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towards a biblical mind

Render unto Caesar?

The dilemmas of taxation policy

by Christopher Townsend

… taxation is the confiscation of our property by people who prefer to spend it on their priorities rather than ours.

Madsen Pirie, President of the Adam Smith Institute, 2000

Taxes, after all, are the dues we pay for the privileges of membership in an organised society.

Franklin D. Roosevelt, 1936

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Summary

Taxation is back on the political agenda: the choice between keeping taxes down and improving public services will soon need to be confronted. This paper considers taxation policy from a biblical perspective and explores some basic issues. How much tax should governments raise? How should the burden of taxation be distributed across society? Within what political structures should the power to raise taxes operate? A number of potential areas for reform of the UK tax system are highlighted. More importantly, this paper emphasises that taxation policy must be considered in the context of a wider debate about the vitality of democratic government, the operation of the economy, the institutional landscape and the channels through which welfare is provided.

Introduction

For those obliged to complete a tax return, taxes may seem at best dull and at worst exasperating; for others whose taxes appear as a deduction on a salary slip, taxes may simply feature as a regrettable fact of life. Taxation does, of course, raise ethical issues at the personal level as tax returns are completed, giving decisions made, or tax planning measures considered. However, it would be easy to overlook the critical role that taxation has played on a much broader canvas at some of the signal moments in human history. The central position of Parliament in the British constitution was secured when the Glorious Revolution of 1688 led to a huge demand for tax revenue to fund wars against France and Spain. Nearly a century later, the cry ‘no taxation without representation’ set off the American War of Independence. Indeed, Bethlehem was the location for the most important birth in history as a result of a tax census.

Taxation is an inevitable aspect of the task of government. In the long term, the overall level of taxation limits the money available to government and therefore the range of functions which government can fulfil. Tax is, by design or by default, a policy instrument which redistributes resources from some to others in society. In the UK in 2000/1 over half of all government expenditure was attributable to ‘welfare state’ commitments in the form of social security payments, education, healthcare and housing. Since taxation involves the compulsory transfer of assets from individuals to government and, in a democracy, a debate about how those assets should be used, taxation is a controversial topic. Debates about taxation are symptomatic of fundamental disagreements about the proper ordering and goals of society. It is with taxation, viewed from the perspective of public policy, and its interaction with the structure of society, that this paper is concerned.

Taxation: the political debate

Today, the political right argues that anything but minimal taxation is verging on the immoral. The Conservative Party fought the last UK election on the basis of a low-tax agenda arguing it was ‘not just the basis of a dynamic economy but also the foundation of a moral, compassionate, free and just society.’ [1] George W Bush has signed legislation to implement $1.35 trillion in tax cuts. In the UK, New Labour’s attitude to taxation has been more ambiguous. Tarnished in the past by a ‘tax and spend’ image Labour has pledged not to increase income tax rates. In its first term, taxation was increased overall by methods which critics labelled ‘stealth taxes’. In its second term, the government has committed itself to increasing expenditure in real terms on public services, health and education faster than GDP growth while continuing to keep income tax rates unchanged. Independent analysts argue that the government’s sums do not add up. From 2003/4, either spending plans will need revision or tax increases of up to 4p in the pound imposed.[2] If a recession is sharper or longer than expected the pressure on public finances

1 William Hague, quoted by Polly Toynbee in ‘Biting that tax bullet’, *The Guardian*, 17 March 2000.
2 C. Emmerson, *Public Spending: What are the Options beyond March 2004?*, Institute for Fiscal Studies (IFS), May 2001; ‘Tax must rise by 4p, Blair told’, *The Observer*, 12 August 2001 (citing forthcoming report ‘Choosing Justice’ by the Institute of Public Policy Research).

will be even greater. The case for tax increases, long marginalised, is moving back onto the political agenda.

Behind these debates about tax and spending levels lie differing political philosophies. On the right of the political spectrum, *pragmatic libertarians*, such as Hayek and Friedman,[3] emphasise individual autonomy and champion freedom, i.e. freedom from coercion and interference. Free markets are the most effective mechanism for allocating resources and seeking to satisfy people's wants. There will be 'winners' and 'losers' but as 'losers' arise from the outcome of market mechanisms rather than any individual's intentions, there is no injustice. So there is no moral justification for redistribution. Indeed, to strive for social justice would lead to the destruction of personal freedom as individuals grow to depend on state action and the state imposes control mechanisms over people and their activities to achieve the distribution of resources demanded by 'social justice'. A minimalist state should concern itself with the protection of the citizen's person and property, the promotion of free markets and the enforcement of contracts, and take only limited steps to provide certain public goods. It is accepted that the state should act as a 'safety net' to prevent destitution but, beyond this, practical help for the disadvantaged should be a matter of private charity. More radical still are *natural rights libertarians*, such as Robert Nozick,[4] from whose theory of property rights some infer that taxation is theft (since money is extracted from people who acquired it justly and used in ways they would not choose) and forced labour (as we are compelled to spend part of our time working for the government). These views find their popular counterpart in 'Tax Freedom Day': on which in any given year we 'stop working for the government' and start working for ourselves.

New Labour's 'Third Way', while claiming continuity with Labour's roots, has sought to occupy a middle ground between individualism and collectivism. However, restatements of the case for a more red-blooded version of *social democracy* are being heard again. The Fabian Society's Commission on Taxation and Citizenship penned a report in 2000 sub-titled 'A New Politics of Tax for Public Spending'.[5] Its 'strong conception of citizenship' is in sharp contrast to the libertarian view. The individual is not autonomous but a member of a civic community of mutual dependence. Freedom must have regard to a person's circumstances and promoting freedom implies ensuring each citizen has the core goods necessary to realise his potential. A universal system of public services and redistribution to reduce disparities in income and promote social inclusion, together with a progressive tax system, based on ability to pay, are favoured. From such a perspective 'Tax is not a necessary evil but an expression of social solidarity.'[6] Nonetheless, pursuing the social benefits which arise from taxation must be balanced by measures to foster rather than undermine the productivity of the economic base from which tax revenues are generated. Finally, the relationship between the individual and the state must operate over a wider nexus than taxation and public services: active democracy and government accountability are vital.

Taxation: some facts and figures

There is, in fact, concern that the sinews which connect taxation with active participation in a democratic society are weakening. A recent comment on research into public attitudes towards taxation was: 'What has struck us most is what we have come to call the phenomenon of disconnection …'.[7] Part of the problem is that people do not understand the tax system, do not know how much tax the UK raises compared with other nations, or how taxes are spent, and fear that they are spent badly. Before considering a biblical perspective on taxation policy it is helpful to begin with a lightning survey of taxation and public spending in the UK today.

Public spending and tax revenues

In 2000/1 public expenditure was £361 billion and represented 37.7 per cent of GDP.[8] The largest components of government expenditure in 2000/1 were social security payments (27.8%), health (14.6%) and education (12.4%). These were followed by debt interest (7.6%), defence (6.2%) and law and order (5.4%).[9] Taxes fund (a) the provision of 'public goods' (such as defence and law and order) for everyone and (b) goods and services produced by public sector (or by the private sector but with payments or subsidies from government) and supplied at zero or reduced cost to end users, and (c) transfer payments from taxpayers to, for example, pensioners or gilt owners.

The tax raised to fund this expenditure was equivalent to roughly £7,900 of tax for every adult in the UK.[10] In 2000/1 the principal sources of tax revenues were income tax (25%), national insurance contributions (16%), VAT (16%), other indirect taxes (i.e. tobacco, alcohol, and fuel duty; road tax; betting duty; lottery monies) (13%), and corporation tax/business rates (13%).[11] Almost all tax was raised by central government with only 8 per cent taking the form of local taxes (i.e. business rates and council tax).[12] For an international comparison, figures for 1997 show tax and social security contributions as a proportion of national income varied significantly across the following range: USA (30%), UK (36%), EU average (42%) and Sweden (52%).[13]

Tax, benefits and redistribution

Taxes overall in the UK are not progressive. While high-income households pay a higher proportion of their income in income tax than low-income households, this is more than offset by the regressive impact of indirect taxes (which divert a larger part of low-income household expenditure towards the Exchequer). When all taxes are taken into account, in 1998/9 the poorest 20 per cent of households paid 40 per cent of their gross income in tax but the wealthiest only 36 per cent.[14]

Once welfare payments, education and NHS benefits are taken into account, the UK tax/welfare system delivers a significant redistributive effect as the table below illustrates:

Summary of effects of taxes and benefits by successive 20% groups 1998–99[15]

	Lowest	Second	Third	Fourth	Top
1 Earned/investment income	2940	7260	16570	26700	51220
2 Income plus cash benefits	7740	12430	20010	28720	52340
3 Total income less all taxes*	4630	8070	12500	17750	33340
4 Net of tax income + benefits**	8820	11470	15840	20380	35440
5 Impact ratio (i.e. (4) ÷ (1))	**300%**	**158%**	**96%**	**76%**	**69%**

* Includes indirect taxes on expenditure **Includes NHS + education

The ratio of 'incomes' received by the top 20 per cent and bottom 20 per cent changes from over 17:1 (before Government intervention) to 4:1 (after Government intervention). Since 1997 fiscal changes have favoured lower-income households but incomes have been growing fastest among the richest 20 per cent of households – rising by 2.8 per cent a year on average after inflation compared to 1.4 per cent for the poorest 20 per cent of households. A more progressive tax and benefits system has merely slowed the

3 See, e.g., F.A. von Hayek, *The Constitution of Liberty*, Routledge, 1960, and M. and R.D. Friedman, *Free to Choose: A Personal Statement*, Secker and Warburg, 1980.
4 See, e.g., R.A. Nozick, *Anarchy, State and Utopia*, Blackwell, 1974.
5 *Paying for Progress: A New Politics of Tax for Public Spending*, The Fabian Society's Commission on Taxation and Citizenship, Fabian Society, 2000.
6 M. Taylor, 'Next stop Utopia … but it'll cost us', *The Observer*, 19 August 2001.
7 *Paying for Progress:* op. cit., p.55.
8 Calculated from HM Treasury, Financial Statement and Budget Report, March 2001.
9 HM Treasury, Financial Statement and Budget Report, March 2000 in *Paying for Progress*, op. cit., p.63.
10 Calculation adapted from L. Chennells, A. Dilnot and N. Roback, *A Survey of the UK Tax System*, IFS, updated version, August 2000, p.1. Total tax receipts were £383 bn implying a current surplus of £22 bn.
11 HM Treasury, Financial Statement and Budget Report, March 2000, in *Paying for Progress*, op. cit., p.65.
12 Ibid.
13 OECD, Revenue Statistics 1965–98, Table 1: see ibid., p.62.
14 Figures drawn from National Statistics, 1998–99: see ibid., p.71.
15 Figures drawn from National Statistics, 1998–99: see ibid., p.70.

growth of inequality.[16] These quintile statistics do not reveal trends at the highest levels of income. Remuneration levels in FTSE 100 boardrooms rose by 28 per cent in 2000.[17] In 1978/79 the top 1 per cent of income taxpayers contributed 11 per cent of all income tax paid; in 1999/00 this share had risen to 20 per cent despite (or some would argue because of) a reduction in the higher rates of tax.[18]

Taxation: towards a biblical perspective

It has been argued elsewhere that Israel, as first established in Canaan, serves as a case study or 'biblical paradigm' of political, social and economic organisation.[19] It is convenient to begin by examining how 'taxation' fits into that 'paradigm': while no direct prescriptions for our own situation emerge, there are some illuminating principles. Then we consider the building blocks of any philosophy of taxation: the relationship between the individual and the community, the role of the state, and principles of social justice. The themes which emerge are then applied to selected issues in relation to UK taxation today.

A biblical 'paradigm'

The economic system

The economic model embedded in biblical law allowed goods to be traded freely, but placed tight controls over markets for key factors of production, land and capital.[20] Land, the primary means of production, was allocated on an equitable basis among families when Israel arrived in Canaan.[21] The freehold sale of agricultural land was prohibited, restoration of lands at the Jubilee was required, and interest-bearing loans by which financial power could be accumulated were banned.[22] In this way, the architecture of the economic system – ownership structures, design of property rights, boundaries of contract law – included built-in resistance to extreme poverty or wealth. So after-the-event fiscal redistribution implemented by a substantial state apparatus was largely absent. In principle, each family had material resources to enable them to earn their own living and, if circumstances dictated, an asset which could be realised for cash without being permanently forfeited. These landholding arrangements were intended to undergird the central importance of the extended family or 'household' within Israel's social structure.

Taxation

Tithing in a theocracy has, to a greater extent than might first be appreciated, characteristics analagous to modern taxation. Tithes were not simply a form of giving but were considered the property of the nation's ultimate ruler, God. So tithes were distinguished from freewill offerings and failure to tithe was 'robbing' God.[23] While not enforced as modern taxes are, payment of tithes was 'obligatory' – a prerequisite for maintaining full membership of Israelite society.[24] If the system of tithes is viewed through a lens which highlights its characteristics as a mode of 'taxation', a number of features emerge:[25]

a) taxation was proportional rather than progressive so that, whatever the household's income, the same proportion was taxable;
b) taxation was universal in its scope: every household, however poor or rich, was to pay its tithe to reflect, and contribute to, its membership of the people of Israel;
c) the level of taxation was capped at a relatively low level which was built into Israel's constitution;
d) communication and reinforcement of the rationale for taxation were integral to the system;
e) taxation was collected centrally (as to two-thirds) and locally (as to one-third) but under a regime of 'self-assessment';
f) taxation financed a cadre of 'professionals', the priests and the Levites, whose work helped to sustain the welfare of the whole community. The Levites' role included health, education and constitutional law matters;
g) taxation collected at the local level funded poverty relief measures which promoted 'social inclusion' of those at the economic margins of society.

Welfare provision

The role of tithes in addressing the problem of poverty was, however, relatively limited. A wide range of poverty relief mechanisms included interest-free loans; bonded service; debt cancellation and freedom for bondservants every seventh year; gleaning laws; and the role of the kinsman-redeemer.[26] These mechanisms involve personal effort on the part of the needy (the grain must be gleaned, the loan repaid, the service rendered), local community-based responses, formal social obligations based on kinship ties, and a commitment to enabling people to make a fresh start. The level of provision envisaged is linked to need but liberally interpreted: '… do not be hard-hearted or tight-fisted towards your poor brother. Rather be open-handed and freely lend him whatever he needs … Give generously to him …' (Deuteronomy 15:7–8, 10). The ideal was voluntary action, encouraged by the 'motive clauses' found in biblical law. But the poor could appeal to the 'elders at the gate' for enforcement of their 'cause' or 'rights': government mediation was present but focused at the local level.[27]

Individuals, community and freedom

Individuals are not in the biblical view autonomous agents who are, or should be, self-sufficient. The individual is located in a community characterised by interdependence in which the family has a unique and important role.[28] So, the idea of freedom needs to recognise the complementary role of obligation. All this undergirds a concern for social inclusion but does not logically entail collective action through government, funded by taxation, where alternative methods of expressing our inter-relatedness exist.

The state

The legitimacy of taxation by the state and the duty to pay taxes is endorsed by Jesus himself: 'Give to Caesar what is Caesar's and to God what is God's…'.[29] However, these words do not shed light on the parameters, moral and functional, within which the state *ought* to operate. There is, in fact, a hint that the state may make demands outside its proper remit: what is Caesar's? The *locus classicus* of NT teaching on the state, Romans 13:1–7, has led some Christians to argue that the Bible gives no mandate to the state to perform any role beyond law, order and defence. But, on any approach, that is too narrow a view of the state's role. Governments are to 'commend those who do good' (1 Peter 2:13–14): to encourage and reward social responsibility by members of society and, in particular, the affluent. Further, the Old Testament's conception of the 'ideal ruler' is one who will be righteous, dispense justice, bring prosperity and help the needy and afflicted.[30]

At the same time, there is a vital strand of biblical teaching which highlights the dangers of state coercion. Old Testament law prohibits the accumulation of military or financial power by the king.[31] When Israel asks for a king 'such as all the other nations have' Samuel warns that the monarchy will absorb manpower (through forced labour) and resources (by various methods) to develop a military arsenal, to finance a bureaucracy, and to provide privileges to a ruling class, and in doing so dislocate family life.[32] Subsequent history provides several instances of abuse of royal

16 'First the taxes, now the spending', *The Guardian*, 10 May 2001, summarising IFS results.
17 'Executive pay shoots up by 28%', *The Guardian*, 29 August 2001.
18 L. Chennells, A. Dilnot and N. Roback, op. cit., p.20.
19 See, e.g., C.J.H. Wright, *Living as the People of God*, Leicester, IVP, 1983.
20 See P. Mills, 'The divine economy', *Cambridge Papers*, 2000, Vol. 9, No. 4.
21 Josh. 13–19.
22 Lev. 25:8–55; Deut. 23:19.
23 Lev. 27:30; Deut 12:6, Mal. 3:9.
24 R.A. Oden, Jr, 'Taxation in Biblical Israel', *Journal of Religious Ethics* (1984), vol. 12, pp.162–181.
25 Lev. 27:30–33; Num. 18:21–29; Deut. 12:4–7, 14:22–29, 33:10. There is some debate over whether the local tithe in the third year was additional to, rather than instead of, the normal annual tithe.
26 Lev. 25:1–7, 25–55; Deut. 15:1–18.
27 J.D. Mason, 'Biblical Teaching and the Objectives of Welfare Policy in the US', *Journal of the Association of Christian Economists*, August 1994, pp.27–28.
28 See, e.g., 1 Tim. 5:8; 2 Cor. 12:14; Mark 7:9–13.
29 Matt. 22:21; cf. Mark 12:17; Luke 20:25.
30 Psalm 72; Prov. 31:9.
31 Deut. 17:14–20.
32 1 Sam. 8.

power and expropriation of economic resources.[33] So while a yearning for the 'ideal state' to help the needy is present, so is the warning that the state can, and often will, bring exploitation, social upheaval and excessive taxation.

Biblical law establishes a clear preference for limited central government and wide dispersion of both political power and economic resources, partly to minimise the risks associated with concentration of power. The Bible focuses attention on a range of institutions which occupy the space between the individual and the state, specifically the nuclear family, extended families and wider kinship groups, local communities, local government and the church.[34] Modern analogues might extend to include employee associations, mutual societies, trade networks, and voluntary organisations. Such institutions are less vulnerable to the 'relational distance' which exists between the state and the individual. The state's scale, and anonymity, can militate against responsible engagement by welfare recipients (who may become tempted to abuse the system) and taxpayers (who may become reluctant to contribute funds).

Social justice/economic 'redistribution'

The passionate concern of the OT prophets for the downtrodden and marginalised underscores the importance of social justice, of practical concern for the poor and powerless, and access to resources to allow a basic standard of living. To accumulate or 'hoard' excessive wealth, rather than putting it to good use, invites condemnation.[35] Large incomes, it seems, may be earned lawfully and applied constructively, not least by generous giving. Still, the advantages of having neither too much nor too little are identified, and – within the church – a strand of egalitarian idealism exists.[36] The priority of personal benevolence (and the prospect of eschatological judgement) are the prominent themes in relation to the use (and misuse) of wealth.[37] However, the Bible offers no formula establishing an abstract ideal of distributive justice.

The issue is what role, if any, the state should play in 'redistribution'. It is helpful to distinguish between *social insurance* (where everyone contributes to a fund from which everyone may draw in defined circumstances such as unemployment and old age and where the goal is insurance or income smoothing) and *tax-funded redistribution* (where assets are transferred from better-off to worse-off to adjust the degree of inequality). The moral argument required to justify the former, which is compulsory co-operation, is distinguishable from that needed to support the 'compulsory generosity' of the latter. The legal checks on the long-term consolidation of excessive wealth differentials present in the Jubilee land laws provide a foothold for such an argument. From a pragmatic perspective, tax-funded redistribution may be the nearest approximation available today to periodic redistribution of wealth-producing assets.

The power to tax: political structures

Democracy

Our survey of biblical material highlighted the value of decentralisation of power. In a nation-state, the mere existence of democracy diffuses power to some degree because elections allow the people to hold governments to account and to wield some influence over government decisions. A precise correlation between 'taxation' and 'representation' does not exist: some UK nationals over 18 are non-taxpayers; some foreign nationals pay UK tax on UK-source income. It is interesting too that the precise shape of democratic institutions can influence the development of a tax system: the incoherence of the UK tax system has been attributed to rapid policy shifts, resulting from a combination of the power of the executive to implement change, regular changes in government, and shuffling of tax policy at each year's Budget.[38]

Decentralisation

Decentralisation favours the revitalisation of regional and local government. Tax-raising powers are an important element: local government with limited discretion to raise funds has little scope to respond to local preferences. The Scottish Variable Rate allows the Scottish Assembly to alter the basic rate of income tax up or down by up to 3 pence in the pound; London can levy road congestion and parking charges to fund transport policy. Local authorities collect council tax which contributes 25 per cent towards local government spending with the bulk paid for by central government grants (so a 1 per cent increase in local spending requires a 4 per cent increase in council tax). If local taxation is taken seriously, a local income tax is generally regarded as the way forward for the UK, and was proposed by the Layfield Committee as long ago as 1976.[39] Practicalities point to implementation by a 'variable rate' mechanism similar to the Scottish arrangement. In federal tax systems equalisation transfers from richer to poorer regions are commonplace – though not universal. The form and extent of such inter-regional transfers would need careful consideration.[40]

The international dimension

Tax harmonisation is on the EU's agenda and the possibility of taxes imposed directly by the EU has been mooted. The issues are complex but the former tends to favour the priorities of the 'market' over national sovereignty and voter preference; the latter could both extend the gap between taxpayer and government, and exacerbate the EU's 'democratic deficit'. International tax co-operation, however, is vital to ensure that multi-jurisdictional commercial activity is taxed fairly, to combat aggressive tax-planning techniques, and to adapt to new developments, such as e-commerce.

The tax burden: who should pay what?

The equitable distribution of the tax burden has several dimensions: horizontal equity (equal treatment of equals), vertical equity (the appropriate basis for unequal treatment of unequals), and inter-temporal equity (the relative burden of current and future taxpayers). Freedom from abuse of power by arbitrary collection of tax (by administrative fiat, opaque and uncertain laws or retrospective legislation) and minimising the compliance burden are parallel, and sometimes competing, concerns. We now explore three contexts in which decisions about the equitable allocation of tax must be made.

Progressive taxation?

In 1986 the Church of England's Board for Social Responsibility wrote: 'It is generally accepted as a principle of taxation that … those with higher incomes should not only pay a larger *amount* of their income in taxation but should also expect to pay a larger *proportion*….'[41] The debate over whether it is desirable for taxation to be proportional (i.e. the same proportion extracted from all income groups) or progressive (i.e. higher-income groups paying a higher proportion) has a long pedigree. From the biblical material, arguments can be made both ways. However, an intriguing possibility emerges for consideration: proportional taxes on income combined with taxes to limit wealth accumulation.

Whether tax increases lead people to work harder (to increase their after-tax incomes) or less hard (because an extra hour's work now generates less 'utility' and an extra hour's leisure is now more appealing) is a moot point. However, eventually, increases in tax

33 2 Sam. 20:24; 1 Kings 4:6; 1 Kings 5:13–14, 9:20–22; 1 Kings 12; Jer. 22:13–18, 1 Kings 4:7–19.
34 Christians, in particular, have good reason not to suppose that their responsibility for the welfare of others, particularly within the family or the church, are assumed by the state's welfare arrangements and as far as the individual is concerned discharged by the payment of taxes: see Gal. 6:10; 1 Tim. 5:3–10.
35 James 5:1–6; cf Lk. 12:13–21.
36 Prov. 30:7–9; Acts 2:44–45; 2 Cor. 8:9, 13.
37 Matt. 25:31–46; Lk. 12:32–34; 16:19–31; 1 Tim. 6:17–19.
38 S. Steinmo, 'Political Institutions and Tax Policy in the United States, Sweden and Britain', *World Politics*, 1989, LXI, pp. 500–535.
39 Layfield Committee, *Local Government Finance: Report of the Committee of Enquiry*, Cmnd 6453, London: HMSO, 1976.
40 See, e.g., L. Blow, J. Hall and S. Smith, *Financing Regional Government in Britain* (2nd edn.), Institute for Fiscal Studies, 1996.
41 Report of Social Policy Committee of the Board for Social Responsibility, *Not Just for the Poor: Christian Perspectives on the Welfare State*, Church House, 1986, p. 110.

rates are counterproductive and reduce the amount of tax collected. There is generally a trade-off between 'efficiency' and 'equity' or, in other words, a 'leaky bucket' which loses some of its contents when used to carry income from the rich to the poor.[42] However, the disincentive effects of a wealth tax (which taxes amounts accumulated from past effort) should in principle be less marked than those caused by high marginal rates of income tax (which penalise current and future effort). It is striking that the OT economic model of low marginal rates of tax (10%) and periodic wealth transfers has some resemblance to the theoretical economist's preference for lump sum taxes (i.e. zero marginal taxation) and cash transfers.

The only tax on wealth in the UK at present is inheritance tax (IHT) which produces less than 1 per cent of all tax revenues. Given the tax-free band, tax-privileged assets, and exemptions for a range of lifetime gifts and legacies, IHT has been described as 'a voluntary tax paid only by those who dislike[d] their relatives even more than they disliked paying tax.'[43] Given that the distribution of wealth is far more unequal than the distribution of income, some form of wealth taxation should contribute to horizontal equity (as taxable capacity should take wealth into account) and vertical equity (to offset inequality). While an annual wealth tax is the purest form of wealth taxation, practicalities favour a wealth transfer tax (WTT).[44] A WTT may be donor-based (with tax levied by reference to a person's estate on death) or donee-based (with tax levied by reference to lifetime aggregate of gifts received). The latter, while somewhat more complex to administer, targets wealth inequality directly. A tax-free band, and progressive tax rate structure, would provide room for bequests to children and, in wealthy households, provide an incentive to distribute personal wealth widely.

Taxation of the family

The principle of horizontal equity is difficult to apply to the taxation of the family. There is an inherent conflict between the idea that individuals should be treated equally and the desire to relate tax liabilities to the totality of a person's economic circumstances (e.g. a spouse's income; the imputed income from domestic provision of non-market services by a 'homemaker'; cost savings from living together; or additional costs of young or elderly dependants). The former points towards an individual basis of taxation; the latter towards a unit system under which household income is aggregated.

Any tax system will inevitably involve implicit – or explicit – convictions about the value, structure and functions of the family unit. Cohabitation and marriage may be treated equally (on the basis that the tax system should not seek to influence personal decisions of this kind) or marriage favoured over cohabitation (on the basis that the relative stability of marriage as the basis for a family unit confers benefits on society as a whole). The married couple's allowance has now been abolished, and funds diverted to child benefit and the children's tax credit as part of the UK government's attempt to reduce child poverty. Tax also affects labour market participation decisions by women. The current system of independent taxation and personal allowances (a) implies that two-earner couples enjoy twice as much tax-free income as one-earner couples, and (b) favours labour market participation by women through a lower marginal rate of taxation on entering the labour market compared with alternative arrangements such as 'income splitting' across the household or transferable personal allowances.[45] The upshot of changes over the last several years is that marriage enjoys no income tax privileges, stay-at-home parents suffer tax disadvantages, and children's tax credits appear to favour singles.[46] All tax systems involve compromises between competing aims but a stronger 'signal' in support of marriage, and incentives for parents to spend time on childcare, might be of greater long-term benefit to children than increased cash benefits to households with children regardless of family structure.

Generational imbalance?

There is a tendency for the current generation to overlook – or disregard – the consequences of today's tax and spending decisions on future generations. A technique, known as generational accounting, provides an insight into this phenomenon. 'Generational imbalance' exists if projected lifetime tax payments of current newborns are less than projected government expenditure over their lifetimes and, as a consequence, the shortfall will be met by higher tax payments by future generations. Recent generational accounts indicate that the UK could achieve generational balance by relatively modest tax increases of under 5 per cent.[47] By contrast, the equivalent figures for Germany, USA and Japan were 9 per cent, 11 per cent and 16 per cent respectively.[48] Generational accounts are sensitive to assumptions made about economic growth and demographic change and must be handled with care. However, the biblical principle that one should pay one's own debts implies that governments should be wary of permitting material levels of generational imbalance. To do so – quite apart from the moral concerns – will merely exacerbate a new form of distributional conflict mediated through inflation or the ballot box: pensioners versus workers.

Tax levels: the future of government expenditure

Historical trends

The twentieth century has seen, in Niall Ferguson's words, the transformation of the 'warfare state' into the 'welfare state'.[49] Until this century, the demands of warfare have been the principal outlet for state spending and in 1898 public expenditure represented a mere 6.5 per cent of UK GDP.[50] From World War II until the mid-1970s was the 'golden age' of the mixed economy and a 'cradle to grave' welfare state. Since then, successive governments have sought to cut down the extent of the state's responsibilities through privatisation, contracting-out services, Private Finance Initiatives, and trimming welfare state provision (e.g. by linking benefits to increases in the Retail Prices Index not earnings growth, and increasing use of means-tested rather than universal benefits). Nonetheless, tax and public expenditure as a proportion of GDP has not fallen noticeably: more pensioners, single-parent families, students and low-paid workers are supported but often – in relative terms – at less generous levels.

A number of factors, quite apart from the emergence of the New Right, lie behind this attempted retrenchment. An *ageing population* combined with expensive technological advances in medicine, has increased demand for pensions, income support and NHS resources. *Family breakdown* and the transition from elitist to *widespread tertiary education* have added to the potential demands on the public purse. Politicians – outside the US – are aware of popular support for public services but are persuaded, with some foundation, that the desire for improved public services is outweighed by *taxpayer resistance*. The electorate is considered likely to punish political parties which advocate or implement tax increases. Oil price shocks have prompted sharp fiscal adjustments and, more generally, the rise of *global capitalism* since the 1970s has altered the policy-making environment. Governments are under pressure from multinationals, financial markets, influential IMF reports and Maastricht Treaty criteria, to keep taxes in check, limit budget deficits and reduce national debt.[51] Free movement of capital on an international scale

42 An expression coined in A.M. Okun, *Equality and Efficiency: The Big Trade Off*, Washington DC: Brookings Institution, 1975.
43 Quoted in J. Cullis & P. Jones, *Public Finance and Public Choice*, OUP, 1998, p.255.
44 See C. Sandford, 'Taxing Wealth', in C. Sandford (ed.), *More Key Issues in Tax Reform*, Fiscal Publications, 1995.
45 See, e.g., G. Stark, 'Taxing Families', in C. Sandford (ed.), op. cit. For possible complications associated with transferable allowances, see *Options for 1996: The Green Budget*, IFS, 1995, pp.47–51.
46 See M. Phillips, *The Sex-Change Society*, Social Market Foundation, Paper No. 44, 1999; see Chartered Institute of Taxation Press Release, 'Tax Credits for all?', 24 July 2001.
47 Figures quoted by N. Ferguson, *The Cash Nexus*, Penguin Press, 2001, pp.216–17, and based on L.J. Kotlikoff and B. Raffelheuschen, 'Generational Accounting around the Globe', unpublished paper, 1999.
48 Ibid.
49 N. Ferguson, op. cit.
50 Ibid., p.105.
51 See, e.g., R. Mishra, *Globalization and the Welfare State*, Edward Elgar, 1999.

following the widespread dismantling of capital controls has prompted 'tax competition' under which nation-states seek to attract investment by multi-national corporations by offering a benign tax environment for the corporate sector and senior executives.

New directions?

Public debate, and resulting political action, over whether to increase taxes in order to improve public services, or to limit taxes and reduce the quality or scope of public provision, is feasible. International comparisons reveal significant differences in the scope of the state's responsibilities. So, notwithstanding pressure from an increasingly global economy, democratic institutions are capable of delivering a different public/private balance depending on voter preference and cultural inclinations.

The biblical material suggests that a limited role for the state combined with a range of alternative welfare support mechanisms is desirable. Nonetheless, faced with 'second best' scenarios, a public sector which intervenes in the provision of health and education and engages in redistributive welfare is a crude approximation of the 'support structures' in OT Israel. It may be less bad than an unfettered free market, a hollowed-out welfare state, and limited government. There would be a real danger that certain groups – elderly people without private/occupational pensions, the long-term sick/disabled, and households with no work or low-paid, transitory work – could suffer severe hardship. The belief that free-market capitalism will generate economic growth which will 'trickle down' to improve everybody's lot and 'welfare pluralism' – involving employers, markets and voluntary organisations – will fill the welfare gap has so far proved optimistic. While this strategy may enhance the income levels of the poorest in absolute terms, relative inequality is often more marked and this undermines wellbeing.

Moreover, economic theory highlights a range of circumstances in which free markets will fail to produce 'efficient' use and allocation of resources, and thereby cautions against an extreme version of the 'minimalist' state. Public goods (such as defence) which benefit everyone are a prime example of market failure but problems also arise where, for example, information is inadequate or asymmetric, natural monopolies exist, or 'externalities' apply. Externalities may be benefits (e.g. A's reduced risk of infection if B is inoculated against polio) or costs (e.g. environmental pollution not reflected in the price paid by the consumer). Public utilities, unemployment insurance, pension provision, healthcare delivery and the education sector all suffer from inherent market imperfections. So a degree of government intervention (whether in the form of regulation, taxes/subsidies or public provision) can in principle improve the allocation of resources.[52] On the other hand, taxes impose direct costs and distortions. For every £1 of tax raised, money is spent on compliance and collection. Distortions arise as well because all taxes – other than poll taxes – alter the relative price of different 'goods', affect economic behaviour, and result in what economists call the 'excess burden' of taxation: a concealed welfare cost.

The key point, however, is that the biblical material pushes us towards the conclusion that a one-dimensional debate over whether to increase or reduce taxation and public provision is inadequate. A tussle over taxation levels needs to give way to a multi-faceted policy agenda. It would be premised on some caution about the desirability of expanding the state's role and willingness to explore alternative mechanisms. For much of the twentieth century there has been a widespread – not universal – tendency to look to the state for solutions to social and economic problems. There is, rightly, more awareness of the mixed credentials of the state at the outset of the twenty-first century. Central government may pursue an agenda remote from the best interests of ordinary citizens and, if pervasive in its role, can contribute to the depersonalisation of society. If the role of central government is to be reined in, what else would need to happen?

First, reform of the institutional infrastructure within which capitalist markets operate, nationally and internationally, so that it generates less pronounced inequalities needs to be explored – with particular attention to the markets for land, labour and capital.[53] Secondly, the scope for 'welfare pluralism' can be encouraged by active promotion of intermediate structures between the individual and the state (including the revitalisation of local government and fostering latter-day counterparts to the Friendly Societies) and measures to reinvigorate a sense of civic responsibility on the part of the affluent.[54] Thirdly, ways to provide households with 'economic ballast', preferably in forms which foster opportunities to earn a livelihood, need investigation.[55] A policy agenda of this breadth, if successfully pursued, would allow taxes to be lowered within an economic, social and political environment more consonant with the balance of biblical priorities.

Conclusion

This paper has highlighted a number of directions in which a tax system needs to develop if the biblical priorities we have identified are to be better reflected: an increased share of tax collection by local and/or regional government; a re-evaluation of the tax treatment of married couples and families; a serious attempt to counteract the sustained accumulation of extravagant levels of wealth across generations by some form of wealth taxation. However, this paper has highlighted that tax policy cannot and must not be seen in isolation. It interacts with the vitality of democratic government, the institutional landscape, the operation of the economy and the channels through which welfare is provided. So a paper such as this serves not only as a precursor to consideration of more detailed tax design issues but as a prologue to a wider debate.

52 See, e.g., N. Barr, *The Economics of the Welfare State*, 3rd edn., OUP, 1998.

53 See, e.g., P. Self, *Rolling back the Market*, Macmillan, 2000, chs.7–8.

54 In 1889 Andrew Carnegie, then one of America's richest men, claimed that 'The problem of our age is the proper administration of wealth, so that the ties of brotherhood may still bind together the rich and poor in harmonious relationship', and urged the wealthy to use wealth for 'the common good' by spending it 'for public purposes from which the masses reap the principal benefit'. Quoted in 'A survey of the new rich', *The Economist*, 16 June 2001.

55 See the IPPR's research programme into asset-based welfare.

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