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# Tax freedom for the poor! [1]

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Establishing a higher threshold for personal income tax was under much discussion last month ? a precursor for conference season debate. Under the banner of ?Fairer Tax in Tough Times [3]?, the Liberal Democrats presented plans to increase the scheduled threshold of £9,205 to a suggested rise of £10,000.

Not slow to capitalise on this ?leak?, the Spectator?s blog drew attention to a Centre for Policy Studies report published by Lord Maurice Saatchi and Peter Warburton in 2001, Poor People! Stop Paying Tax! [4], that itself recommended £10,000 at which the low-paid began to pay. For the think tank that Margaret Thatcher and Keith Joseph built, it is absurd that the State ?even taxes people who can?t afford to pay tax at all.? But insult is added to injury:

> *Governments put up tax, which reduces individual incomes and creates more dependence on the state. And citizens claim more state benefits to compensate. And so it goes on until the government is claiming billions of pounds a year in taxes from citizens who also claim billions of pounds a year in benefits from the government.*

This political duel over who is truly the friend of the poor should set off a policy debate on taxes in general; namely, is it better for taxes to be wide and shallow ? that is, paid by everyone, allowing for overall rates to be low ? or narrow and deep ? again, paid by the wealthy few who are considered able to pay them and, necessarily, rather high?

**Establishing the framework of income tax policy**

In the predominant social democratic environment of current debate, the arguments for the latter option are well-rehearsed, and are usually couched in terms of making the well-to-do ?pay their fair share?, if not in the less-benign tone of ?soaking the rich?. But the rationale for the former position is less well-known ? certainly among the leftist intelligentsia ? and so deserves a short hearing. One reason is based on shared solidarity; as Saatchi and Warburton note, ?One of the arguments that is frequently aired is that the payment of income tax or council tax, even at a low level, is a mark of civic responsibility: an acknowledgement of the cost of government services.? Or asMadsen Pirie [5] has written, ?Simple taxes ... make clear the duties of citizenship, and allow people to feel that they are partners with government, making the sacrifices required to enable society to function, and knowing what that involves on their part.? To quote the Prime Minister and his Chancellor, ?We?re all in this together.?

Another reason is based on subtle factors of containing the growth of the State and its entitlement culture: Citizens are more aware of abuse of the public treasury and State-aggrandisement if they bear a portion of the tax burden, less concerned if they personally bear none of the costs ? especially so if they are among

the recipients. ?As long as it is admitted that the law may be diverted from its true purpose,? cautioned Frédéric Bastiat in *The Law* [6], ?? that it may violate property instead of protecting it ? then everyone will want to participate in making the law, either to protect himself against plunder or to use it for plunder.? The aim, then, according to this interpretation of comprehensive income taxes, is to make all citizens conscientious taxpayers, and therefore make everyone invested in good government.

Yet another, a bit esoteric in nature, posits that various business interests gain unfairly from the selective practice of ?tax expenditures? ? a feature spawned from crony capitalism (or ?corporatism?) ? and that if such loopholes were removed, then a truly competitive free market economy would exist, with subsequent lower tax rates for all.

**The socio-economic virtues of income-tax freedom for the poor**

The first taxation policy ? wide and shallow ? has much to recommend it, though with respect to the subject of personal income taxes, the alternative position ? narrow and deep ? may be preferable: Taking those who are low-paid off the income tax register serves the greater common good.

> *Low earners still must pay any number of direct and indirect taxes, whether consumption taxes, property taxes, or National Insurance. They, like all other British taxpayers, know of sacrifice and social solidarity, and thus it cannot be argued they are oblivious of the costs of government to them. They certainly meet the standard as set forth by Adam Smith in The Wealth of Nations: ?The subjects of every state ought to contribute toward the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state (V.ii.b.3[7]).?*

Nor is raising the income threshold necessarily a complete loss to government revenues. Allowing the low-paid to keep more of their salaries is an incentive for increased productivity (which declines when despair and despondency hit the unemployed); furthermore, these new-found earnings may be saved or spent ? both which serve businesses either looking for investment or sales opportunities. Other benefits outlined by Tom Clougherty [8] include eliminating the ?benefits trap? and reducing the size of the ?tax wedge?.

Raising the income threshold by removing the low-paid from the tax rolls also removes many from the welfare rolls, too. ?The most effective way of giving extra income to low earners is not through a cumbersome system of credits and allowances, but by not taxing them in the first place,? wrote Pirie (who envisions a slightly higher benchmark). ?If their money is not taken by government, it does not need a complex bureaucracy to give some of it back to them.?

Some of those earning less than half the average wage find themselves needing benefits only because part of their money is taken in tax. If the threshold at which income tax is levied were raised to half the average wage (which is almost the same as the minimum wage, about £12,000 a year), those earning less than that would not pay it at all. Only income earned above the £12,000 level would come under income tax. This would not only be simpler and more efficient than the present welfare system, it would end most its poverty traps. There would always be an incentive to earn more, for no additional income would bring with it a reduction in benefits. Even above £12,000, people would only pay the basic rate on each pound earned above it, and none at all on the first £12.000. The incentive would always be there to earn more if people could.

Bastiat foresaw the adverse consequences of these traps: ?The present-day delusion is an attempt to enrich everyone at the expense of everyone else; to make plunder universal under the pretence of organising it.? Tax-credit and tax-benefit policies, however well-intentioned, have become perverted and

often serve as barriers to advancement and independence for those whom they were intended to help.

**Curbing a ravenous government of its revenue dependency**

Need it be said that a preference for personal income taxes that are narrow and deep is not an endorsement for wild abandon? (And by ?deep?, what is connoted are taxes which are ?deeper? in comparison to those applied to the poor.) Smith anticipated Laffer Curve findings which suggest that higher taxes do not unquestioningly entail enhanced revenue streams (see quotation below) ? not to mention the moral issues involved with the gratuitous confiscation of private property. Both Pirie and Clougherty, as well as Saatchi and Warburton, emphasise that a significant cause for generating ever-more revenue to fund expenditures has been the unprecedented growth of the Welfare State ? of which tax reallocations form a part.

Though it has become a cliché among conservative circles, it is no less true that most Western democracies don?t suffer from too few taxes, but rather from too much spending.

These effects of over-government affect all taxpayers and, along with providing tax relief for the poor, should constitute a major reform of government policy. Smith?s eighteenth-century standard for taxation is as relevant now as then:

> *Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the publick treasury of the state. A tax may either take out or keep out of the pockets of the people a great deal more than it brings into the publick treasury, in [that] ... it may obstruct the industry of the people, and discourage them from applying to certain branches of business which might give maintenance and employment to great multitudes. [...] It is in some one or other of these ... ways that taxes are frequently so much more burdensome to the people than they are beneficial to the sovereign (V.ii.b.6[7]).*

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