

Wealth, liquidity, and tax design

Separate the value of assets from cash available for payment and the income they generate. Then compare four tax mechanisms, preserving the chapter's criticism of frictionless revenue claims while testing its predictions and explicit design qualifications.

2 lessons · approximately 5 hours, plus multi-day practice

How to use this workbook

Read the assigned manuscript first. This workbook contains accompanying teaching and invented cases, not a revision of the source. Attempt exercises before consulting the rubrics and explanations. Written work is self-assessed or discussed with a tutor; no secure examination, academic credit or certificate is implied. Use a clearly labelled fictional case when live practice or personal disclosure would be unsuitable. Links use the course's intended publication address; for offline review, open the supplied source PDF at the full-book page numbers shown.

- Construct a net-wealth, cash-flow, and liquidity analysis.
- Explain marginal valuation and control rights.
- Distinguish four capital-related tax mechanisms.
- Assess valuation and payment safeguards.
- Evaluate empirical claims without confusing ownership transfer with lost output.

[Open the module and source reading links](#)

Lesson sequence

1. Separate wealth, liquidity, and control
2. Compare taxes by the behavior they change

Separate wealth, liquidity, and control

Allow approximately 100 minutes, plus any continuing activity.

Learning objectives

- Distinguish net asset wealth, liquidity, and cash flow using a balance sheet.
- Explain why a marginal price does not guarantee block-sale proceeds.
- Identify valuation, governance, and financing issues in an annual liability.

Assigned source readings

Complete consecutive source range, including its arguments and examples

Full-book PDF pages 54–58. Section links open the chapter at the relevant page.

Develop the argument

Three quantities, three different questions

The chapter's central correction is that wealth is not synonymous with ready cash. Net asset wealth is the estimated value of assets less liabilities. Cash flow is money received over a period. Liquidity is the capacity to convert assets into cash quickly, in meaningful size, with limited price impact and transaction cost. These concepts answer different questions: what is owned, what arrives, and what can be paid when due. The source includes liquidity as an unstyled subheading between asset wealth and cash flow; it is essential reading even though it is not marked as a formal heading. A valuable growing business may distribute little cash, while a person with high earnings may have little accumulated wealth. None of these distinctions alone settles a tax's fairness. They establish the balance-sheet and financing facts required before assessing it.

A marginal valuation is not a liquidation guarantee

The source explains that multiplying a quoted share price by a large holding creates a mark-to-market estimate, not a promise that the entire holding can be sold at that price. Buyers may require a discount for size, risk, information, or the speed of sale. Yet the reverse exaggeration must also be avoided: a large sale need not permanently collapse value, and its effect depends on market depth, execution, buyers' resources, and information. Distinguish temporary price pressure from a change in expected future cash flows. A transfer of shares changes ownership; it does not mechanically destroy the factory represented by those shares. The book links repeated sales to other investors' valuations, including pensions. That is a possible transmission channel whose magnitude and persistence require evidence rather than an assumption that all investors lose equally.

Control rights and valuation uncertainty

A control block combines financial claims with governance rights. Selling enough voting shares can change who appoints managers or determines strategy. The source describes this as a potential restructuring of governance, which is different from a simple cash withdrawal. Whether the change improves or damages the company is a separate question; founder control is not automatically optimal, nor is its loss automatically harmless. Private companies, intellectual property, partnership interests, and some property require appraisal because no continuously traded price exists. Document the valuation date, method, comparable transactions, assumptions, and uncertainty interval. Do not treat a contested appraisal as proof of fraud or treat every estimate as arbitrary. The analytical problem is to design a reliable, reviewable procedure whose costs are proportionate to the revenue and other objectives.

Finance a liability before predicting the consequences

The wealth-tax example lists selling, borrowing, using distributions, restructuring, migration, and disputes as responses. Build those branches explicitly. Borrowing can bridge a cash-flow gap but adds interest, collateral demands, and refinancing risk. A sale may change ownership or control; a distribution may reduce retained funds; a payment deferral changes timing and collection risk. Available exemptions and payment rules can materially alter the result. The source's moral discussion emphasizes administrative intrusion and discretion. These are legitimate governance concerns to assess through reporting burdens, appeal rights, privacy safeguards, and enforcement consistency, rather than an inevitable binary choice between no compliance and unlimited surveillance. The author's conclusion that recurring levies tax investment more than indulgence is an argument to evaluate, not a definition. A complete judgment combines liquidity analysis with distribution, public benefits, avoidance, administration, and feasible alternative tax bases.

A founder's annual cash requirement

Invented for this course.

In a fictional company, Mira owns 60% of voting equity valued at 20 million units in total. She has 100,000 cash, receives 150,000 annual distributions, and faces a hypothetical 240,000 liability on her 12 million stake. Ignore exemptions solely for this exercise.

1. Net equity value is 12 million before any personal liabilities; annual distributions are 150,000. Neither quantity is interchangeable with the 100,000 cash balance.
2. Cash plus distributions totals 250,000, so the stated liability could be paid in this simplified year, leaving 10,000 before living costs and other obligations. Do not announce a forced sale prematurely.
3. If distributions stop, a 140,000 shortfall remains after existing cash. Compare borrowing, permitted deferral, and sale, with explicit costs and uncertainty.
4. At the stated valuation, selling 1% of the company would notionally raise 200,000. Actual proceeds and control effects require transaction and voting-right information.

The calculation identifies a liquidity question, not a guaranteed collapse. The conclusion changes when distributions, debts, payment timing, and market depth change.

Practice and evidence

1. Build a stock-flow-liquidity statement

Rework Mira's case for a second year with zero distributions, 50,000 cash, and a valuation interval of 16–24 million. Use the same hypothetical 2% rate on her stake.

Deliverable: A range-based liability and financing statement.

1. Calculate low and high stake values and liabilities.
2. Show the cash shortfall for each.
3. Compare two financing routes without assuming unlimited borrowing.

Categories · 3 points

Keeps wealth, income, cash, and liabilities distinct.

Arithmetic · 3 points

Calculates ranges and shortfalls correctly.

Limits · 3 points

Names financing and valuation facts absent from the case.

2. Audit valuation and governance

Create an appraisal protocol for an invented private company with two share classes and a founder control block.

Deliverable: A one-page protocol and a 200-word governance-risk note.

1. Identify rights attached to each class.
2. State valuation methods and appeal safeguards.
3. Explain how a sale could change control without equating ownership transfer with destruction.

Rights · 3 points

Distinguishes cash-flow rights from voting rights.

Procedure · 3 points

Makes uncertainty, dates, and appeals explicit.

Reasoning · 3 points

Treats governance outcomes as conditional and evidence-dependent.

Reflection

Where in a public debate have you seen an asset valuation used as though it were an immediately spendable balance?

Formative self-check

Choose an answer before looking at the answer key. These questions are open practice, not a secure assessment.

1. A 5-million asset produces no distributions this year. Which statement is correct?

- A. Its owner has 5 million cash
- B. It has no value
- C. Wealth and current cash flow differ; liquidity must be assessed separately
- D. A sale must destroy it

2. A quoted share price values a large holding at 10 million. What is not guaranteed?

- A. That a marginal trade occurred
- B. That the entire block can immediately be sold for 10 million
- C. That ownership rights exist
- D. That the price provides any information

3. A founder sells voting shares to meet a payment. Which inference requires additional evidence?

- A. The buyer becomes an owner
- B. Voting concentration may change
- C. Cash can be raised through a sale
- D. Productive capacity necessarily falls

Answer explanations

1. C — Wealth and current cash flow differ; liquidity must be assessed separately

Valuation can reflect future returns while current distributions are zero. Neither ready cash nor destruction follows automatically.

2. B — That the entire block can immediately be sold for 10 million

A marginal quote is informative but does not guarantee block execution at that price. Market depth and sale conditions matter.

3. D — Productive capacity necessarily falls

Ownership transfer is not identical to destruction of assets or output. Governance and financing effects must be traced rather than assumed.

Compare taxes by the behavior they change

Allow approximately 100 minutes, plus any continuing activity.

Learning objectives

- Distinguish liquidity pressure, realization lock-in, trading frictions, and succession effects.
- Evaluate moderate designs and exceptions retained in the source.
- Connect investment effects to ordinary savers without asserting universal incidence.

Assigned source readings

Complete consecutive source range, including its arguments and examples

Full-book PDF pages 58–66. Section links open the chapter at the relevant page.

Develop the argument

Capital gains and the realization decision

The chapter next examines a tax triggered by selling an appreciated asset. A realization-based tax can create a wedge between holding and reallocating: an investor may defer sale to postpone payment. This is the lock-in mechanism. The source also describes borrowing against appreciated assets, which avoids an immediate sale but introduces leverage and financing risk. Distinguish the tax rate, the gain, the asset's total value, and the timing of liability. A gain tax does not normally apply to the entire sale price in the simplified example used here. Lock-in can delay useful reallocation, but observed holding is not itself proof of inefficiency. Compare the after-tax return from keeping an asset with the after-tax, risk-adjusted return from switching, and examine loss treatment and expectations about future rates.

Transaction taxes and market services

A transaction levy changes the cost of trading rather than merely the return on ownership. The source emphasizes liquidity, price discovery, bid-ask spreads, and financing costs, calling trading market plumbing. A small rate can become material when the same capital turns over frequently. Nevertheless, fewer trades do not automatically imply worse social outcomes: the function and quality of displaced trading matter. The source predicts higher volatility, but volatility effects should be tested rather than inferred solely from reduced volume. Study execution costs, depth, relocation, substitution into untaxed instruments, revenue, and effects on productive financing. A defensible comparison recognizes potential benefits sought by advocates, such as reduced harmful short-term trading, while asking whether the instrument actually selects that activity rather than imposing broad friction.

Succession and continuity

The inheritance section focuses on a cash liability attached to a transfer that may consist largely of a business, farm, or property. Its strongest mechanism is a mismatch among payment timing, available cash, and financing capacity. Separate sale of an operating firm from liquidation of its productive assets. A new owner may preserve operations; a distressed breakup may not. The source explicitly distinguishes low, simple transfer taxes from high, complex regimes and later says none of the four taxes is necessarily always wrong. These qualifications belong in every fair summary. Consider thresholds, installment options, valuation rules, anti-avoidance measures, and potential unequal treatment between similar assets. The author's cultural prediction that families may consume more or build less is contestable and requires evidence about behavior, rather than being established by the existence of a tax.

Compare mechanisms rather than repeating one slogan

The chapter's common-failure section links four instruments, but they are not mechanically identical. A wealth levy can demand recurring cash; capital-gains taxation can discourage selling; a transaction tax increases the cost of moving; succession taxes can create a payment at transfer. Notice that some predicted responses run in opposite directions. The plain-language critique asks analysts to look beyond lifestyle and headline percentages toward ownership, pricing, investment, valuation, and trust. Its concluding wage argument connects capital formation to productivity and ordinary people's future opportunities. Preserve that possible connection while acknowledging labor institutions, technology, demand, and how tax revenue is spent. Chapter notes and the repeated Hazlitt examples provide research leads and reinforce all four mechanisms; the closing Adam Smith quotation restates the distinction between money and what money can purchase. Report cited numerical findings as the book's summaries unless original studies have been inspected. A good comparison identifies which margin each design changes, who gains and loses, and conditions under which a redesigned tax could meet its objective with smaller costs.

The investor's switching decision

Invented for this course.

An invented investor owns an asset worth 100,000 with a purchase basis of 60,000. Selling triggers a hypothetical 25% tax on the gain. The current asset is expected to return 4% over one year; an alternative is expected to return 5%, with equal risk assumed solely for calculation.

1. The gain is 40,000 and immediate tax is 10,000, leaving 90,000 to reinvest. Taxing the whole 100,000 would be a category error.
2. Holding yields a stated pretax year-end value of 104,000. Switching produces 94,500 before any further tax at year end.
3. These values do not complete a lifetime comparison because the held asset retains an embedded liability. Specify the eventual sale date and tax assumptions before declaring one strategy superior.
4. Use the example to identify a deferral incentive, then test whether a higher alternative return, losses elsewhere, or a different horizon reverses the choice.

An immediate realization tax can discourage switching, but a proper comparison includes deferred liabilities, risk, and time. This is a teaching example, not investment advice.

Practice and evidence

1. Create a four-instrument mechanism matrix

Compare annual wealth, realized gains, transactions, and inheritance taxes as presented in the chapter.

Deliverable: Four mechanism cards with a potential benefit, a risk, a design safeguard, and a falsifying observation.

1. Identify the legal trigger and payment timing.
2. Separate selling incentives from holding incentives.
3. Include the source's explicit moderate-design qualification.

Differentiation · 3 points

Does not describe all four instruments as identical forced sales.

Balance · 3 points

Tests policy objectives as well as unintended effects.

Evidence · 3 points

Names observable outcomes appropriate to each mechanism.

2. Evaluate a succession proposal

An invented family workshop has valuable equipment, little cash, and a proposed succession levy. Compare immediate payment, installments, and sale to an outside operator.

Deliverable: A 350-word continuity assessment with a financing timeline.

1. State missing valuation and profit information.
2. Distinguish ownership continuity from operating continuity.
3. Evaluate administrative and equal-treatment trade-offs.

Continuity · 3 points

Avoids assuming that an outside sale necessarily closes the business.

Design · 3 points

Explains how payment timing changes liquidity pressure.

Trade-offs · 3 points

Includes collection risk and treatment of other taxpayers.

Reflection

Which tax debate would become clearer if participants identified the exact transaction or date that triggers payment?

Formative self-check

Choose an answer before looking at the answer key. These questions are open practice, not a secure assessment.

1. Which source mechanism tends to delay selling rather than compel it?

- A. Annual cash liability on illiquid wealth
- B. Realization-based capital-gains lock-in
- C. An immediate succession bill without cash
- D. A margin call

2. Trading volume falls after a transaction tax. What remains to be established?

- A. Whether trading volume fell
- B. Whether the tax has a rate
- C. Effects on execution, price discovery, volatility, revenue, and financing
- D. Whether any transaction ever occurred

3. Which summary best matches the chapter's own qualification?

- A. Every capital-related tax is always wrong
- B. Only heirs can ever bear succession-tax costs
- C. All asset sales destroy productive capacity
- D. Each tax can be designed moderately, and its behavioral effects still need analysis

Answer explanations

1. B — Realization-based capital-gains lock-in

Lock-in arises because selling triggers a liability. This differs from situations where cash must be raised to meet an already-due obligation.

2. C — Effects on execution, price discovery, volatility, revenue, and financing

Volume is one outcome, not a full welfare measure. The services and costs of displaced trades must be examined.

3. D — Each tax can be designed moderately, and its behavioral effects still need analysis

The common-failure section explicitly rejects doctrinal purity. Preserving that caveat is necessary for source fidelity and fair assessment.

Module assessment

A mixed-asset levy review

An invented region proposes a recurring asset levy and a separate succession levy to fund vocational training. A representative estate holds public shares, a private workshop, rental property, debt, and cash. No actual valuations are supplied.

Required evidence

- A requested-data schedule and stock-flow statement template.
- A financing and governance scenario analysis for both levies.
- A comparison with realized-gain taxation and a conditional recommendation.

Assessment criteria

Categories · 5 points

Keeps asset values, liabilities, income, gains, and payment capacity distinct.

Mechanisms · 5 points

Separates sale pressure, lock-in, control transfer, and operating continuity.

Public outcomes · 5 points

Includes training benefits, distribution, administration, and collection risk.

Evidence · 5 points

Specifies estimates and counterfactuals needed before a numerical forecast.

Model response: consult after your attempt

A strong response asks for asset-specific rights, bases, values, cash flows, debt terms, and payment dates before calculating receipts. It models several financing routes rather than assuming universal forced liquidation, considers appraisals and appeal procedures, and treats public training benefits as part of the comparison. It may support or reject a design, but it must explain why the selected base and payment rules produce better outcomes under stated assumptions.

Source cautions and interpretation

- Footnotes 12–16, all four chapter notes, repeated Hazlitt examples, and closing quotation were read. Footnote 16 is attached to a chapter-end note and must not be omitted.
- Claims about market-wide price pressure, volatility, migration, and long-run accumulation are source claims, not independently verified estimates.
- Liquidity is an unstyled source subheading and is explicitly taught. No image blocks occur.

- The module does not give tax or investment advice; hypothetical rates and examples are instructional. Source remains unchanged.

Source coverage

Chapter 3: Wealth Is Not Money

The complete opening quotation and chapter introduction establish the problem and author's governing position; the first teaching section reconstructs the argument and separates its assumptions from evidence.

[Read source section: full-book PDF page 54](#)

The Governing Claim

Frames the asset-value/cash distinction as a prerequisite to policy evaluation rather than a complete fairness verdict.

[Read source section: full-book PDF page 54](#)

Wealth, Liquidity, and Cash Flow: Three Different Animals

Defines net wealth, liquidity, and cash flow separately in the founder balance-sheet example.

[Read source section: full-book PDF page 54](#)

Asset wealth

Computes assets net of liabilities and treats quoted values as estimates rather than cash balances.

[Read source section: full-book PDF page 55](#)

Cash flow

Distinguishes periodic distributions from accumulated value and tests a year with zero distributions.

[Read source section: full-book PDF page 55](#)

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

Explains marginal quotes, block execution, temporary pressure, and the need to measure broader spillovers.

[Read source section: full-book PDF page 55](#)

Control Blocks: When Selling Destroys the Thing Being Taxed

Distinguishes voting and financial rights; tests control transfer without assuming productive assets disappear.

[Read source section: full-book PDF page 56](#)

Valuation: The Quiet Hell Beneath the Slogan

Builds an appraisal protocol with dates, comparable evidence, uncertainty, costs, and appeal.

[Read source section: full-book PDF page 56](#)

Why This Matters Morally

Treats reporting, privacy, discretion, and enforcement consistency as governance trade-offs requiring safeguards.

[Read source section: full-book PDF page 57](#)

Primary Example (13): The Wealth Tax

Compares cash, distributions, borrowing, deferral, and sales before asserting forced liquidation.

[Read source section: full-book PDF page 57](#)

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

Explains realization-triggered liability and deferred tax as distinct from the whole asset’s value.

[Read source section: full-book PDF page 58](#)

Primary Example (15): Capital gains lock-in

Works a gain-basis calculation and requires deferred liabilities and time horizons in switching comparisons.

[Read source section: full-book PDF page 58](#)

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

Distinguishes transaction levies from ownership taxes and identifies repeated trading frictions.

[Read source section: full-book PDF page 59](#)

Primary Example (16): Transaction taxes

Tests execution, market depth, price discovery, relocation, volatility, and the possible value of reduced harmful trading.

[Read source section: full-book PDF page 59](#)

Inheritance Taxes: The Mirage of “Taxing the Dead”

Preserves the source’s low/simple versus high/complex distinction and analyzes payment timing at succession.

[Read source section: full-book PDF page 60](#)

Primary Example (18): Inheritance taxes

Compares installments and sale while separating ownership continuity from operating continuity.

[Read source section: full-book PDF page 60](#)

The Common Failure: Converting Portfolios into Cash by Force

Contrasts four distinct mechanisms, including their opposite incentives to sell or hold; retains moderate-design caveat.

[Read source section: full-book PDF page 61](#)

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

Translates lifestyle and small-percentage slogans into liquidity, valuation, governance, and financing questions.

[Read source section: full-book PDF page 61](#)

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

Connects capital formation to productivity and savers conditionally, including revenue uses and other wage determinants.

[Read source section: full-book PDF page 62](#)

The Lesson Line

Tests the closing investment claim through a balanced four-instrument comparison rather than doctrinal agreement.

[Read source section: full-book PDF page 63](#)

Chapter 3 Notes

Reads four endnotes and attached footnote 16; marks estimates and bibliographic claims as unverified source reports.

[Read source section: full-book PDF page 64](#)

The "Hazlitt" Examples (Primary)

Synthesizes all four tax mechanisms and includes the closing Adam Smith quotation in the required complete reading.

[Read source section: full-book PDF page 65](#)

Liquidity

Defines speed, size, price impact, and transaction costs separately from wealth and cash flow; tested in the founder financing exercise.

[Read source section: full-book PDF page 55](#)