline.

Better test: If a tax discourages reallocation, it can freeze capital where it is rather than where it would be most productive.

A society obsessed with “taxing gains” can accidentally create a world where capital stays put, not because it is wise to stay, but because moving triggers a penalty. The economy becomes less a river and more a reservoir.

Transaction Taxes: The Seduction of “A Tiny Fee on Everything”

Transaction taxes are the policy equivalent of glitter: a little bit sprinkled everywhere looks harmless. A tiny tax on every trade, every transfer, every transaction—what could it hurt?

It hurts the very function that trading performs: liquidity and price discovery. A small tax becomes a large wedge when applied repeatedly. It discourages rebalancing. It reduces the number of trades. It widens spreads. It raises the cost of capital by making markets less liquid and more volatile.¹³

The political story says it targets “speculators.” The economic reality is that it taxes the plumbing.

Primary Example (16): Transaction taxes

Claim: “A tiny tax on transactions raises revenue and discourages useless speculation without affecting real investment.”

Hidden assumption: Market trading is mostly noise, and reduced trading does not affect

¹³ Colliard & Hoffmann (2017), “Financial Transaction Taxes, Market Composition, and Liquidity,” *Journal of Finance*. Analyzed the French financial transaction tax (introduced in 2012). It found that while market share of high-frequency trading fell, market quality deteriorated significantly: liquidity dropped, and the cost of capital for firms rose.

liquidity or capital costs.

Behavioural response: Traders reduce activity, shift trading to untaxed venues, widen spreads to cover the tax, and reduce market-making.

Second effects: Lower liquidity; higher volatility; higher cost of capital; reduced efficiency of price discovery; reduced retirement returns through higher friction and weaker market performance.

Who pays: Savers and investors through worse execution and lower returns; firms through higher capital costs; the public through reduced competitiveness of domestic markets.

Better test: If a tax damages liquidity, it taxes investment indirectly by making financing more expensive.

Transaction taxes are rarely marketed honestly. They are sold as moral hygiene. But markets are not a moral essay; they are a coordination mechanism. Damage the mechanism and you do not punish vice; you reduce the economy's ability to allocate capital efficiently.

Inheritance Taxes: The Mirage of "Taxing the Dead"

Inheritance taxes are defended with a pleasing theatrical line: "The dead do not need the money." But inheritance is not about the dead. It is about the living—the heirs, the businesses, the farms, the family enterprises, and the intergenerational transfer of capital.

If inheritance taxes are low and simple, they function as a limited levy on transfer. If they are high, complex, and aggressively enforced, they can force liquidation of family assets to pay cash taxes—again, because the tax is due in cash.¹⁴

The same confusion returns: wealth is treated as money.

Primary Example (18): Inheritance taxes

Claim: "Tax inheritances heavily; it reduces inequality and targets unearned wealth without affecting the productive economy."

Hidden assumption: Inherited wealth is liquid, and paying the tax does not alter ownership or destroy productive assets.

Behavioural response: Families restructure assets, spend resources on avoidance, and in some cases liquidate businesses or sell property to raise cash.

Second effects: Forced sales of family enterprises; loss of continuity and long-term

¹⁴ Tsoutsoura (2015), "The Effect of Succession Taxes on Family Firm Investment: Evidence from a Natural Experiment," *Journal of Finance*. Used a reform in Greece to show that higher inheritance taxes led to a significant drop in investment and slower sales growth for family firms, as cash was diverted to pay the tax rather than reinvested.

stewardship; increased avoidance industry; potential shift toward consumption during life to reduce taxable estate.

Who pays: Heirs and family enterprises; local communities where such businesses operate; the public through reduced investment and increased compliance costs.

Better test: If a tax forces liquidation of productive assets, it taxes continuity and investment, not merely inheritance.

Inheritance taxes also have a cultural dimension. If intergenerational transfer is treated as morally suspect, families respond not only financially but psychologically: they invest less in long-term projects, and they convert capital into forms more easily hidden or consumed. A society that tells its builders that continuity will be penalised should not be surprised when fewer people build.

The Common Failure: Converting Portfolios into Cash by Force

All four examples share the same structure. They treat asset wealth as if it were a cash pile.

- Wealth taxes require annual liquidity from illiquid assets.
- Capital gains taxes can freeze reallocations and encourage leverage.
- Transaction taxes damage liquidity and raise capital costs.
- Inheritance taxes can force liquidation of productive assets.

Each of these can be designed moderately. None of these is necessarily always wrong. The point is not doctrinal purity. The point is that the *arithmetic* commonly used to sell them is fraudulent because it omits how wealth is structured and how people respond.

The public is told, “It is only two percent.” But “two percent” is not a moral incantation. It is a recurring claim that must be serviced in cash. If the asset does not yield cash, the owner must create cash by selling or borrowing. Borrowing adds leverage and interest burdens. Selling creates price pressure and can destroy control. Both have consequences.

This is why the rhetoric of painless extraction so often ends in coercion. The state has promised outcomes based on paper valuations. To deliver those outcomes, it must compel the conversion of paper value into cash on demand. That is not gentle policy. That is forced liquidity.

Plain-language wealth-tax critique: what the slogan misses

If the public is told “a wealth tax will not change how billionaires live,” the correct response is: it does not need to change their lifestyle to change the economy. The question is what it changes in capital pricing, in investment behaviour, in ownership structure, and in institutional trust.

If the public is told “it is only a small percentage,” the correct response is: a small annual percentage is not small when the base is illiquid and must be appraised and serviced in cash. It becomes a permanent liquidation mandate, not a one-time levy.

If the public is told “they can just sell a little stock,” the correct response is: repeated selling is not neutral. It changes prices at the margin. It can depress valuations. And it pushes costs onto other holders of capital, including ordinary savers.

If the public is told “we can value everything fairly,” the correct response is: valuation is the battlefield. The harder the asset is to price, the more contentious and coercive the system becomes. The state must either accept erosion of the base or build an intrusive enforcement apparatus. There is no painless third option.¹⁵

"Show me the incentive and I will show you the outcome." — Charlie Munger

A politics that refuses to understand these points is not merely wrong. It is dangerous, because it turns taxation into a permanent contest over valuation and liquidity—an administrative struggle that expands discretion and shrinks trust.

The deeper point: investment is the future's wage packet

Most people are not capitalists in the theatrical sense. They are capitalists in the quiet, institutional sense: they have pensions, retirement accounts, insurance policies, or hopes that depend on firms investing in productivity. Investment is how wages rise over time. It is how productivity increases. It is how the floor lifts.

A policy regime that repeatedly taxes the conditions of investment—liquidity, valuation certainty, expected returns—does not strike indulgence. It strikes the future.

¹⁵ **Jakobsen et al. (2020)**, "Wealth Taxation and Wealth Accumulation: Theory and Evidence from Denmark," *Quarterly Journal of Economics*. This paper uses high-quality administrative data to show that wealth taxes significantly reduce wealth accumulation. Even a 1% tax reduced wealth by over 20% in the long run due to behavioral responses and compound effects.

This is why the rhetoric of “eat the rich” is not merely vulgar. It is analytically lazy. It confuses moral emotion with economic mechanics. It treats capital as a static hoard rather than as a process that funds production.

If you want to improve life for ordinary people, you do not begin by making capital formation more expensive, more uncertain, and more politically negotiable. You begin by opening ladders: lowering barriers to building, reducing regulatory capture, enforcing contracts, stabilising money, and ensuring entry and competition.

The Lesson Line

When you tax what is hard to measure and harder to sell, you end up taxing investment, not indulgence.

Chapter 3 Notes

[1] Wealth Tax: Capital Flight & Accumulation Jakobsen et al., "Wealth Taxation and Wealth Accumulation: Theory and Evidence from Denmark," *Quarterly Journal of Economics* (2020). Using high-quality administrative data, this study showed that wealth taxes significantly reduce wealth accumulation—even a 1% tax reduced wealth by over 20% in the long run due to behavioral responses and compound effects.¹⁶

[2] Capital Gains: The Lock-In Effect Dai et al., "Capital Gains Taxes and Asset Prices: Capitalization or Lock-in?" *Journal of Finance* (2008). Empirically confirmed the "lock-in" effect, demonstrating that higher capital gains taxes reduce selling pressure and trading volume, distorting asset prices by preventing reallocation.

[3] Transaction Taxes: Market Quality & Cost of Capital Colliard & Hoffmann, "Financial Transaction Taxes, Market Composition, and Liquidity," *Journal of Finance* (2017). Analyzed the French financial transaction tax (2012) and found that while it reduced high-frequency trading, it significantly deteriorated market quality—liquidity dropped, and the cost of capital for firms rose.

[4] Inheritance Taxes: Investment & Sales Growth Tsoutsoura, "The Effect of Succession Taxes on Family Firm Investment: Evidence from a Natural Experiment," *Journal of Finance* (2015). Examined a tax reform in Greece, finding that higher inheritance taxes led to a significant drop in investment and slower sales growth for family firms, as cash was diverted from the business to pay the tax liability.

¹⁶ **Kleven et al. (2013)**, "Taxation and Migration of Superstars," *American Economic Review*. Showed that high-income "superstars" (e.g., footballers, inventors) are highly responsive to tax rates and will migrate to lower-tax jurisdictions, shrinking the tax base and shifting the burden to less mobile residents.

Governing Claim Treating "wealth" (illiquid assets) as spendable cash turns policy into arithmetic theatre and administration into coercion; when you tax what is hard to measure and harder to sell, you end up taxing investment, not indulgence.

The "Hazlitt" Examples (Primary)

1. The Wealth Tax (Liquidity & Valuation):

- o *Claim:* A small annual tax on "wealth" is harmless because the rich can afford it.
- o *Hidden Assumption:* Wealth is liquid, stable, and easily valued.
- o *Mechanism:* Requiring annual cash payments from illiquid assets (founder equity, private business) forces sales, depresses prices, and invites valuation disputes.
- o *Lesson:* If revenue requires annual forced liquidity from illiquid assets, the policy taxes capital formation.

2. Capital Gains Lock-in (Reallocation):

- o *Claim:* Taxing realised gains heavily targets windfalls without harming the economy.
- o *Hidden Assumption:* Investors will sell and reallocate capital regardless of the tax penalty.
- o *Mechanism:* Investors delay selling to avoid the tax ("lock-in"), freezing capital in older, less productive uses rather than recycling it into new ventures.
- o *Lesson:* If a tax discourages reallocation, it freezes capital where it is rather than where it is most productive.

3. Transaction Taxes (The Plumbing):

- o *Claim:* A tiny tax on trades discourages speculation and raises easy revenue.
- o *Hidden Assumption:* Trading is "noise" and does not affect the cost of capital.
- o *Mechanism:* Taxing every trade reduces liquidity, widens spreads, and raises the cost of capital for all firms, ultimately hurting savers and pension funds.

- o *Lesson:* If a tax damages liquidity, it taxes investment indirectly by making financing more expensive.

4. **Inheritance Taxes (Continuity):**

- o *Claim:* Taxing huge estates reduces inequality and hits only the "idle" heir.
- o *Hidden Assumption:* The estate is liquid cash, not a family business or farm.
- o *Mechanism:* High taxes force the liquidation of operating businesses to pay the cash liability, destroying continuity and long-term stewardship.
- o *Lesson:* If a tax forces liquidation of productive assets, it taxes continuity and investment, not merely inheritance.

"It would be too ridiculous to go about seriously to prove that wealth is not money, or in gold and silver; but in what money, gold, and silver purchase."

— **Adam Smith**, *The Wealth of Nations* (1776)