ABSTRACT

Research in taxation often treats it as a branch of law or economics, but in this thesis I argue that this obscures the fact that tax systems are not based on scientific, techno-rational principles, but are socially constructed phenomena, embodying fundamental, value-based decisions imbricated in power relationships. I demonstrate that throughout history tax systems have reflected the prevailing state form and the dominant power relationships underpinning them and that we are currently living in a neoliberal state, in which societal relations are determined by economic principles.

I therefore argue that the UK tax system tends to be utilized to encourage individuals to engage in economic, entrepreneurial activity and are presented as being governed by techno-rational, economic principles, but are, in fact, a rationalizing discourse for the transfer of power from labour to capital and from poorer to wealthier taxpayers. This transformation is underpinned by the exercise of power, but in a neoliberal state power operates in a covert, capillary fashion through assemblages and the construction of knowledge, rather than in an overt, hierarchical fashion.

I demonstrate how the contemporary debates relating to tax simplification and the use of general principles rather than detailed rules in tax legislation have been, or might be, used to further entrench neoliberal values in the tax system, but that the failure to achieve significant simplification due to its open and transparent nature demonstrates the limits of power and the more opaque

nature of general principles might have more potential for achieving this. However, no power can be absolute and I argue that the increased public interest in and awareness of taxation since 2010, which led to the emergence of UK Uncut, demonstrates that there is always the potential for resistance to a hegemonic discourse, which may lead to the emergence of alternative discourses.

TABLE OF CONTENTS

ABSTRACT i
ACKNOWLEDGEMENTS v
SUMMARY OF ABBREVIATIONS vii
CHAPTER 1: INTRODUCTION 1
1.1. The Lessons of History 1
1.2. Tax Policy – The Big Choices 4
1.3. A Conceptual Framework of Power 8
1.4. Taxing Questions 13
1.5. Outline of the Thesis 15
CHAPTER 2: GENESIS OF THE THESIS 27
CHAPTER 3: THEMES AND CONCEPTS 35
3.1. Introduction 35
3.2. Why and How Governing Regimes Levy Taxation 35
3.3. Power – a Conceptual Framework 42
3.4. The Evolution of the Neoclassical Paradigm of Taxation 56
3.5. Summary 81
CHAPTER 4: STATE FORMS AND TAXATION 83
4.1. Introduction 83
4.2. The Feudal State and Its Decline 85
4.3. Taxation in the Liberal State 95
4.4. The Rise of Welfarism 102
4.5. The Welfare State 111
4.6. Summary 117
CHAPTER 5: THE NEOLIBERAL STATE 119
5.1. Introduction 119
5.2. The Nature of the Neoliberal State 120
5.3. The Construction of the Economic State 130
5.4. Summary 141
CHAPTER 6: TAXATION IN THE NEOLIBERAL STATE 143
6.1. Introduction 143
6.2. Taxation in the Neoliberal State 144
6.3. Getting People to Work – the Taxation of Labour 148
6.4. Lightening the Load – the Taxation of Capital 167

6.5. The 10p Tax Controversy – the Unmasking of Power 180
6.6. Summary 192
CHAPTER 7: TAX SIMPLIFICATION – THE LIMITS OF POWER 197
7.1. Introduction 197
7.2. Calls for Simplification and Responses to Proposals 198
7.3. Barriers to Simplification 207
7.4. Summary 229
CHAPTER 8: RULES AND PRINCIPLES 233
8.1. Introduction 233
8.2. The Nature of Rules and Principles 235
8.3. Rules and the Operation of Power 242
8.4. Tax Avoidance and the Construction of Certainty 262
8.5. Principles and Power 272
8.6. Summary 284
CHAPTER 9: THE SHOOTS OF RESISTANCE 287
9.1. Introduction 287
9.2. Discretion, Accountability and Power 288
9.3. Troubling Cases 303
9.4. Summary 322
CHAPTER 10: CONCLUSION 327
10.1. Introduction 327
10.2. Questions Addressed 327
10.3. Arguments Advanced 329
10.4. Contribution Made 341
BIBLIOGRAPHY 345

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SUMMARY OF ABBREVIATIONS

CFC – Controlled Foreign Companies

CGT – Capital Gains Tax

EPD – Excess Profits Duty

EPT – Excess Profits Tax

FSB – Federation of Small Businesses and the Self-employed

FYA – First Year Allowances

GAAR – General Anti-avoidance Rules or General Anti-abuse Rule

HMRC – HM Revenue & Customs

IFS – Institute of Fiscal Studies

NAM – National Association of Manufacturers

NGO – Non-government organizations

OTS – Office of Tax Simplification

PAC – Parliamentary Accounts Committee

PAYE – Pay As You Earn

PFI – Private Finance Initiative

RPI – Retail Price Index

VAT – Value Added Tax

CHAPTER 1: INTRODUCTION

1.1. The Lessons of History

When plunder has become a way of life for a group of men living together in society, they create for themselves in the course of time a legal system that authorizes it and a moral code that glorifies it.

(Bastiat 1845 II.1.11)

In 1381 Wat Tyler led a march on London in protest at the imposition of a poll tax by the king, Richard III. This became known as the Peasants' Revolt, although some of the marchers were traders and craftsmen rather than peasants. Whilst on their way into London they captured and beheaded the Archbishop of Canterbury, but the protesters' success in getting their central grievance addressed was limited. They presented a petition to the king, who promised to consider it. When Wat Tyler subsequently went to speak to the king personally, he was attacked by a group led by the Lord Mayor of London and died of his injuries (Dunn 2004).

Some 600 years later in 1990, there were widespread protests against the imposition of a tax officially known as the Community Charge, but popularly termed the 'poll tax' because it was similarly levied per head of the population. There were many incidents of civil unrest, one of the biggest taking place in Trafalgar Square in March 1990. Unlike their 14th century counterparts, these protesters could claim tangible victories; the protests were a major factor in the resignation of Prime Minister Margaret Thatcher later that year and the Community Charge was abolished in 1992. It was replaced by the Council Tax, which contains both a personal element and a property element and is therefore

closer to the Community Charge's predecessor, domestic rates, which was a property-based tax.

These two protests against similar taxes, albeit 600 years apart, cannot be dismissed as isolated incidents; throughout history, and in many countries, there have been protests against unpopular taxes. One of the earliest resulted in the signing of Magna Carta[1]. Although it is now widely seen as a watershed in the development of the rule of law, this charter was originally intended to address specific financial grievances of the barons regarding the payment of various feudal dues which had the nature of taxes, even if they were not described as such (Frecknall-Hughes & Oats 2007). The Boston Tea Party of 1773, a major catalyst of the American Revolution, was a protest against the imposition of excise duty on the import of tea, which was designed to protect the monopolistic position of the East India Company (Boden 2012). Resentment at the imposition of unpopular taxes, such as the salt tax, was also a major factor in the French Revolution (Frecknall-Hughes 2015).

Such examples demonstrate the preparedness of citizens to actively resist the imposition of taxes which they consider to be unjust. This may be because taxation is a direct and overt nexus between the state and its citizens (Boden et al. 2010), where the relationship can be characterized as 'the obligation to contribute money or goods to the state in exchange for nothing in particular' (Martin et al. 2009:3). The sacrifice required of citizens in the payment of tax can be distinguished from other types of sacrifice required by the state, such as

[1] An agreement signed between King John and feudal barons at Runymede in 1215.

compliance with its traffic laws or military conscription. Money raised by taxation is fungible and makes most or all of the state's activities possible, rather than merely one, and the more extensive the activities of the state, the greater its reliance on taxation (Martin et al. 2009). Furthermore, the transfer of income or wealth to the state through taxation results in an immediate financial loss to a citizen and the effects of any increase (or decrease) in taxation are therefore felt immediately and directly.

The fact that tax is at the nexus of relations between citizens and the state and that citizens can be prepared to actively resist taxes which they feel to be unjust suggests that taxes may only be imposed if there is a broad, general consent, or at least acquiescence, and this is only likely to achieved if there is a consensus that they are fair. If the characteristics which make a tax appear fair were simple and self-evident there might be little controversy. However, in this thesis I argue that taxation is a complex socio-political phenomenon which embodies many subjective choices. This suggests that the process by which this consensus is arrived at has a discursive dynamic and that tax policy, the basic underlying aims and design of any tax system, reflects the result of this process. This thesis therefore aims to explicate the dynamics which underlie the discursive construction of tax policy, and, in the following section, I set out the fundamental tax policy choices which must be made and the ways in which interested parties might influence this debate through the exercise of their power. Power need not be exercised overtly through legitimate authority or coercion and is at its most complete and effective when it is exercised covertly,

thus making it less visible and I set out a conceptual model for analyzing the operation of power in section 1.3.

1.2. Tax Policy – The Big Choices

At its most basic, taxation is a process through which the government appropriates money or assets from and distributes the revenue collected to its citizens. The distribution of revenue may either be through direct payments, such as social welfare benefits, or, more indirectly, through the provision of public services, such as education, health or transport infrastructure. The first choice which must be made is the extent of the role of the state in civil society, which drives the amount of expenditure necessary to finance this role and which, in turn, determines the level of taxation necessary. This question can be posed in reverse by determining whether, and the extent to which, it is legitimate for the state to appropriate the income and assets of its citizens, which will determine the extent of the role of the state.

Libertarians such as Nozick (1973) consider that individuals are entitled to make their own choices concerning how they dispose of their income and assets and that taxation is an infringement of this right by the state. They regard taxation as a confiscation of income or assets by the state akin to forced labour, and are therefore only prepared to concede the state a very limited role in fulfilling basic functions which cannot realistically be provided by individuals, such as national security and law and order. Libertarians assert that services such as healthcare and education should be provided and financed privately. Consequently the necessary level of taxation will be commensurately low.

If the role of the state is limited and functions such as education and healthcare are to be financed individually by taxpayers, the quality of service which they receive will be determined by the amount they can afford, or are willing, to pay. If these services are provided by the state, financed through the taxation system, individual taxpayers' contributions may be determined by their financial capacity, but the benefits may be allocated according to some notion of merit or need (which might themselves be discursively constructed). Wealthier taxpayers might therefore favour limiting the role of the state, thereby limiting the provision of these services to poorer taxpayers. This may have the effect of entrenching and perpetuating their privileged position. Conversely, poorer taxpayers are likely to favour a much more extensive role for the state in order to maximize their life chances and participate in society on a more equal footing.

Once the extent of the role of the state and the total amount of tax revenue needed have been determined, the next logical questions are who should pay tax, how much tax revenue different groups should be required to contribute, and the amount of benefit each group should receive in return. If the level of taxation is modest these choices are relatively unimportant because the amount of money individuals are required to pay is low and government expenditure will be largely restricted to items such as national security and law and order, from which all taxpayers might benefit in roughly equal measure. Whilst conflicts concerning the distribution of the tax burden may arise whatever the level of taxation, these may assume greater importance when there is a high level of taxation and commensurate government expenditure.

A closely related choice is the extent to which the taxation system should be used to redistribute wealth between different groups within society. This might usually be a redistribution of wealth from wealthier to poorer groups, but could be redistribution from poorer to wealthier groups or between different groups of roughly equal wealth, but different demographic characteristics. If wealthier taxpayers are able to negotiate a tax system under which they contribute no more, or only a little more in absolute terms, than poorer taxpayers whilst receiving an equal, or even greater amount of benefit, there will be a limited redistribution of wealth. Similarly, poorer taxpayers can maximize their life chances by ensuring that wealthier taxpayers contribute significantly more.

Whatever level of taxation and whatever combination of taxes is chosen, public funds are always a finite and hence scarce resource. There will always be competing priorities for funding and the allocation of public funds always involves the exercise of subjective choice. For example, one way of allocating public funds is to directly allocate them to people through welfare benefit payments, tax credits or tax concessions and choices must be made concerning the level of such expenditure and individuals or groups to whom it will be paid. Decisions as to what proportion of tax revenue the government should spend on different areas are choices which reflect hegemonic priorities and different priorities might benefit different sections of society. For example, in an interview shortly after taking up his appointment as chief conductor of the Berlin Philharmonic Orchestra in 2002, Sir Simon Rattle claimed that the city of Munich spent more on subsidizing the arts than the whole of Great Britain

(Rattle 2002), which was for him indicative of the importance Germany placed on the arts and, more specifically, *Kultur*, i.e. ‘highbrow’ music and theatre.

Where expenditure only benefits or taxes are only payable by specific groups narrow self-interest would not lead the majority of taxpayers to support them. For example, most social welfare payments are only made to a minority of citizens, many of whom may not be taxpayers. Similarly, subsidies for the arts may well be for the direct benefit of a minority of citizens, although the indirect benefits may be more widely felt. The majority of taxpayers who contribute to these benefits might therefore be expected to oppose them if they are taken in isolation. However, a taxation system will reflect many different priorities and taxpayers will give their consent if the system, taken as a whole, is seen to balance the interests of different groups (Martin et al. 2009).

History suggests that broadly fair tax systems are highly desirable, but the process by which this consensus is arrived at is a complex one. I have set out the choices inherent in tax and a major motivation is my concern that taxation has traditionally been regarded as a branch of either black letter law or orthodox economics, which may ignore or even deny the subjective nature of tax. In reality, taxation is heterogeneous and a product of states, cultures and politics and this thesis explores the complex dynamics of the debates which inform this process.

Taxation is a fruitful lens through which to analyze relationships between individuals and the state since history has shown that there is a longstanding

power relationship between rulers and subjects, which is articulated through tax regimes (Boden 2012). Tax can therefore be seen as a technology which mediates such tensions and relationships and the way that choices are made and conflicts are resolved can give valuable insights into societal power relationships. For example, in the example given by Rattle (2002), it may be debatable whether the decisions to allocate scarce funds to subsidizing the arts indicate the priorities of society in general or merely the priorities of those with the power to make decisions.

This thesis analyzes the discourse[2] which generates tax policy in terms of the power relationships between different groups in society, but the ways in which power can be deployed are not necessarily overt and the following section explores a conceptual framework of power which encompasses the various ways in which it may be exercised.

1.3. A Conceptual Framework of Power

The imposition of taxation involves the exercise of power, the most overt example of which is the power of the state to compel taxpayers to pay their tax liabilities. However, as I have argued, in order to compel taxpayers to pay without giving rise to mass resistance or worse it is necessary to obtain consent through a consensus that the tax system is broadly fair. Taxation involves many subjective choices and the concept of fairness is discursively constructed and the manner in which these debates are conducted can be influenced by the exercise of power.

[2] A domain of language use that is unified by common assumptions (Abercrombie et al. 1988:71)

The most explicit means of exercising power is brute force. However, as I suggested in chapter 1.1., this is usually of limited use in raising taxes. Not only might it incite popular unrest, but it is also costly and impractical for the state to intimidate or coerce large numbers of taxpayers. States might therefore be expected to use less direct means to secure the consent of those that they govern in order to impose taxes. Boden (2012) argues that, whilst the power to coerce citizens to pay tax or to impose sanctions on those who do not are the most overt manifestations of power, it may also be exercised in more covert ways and draws on Lukes's (2005) three dimensions of power as a theoretical framework.

The first dimension of power is the ability to force a person to act in a way in which they would not otherwise act by using legitimate authority, coercion or intimidation. In the field of tax, the legitimate authority of the government to collect taxes, compel taxpayers to make disclosures about their financial affairs in order to raise an assessment and to impose sanctions on those who fail to comply with their obligations are examples of the first dimension of power. Similarly, in a society not governed by the rule of law, the ability to make arbitrary assessments backed up by the threat of force is also an example of the first dimension of power. The first dimension is overt and, if this were the only means of wielding power, it would not be necessary to analyze it at any length to understand its operation as it would be amenable to positive observation. Such views of power have limited explanatory potential, Lukes (2005) argues, because they rely purely on directly observable phenomena.

The second dimension of power is the power to mobilize bias such that certain topics are able to be discussed and decided upon, whilst others are excluded. Dominant groups may therefore ensure that, whilst there is a genuine element of choice in debates, the only issues which can be seriously discussed and the only solutions which can be seriously considered are those which do not threaten their hegemony. Other issues and solutions may be discussed, but might be dismissed as unfeasibly utopian, or even mad, and therefore not considered seriously (Foucault 1981 [1969]) and individuals and groups, such as political parties, may self-censor in order to avoid ridicule. In the context of taxation this might mean that serious discussion of the redistribution of wealth to poorer members of society is inhibited, although hegemonic groups may be prepared to accept a limited amount of redistribution, provided that it does not seriously undermine their position.

Whilst in the second dimension of power individuals and groups may be aware of a variation between their interests, in the third dimension individuals are unaware of any variation, because power is wielded by hegemonic groups in such a way that they can discursively frame beliefs and ideologies such that others believe that their interests are congruent with those of the hegemonic group. At its most effective, groups might have so thoroughly internalized the dominant paradigm that they are unable to conceive of any realistic alternatives to it (Gramsci 1971).

Lukes (2005) acknowledges that the third dimension of power presents an intractable problem in that it is only possible to analyze its successful operation

by removing yourself from society and viewing it from the outside. If a society has been constructed so as to serve the interests of the dominant ideology, those inside it who are subservient will be unaware of the hidden power which keeps them in their place. They therefore have a 'false consciousness' and believe that they are free moral agents, holding views as a result of free will.

In the second and third dimensions, power operates very differently from the first. The first dimension is overt, but it also operates in a top-down hierarchical manner. For example, in the area of taxation, HM Revenue & Customs (HMRC) has the power to compel individuals to pay tax and make disclosures about their financial circumstances simply by virtue of the legal powers vested in it by statute and there is a clear power flow from HMRC to taxpayers. In the second, and particularly in the third, dimensions, power arises from the interaction of a network or assemblage[3] of actors comprising, for example, quangos, international organizations and large corporations and in which the government is simply one actor (Foucault 1979 [1975]; Dean 2010). Power therefore flows in a capillary manner between the various actors, which makes resistance more difficult because it is only possible to attack one small part of the assemblage.

In this thesis I argue that the orthodox economic approach that underpins much of the knowledge about tax is an example of the third dimension of power. It creates knowledge about the future consequences of present actions and decisions, which can attain a hegemonic status not by persuading taxpayers that certain outcomes are necessarily fair, but that they flow inevitably from

[3] A collection of persons or things (Chambers 1988)

particular decisions. It is not possible to conduct controlled experiments in the social sciences, including economics (Blaug 1997), therefore the consequences of alternative courses of actions will remain unknown. They also exploit inherent uncertainties to persuade taxpayers that these outcomes are either beneficial to them or the least of evils, with any alternatives inevitably having less favourable consequences (Murphy & Nagel 2002).

However, in order to gain acceptance, a particular form of knowledge must establish itself as more plausible than the alternatives, and this may be influenced by the social, cultural and intellectual capital of those putting forward the arguments. The protagonists in the debates are often not neutral, but are putting forward arguments which further their own interests, which are not fixed and immutable but are discursively constructed (Daunton 2007). They can therefore exert power through their capitals to construct knowledge in a way which benefits them.

In this thesis I argue that powerful groups therefore use the techno-rational, economic paradigm of taxation as a rationalizing discourse to mask the operation of power and to discursively construct tax systems to their own advantage. This paradigm is used as a rationalizing discourse by presenting tax policy as objective and governed by techno-rational principles, which therefore, purportedly, removes any element of choice and prioritizes the economic over the social domain.

Using economics to construct knowledge around a techno-rational paradigm of taxation which favours powerful groups might be an example of the second dimension of power if other groups accept it grudgingly as the least of evils or of the third dimension of power if the paradigm has become so hegemonic that they cannot conceptualize any alternative (Gramsci 1971). However, dominant groups may also construct a normative knowledge which supports the techno-rational paradigm and underpins their dominance. If other groups accept and internalize the normative knowledge, this will also be an example of the third dimension of power.

1.4. Taxing Questions

In chapter 1.2. I argued that taxation is not simply the product of a set of techno-rational rules, but rather is determined by many subjective decisions concerning the allocation of resources between different groups in society. These decisions are subjective and involve the operation of power, which may operate in either an overt or a covert manner.

Accordingly the principal research question addressed in this thesis is *how, in a neoliberal state, are power relationships between citizens and the state mediated through taxation and what are the consequences for tax policy?*

With regards to taxation, formal relationships between citizens and the state are strictly bilateral and confidential. For example, individuals must make a return of

their income and the state will assess them accordingly. However, the formulation of tax policy involves multilateral relationships and public debate and discussion as actors combine into social groupings of various sorts in order to express their preferences. The state is not necessarily a neutral institution in such multilateral relationships and certain social groupings might assume a hegemonic position, thus exerting power through the state by ensuring that it serves their interests at the expense of the interests of other social groupings.

In order to answer this question I will address three subsidiary questions:

My first subsidiary question is: *what strategies might be deployed in the formulation of tax policy in order to achieve the exercise of power?*

The exercise of power in the formal bilateral relationships between citizens and the state is structural and largely hierarchical, but this can be frustrated by violent or civil disobedience or deceit. However, the formulation of tax policy in the first place involves capillary flows of power through numerous social actors. Tax policy is therefore the product of these networked social relationships and the strategizing of various social groups.

My second subsidiary question is: *what are the factors which might inhibit the exercise of power in the formulation of tax policy?*

In multilateral networks power is capillary and, as such, its exercise is subject to restraint and inhibition. This question will therefore allow the exploration of the factors which limit the exercise of power.

My third subsidiary question is: *given that tax policy is discursively framed, how might counter-hegemonic discourses challenge and supplant dominant paradigms?*

This question addresses how resistance to the operation of power in the formulation of tax policy might arise and how it can be effective in creating new tax regimes.

1.5. Outline of the Thesis

The thesis argues that tax systems have always reflected the dominant power relationships within the state and between the state and its citizens. I advance the argument that the UK exhibits many of the characteristics of a neoliberal state. The state has now become simply one actor in an assemblage which includes other bodies such as corporations and quangos to which it has ceded power. Instead of exercising power overtly in a hierarchical fashion it now does so covertly through indirect means. One of the principal means of exercising indirect control is through economic knowledge and the neoliberal state is an economic state in which the economic domain is prioritized over the social and moral domains.

The tax system is therefore constructed and legitimated through the principles of neoclassical economics, which gives it the appearance of being a value-free, techno-rational set of rules. I further argue in contradistinction that it is a means of enforcing neoliberal ideology by disciplining taxpayers to undertake work and entrepreneurial activity and by transferring resources to capital.

I argue that constructing the tax system according to neoliberal principles undermines notions of justice and social equity and I critique the economic rationale of taxation and unpack the power relationships which underpin it. However, power is never absolute and I explore the possibilities for the re-democratization of tax policy formulation and the reassertion of different forms of power relationships.

The rest of this thesis consists of the following chapters.

Chapter 2

This gives a brief description of how the thesis developed from my long-term thinking about the normative values and principles which underlie tax policy and therefore the detailed rules which make up tax law and practice. This thinking also influenced my epistemological approach, which views tax policy as being subjective, inherently value-laden and discursively constructed through the exercise of power.

Chapter 3: Themes and Concepts

Chapter 3 sets out three principal arguments: that tax policy formulation is inherently subjective; that notions of power need to be theorized in order to

understand these subjective choices; and that in current times neoclassical economics determines the nature of the knowledge/power nexus. In chapter 3.2. I discuss why it is necessary for states to levy taxation. In order to avoid the fate described by Hobbes (2015 [1651]) of living in a state of perpetual warfare it is necessary for individuals to live in some form of organized society, which has generally been some form of state. These need organizing structures and therefore require revenue from their members in order to function. However, the extent of their functions and the ways in which the revenue is to be raised must be negotiated and the manner and outcomes of this process of negotiation are influenced by the exercise of power by various groups.

Power may be exercised in a number of ways in the negotiation process and chapter 3.3. therefore discusses Lukes's (2005) three dimensions of power as a framework for exploring and analyzing this process and considers the ways in which the second and third dimensions of power operate in practice. The third dimension of power is one where constructed knowledge is a primary force. Therefore in chapter 3.4. I demonstrate that the knowledge which underpins the neoliberal state and its taxation system is a set of constructs derived from neoclassical economics through the reinterpretation of Adam Smith (2015 [1776]) and the economic models of Ricardo (1815), the marginal analysts and Hayek (1944), which are based on contestable assumptions. However, the consideration of economics literature is deliberately limited to discussion of concepts which underpin my discussion in later chapters.

Chapter 4: State Forms and Taxes

In chapter 4 I argue that throughout history taxation has reflected the dominant power relationships in society. In chapter 4.2. I demonstrate that the tax system in the English feudal state of the 12th and 13th centuries, rudimentary as it was, was essentially a system of tribute in which feudal dues were paid to the sovereign by virtue of their social position. However, the power of the sovereign was not absolute and the signing of Magna Carta in 1215 was an early example of resistance against tax systems which were perceived as inequitable.

Whilst the signing of Magna Carta did not seriously challenge the established order, the Black Death of the 14th century and the rise of the mercantile class from the 15th century onwards presented a much more substantial threat and the feudal state went into a slow decline until the Industrial Revolution, out of which emerged the liberal state which held sway until the middle of the 20th century.

In chapter 4.3. I argue that the liberal state was a pragmatic compromise between the landed aristocracy and the newly emergent industrial bourgeoisie in which the aristocracy retained political power whilst ceding power over the economy and many other aspects of civil society to the bourgeoisie. The liberal state was therefore a constrained state and the tax system largely reflected the bourgeoisie's priorities and interests with the result that indirect consumption taxes became politically unacceptable and the general level of taxation remained low.

However, just as the rise of the mercantile class threatened the aristocracy, in the late 19th and early 20th centuries the rise of organized labour threatened the power of both the aristocracy and the bourgeoisie. In chapter 4.4. I demonstrate that, partly in response to this threat and partly for pragmatic reasons, the state increased its role in society by providing, for example, education and pensions and instituting measures to alleviate poverty. The level of taxation therefore rose substantially in order to finance this. This reached its zenith in the Welfare State of the decades after World War II and in chapter 4.5. I analyze the ideological shifts which led to its foundation, the highly redistributive tax system with high marginal rates of taxation which sustained it and the economic and social forces which emerged in the 1960s and 1970s which led to its demise, paving the way for the emergence of the neoliberal state.

Chapter 5: The Neoliberal State.

In chapter 5 I explore and critique the relationship between individuals and the neoliberal state and the economic knowledge underpinning it. In chapter 5.2. I argue that, like the liberal state of the 19th century, the formal role of the state is constrained and it has divested itself of many functions through the privatization of nationalized industries and the establishment of numerous quangos.

However, unlike its predecessor, the neoliberal state has not relinquished control over citizens, but seeks to exercise control through indirect means of coercion. The state does not therefore exercise power in a hierarchical fashion, but becomes simply one actor in an assemblage consisting also of quangos and large corporations in which power flows in many different directions in a

capillary fashion. It also exercises power through economics and I argue that the neoliberal state is an economic state, a key aim of which is the transfer of resources to capital. In the neoliberal state the economic domain has been divorced from the social domain with precedence being given to the former and the neoliberal state therefore uses economic rationales to incentivize individuals to undertake economic activity and put themselves at the service of capital.

In chapter 5.3. I argue that the neoliberal state did not simply emerge as a pragmatic response to the economic problems of the 1970s, but that it always had an ideological purpose, which was the wresting back of power by capital and, in particular, large corporations from labour. This was evident from the opposition of the National Association of Manufacturers (NAM) to President Roosevelt's New Deal in the 1930s in the USA and the founding of the Mont Pélérin Society in 1947 and one of the key texts was Hayek's *The Road to Serfdom* (1944) in which his opposition to the prevailing post-war ethos of welfarism and interventionism was primarily ideologically motivated

Chapter 6: Taxation in the Neoliberal State.

Chapter 6 explores and critiques the features of a tax system which one might expect to find in a neoliberal state and demonstrates that over the last 35 years the UK tax system has been reformed so as to correspond far more closely with these rationales. In chapter 6.2. I argue that in a neoliberal state the taxation system becomes a key component of economic policy and a means of Foucauldian discipline and control in which individuals are incentivized to put themselves at the service of capital.

In chapter 6.3. I demonstrate that income tax has become much less progressive since 1979 through substantial cuts in the rates of tax payable by high earners. Coupled with increases in the rates of more regressive taxes such as national insurance and value added tax (VAT) this has substantially shifted the tax burden to poorer taxpayers. This has been justified by the theory that in order to incentivize taxpayers to work it is necessary to tax poorer taxpayers more and high earners less. However the empirical evidence is contestable and I argue that this is a rationalizing discourse for transferring resources to wealthier taxpayers.

In chapter 6.4. I argue that the interests of capital have been favoured through substantial reductions in the rate of corporation tax. In the 1980s these were justified by the need to incentivize taxpayers to undertake entrepreneurial activity and they were also accompanied by a broadening of the tax base through the abolition of first year allowances (FYA). However, by the 1990s the increased international mobility of capital meant that the justification had changed to the need for the UK tax system to be internationally competitive and these cuts were accompanied by a narrowing of the tax base through, for example, exempting foreign dividends from UK corporation tax.

The chapter concludes in 6.5. with an account and analysis of the controversy surrounding the abolition of the 10p tax rate in 2008. This illustrates how government policy really was motivated by a techno-rational paradigm of taxation and was a real-life demonstration of its flaws and the concessions

extracted from the government also demonstrated that successful resistance was not futile.

In this chapter I analyze how the UK tax system has been reformed over the last 35 years in accordance with neoliberal principles, but in the following two chapters I examine two contemporary debates to explore the strategies deployed to exercise power in tax policy formulation.

Chapter 7: Tax Simplification

In chapter 7 I take the issue of tax simplification and explore how it reveals the operation of power, in particular the adoption of some form of the flat tax. In chapter 7.2. I demonstrate that there have been many calls over the years to simplify the tax system. Many of these (e.g. Avery Jones 1996; Freedman 2004) appear to have had no motive other than simplification, but others, including proposals for a flat tax, have had a more explicit ideological motive of reducing the role of the state (e.g. Sastry & Nugent 1998).

However, radical simplification remains elusive since it has not proved possible to mobilize support and there is often resistance to proposed simplifying measures on the grounds that they are inequitable. This suggests that the second dimension of power is inadequate for this purpose and in chapter 7.3. I examine the reasons for this. I identify an opposition between simplicity and equity and argue that taxpayers will generally prioritize equity over simplicity where inequity impacts them negatively because they bear the full cost of inequity whilst enjoying only a fractional part of the benefit of greater simplicity.

Furthermore, since proposals for simplification need to be specific, groups of taxpayers are always able to calculate the effect of these on them personally and on other taxpayers. It is therefore difficult to mislead taxpayers in these circumstances. In particular, if a version of the flat tax is seriously proposed, it will quickly become apparent that this will result in a transfer of resources to wealthier taxpayers and is likely to provoke resistance.

Chapter 8: Rules and Principles

In chapter 8 I discuss the debate about the use of detailed rules versus broad principles, including some form of General Anti-avoidance Rule (GAAR), in the formulation of tax law in order to examine whether the latter might have greater potential to transfer resources to capital. In chapter 8.2. I argue that both rules and principles are inherently indeterminate and that their application to specific situations often involves the use of judicial discretion. However, whilst the indeterminacy of principles is overt, with rules this is concealed behind a techno-rational, objective façade and the construction of legal certainty through the *post hoc* rationalization of judicial decisions is the operation of Lukes's (2005) third dimension of power.

In chapter 8.3. I demonstrate the indeterminacy of rules by analyzing a number of cases in which the decision appears surprising and contrary to the meaning of the legislation. It is notable that most of these cases were decided in favour of the tax authority and, whilst some might be considered simply as curiosities, others appear to have been motivated by a desire on the part of the judge to force the taxpayer to pay tax and thus transfer resources to the state.

These two sections illustrate that certainty in the meaning of the law is unattainable, but in chapter 8.4. I argue that this inherent, but hidden, uncertainty can be exploited for the purpose of tax avoidance. The rationale for this rests on the twin principles of libertarianism, which holds that taxation may only be levied if its scope and amount is certain, and legal formalism, which holds that the law contains an objective truth, and powerful taxpayers can exercise power through lobbying to ensure that this 'truth' is constructed so as to favour their interests and legitimate tax avoidance.

However, the fact that five of the six cases analyzed in chapter 8.3. were decided in favour of the tax authority demonstrates that it is no foregone conclusion that judges will rule in favour of powerful taxpayers and an independent judiciary might therefore be a barrier to the transfer of resources to capital. In chapter 8.5. I therefore discuss whether moving to principles-based legislation might indeed facilitate tax avoidance. Unlike rules, the discretion and uncertainty inherent in principles is overt and principles-based legislation may therefore be most effective in counteracting tax avoidance if this uncertainty is used to persuade taxpayers to self-regulate their behaviour and not devise tax avoidance schemes for fear that HMRC can disallow them too easily. However, taxpayers may demand greater certainty and this might eventually be provided by judicial adjudication, with the result that the principles evolve into a set of rules which can be navigated for the purpose of tax avoidance. Certainty might also be provided through the issue of extra-legal guidance. This is a vehicle through which the third dimension of power can be exercised, since it is subject to less democratic scrutiny than legislation and is therefore more susceptible to

lobbying by powerful interests. I use the recent issue of guidance concerning the operation of the recently enacted GAAR in the UK to demonstrate how legislation which will ostensibly substantially restrict the scope for tax avoidance might in fact permit it to continue largely unhindered.

Chapter 9: Shoots of Resistance

In chapter 9 I examine the rise of UK Uncut in late 2010 in order to examine whether and how principles of social justice might reassert themselves in the tax system. I also assess the significance of the judicial review successfully petitioned for by UK Uncut into the decision by HMRC to forgive £10m of interest payable by Goldman Sachs on the late payment of national insurance contributions arising from a failed avoidance scheme. Whilst the previous chapters might strike a pessimistic note by arguing that the majority of taxpayers are being manipulated by an elite into consenting to a tax system which exploits them, in my final chapter I explore Lukes's (2005) argument that power can never be absolute. I use the rise of UK Uncut, to explore the potential for more sustained resistance to the techno-rational paradigm of taxation and the exercise of power by an elite.

In chapter 9.2. I argue that in a neoliberal state hegemonic groups of taxpayers form part of the same assemblage as HMRC and exert power through a combination of economics, ideology and the principle of taxpayer confidentiality, since the last of these should, in theory, prevent knowledge of how power is wielded becoming public. Since HMRC requires a substantial degree of administrative discretion in order to function on a day to day basis, these

taxpayers might therefore be able to use their power to secure favourable treatment. However, as part of the government, HMRC is conflicted since it is not only part of a neoliberal assemblage of power, but is also visible, and therefore accountable, to the general public. If allegations of favourable treatment of powerful taxpayers should become public knowledge, this conflict could be exploited through public pressure to hold HMRC accountable for the way in which this discretion is applied.

In chapter 9.3. I therefore use the challenge by UK Uncut as a case study to demonstrate that, although they lost the judicial review, they succeeded in exposing the normally hidden operation of power. This may therefore have an effect on public opinion which might in the longer term lead to a change in the dominant paradigm of tax policy.

Chapter 10: Conclusion

In chapter 10 I draw some conclusions from the discussions in the preceding chapters.

CHAPTER 2: GENESIS OF THE THESIS

A PhD thesis is a major undertaking, requiring a commitment of a number of years, particularly when it is undertaken part-time and must therefore be balanced with other work and family responsibilities. It therefore requires a high degree of motivation, which means that the topic of the thesis, the epistemological approach and the manner in which the research is carried out must all stem from the personal interests of the researcher. In this chapter I therefore set out how my interest in researching in taxation as a branch of the social sciences and, more specifically, in the role of power in the formulation of tax policy arose.

After graduating from Bristol University with a degree in German I entered the accountancy profession, training with Touche Ross (now Deloitte). It was during my training contract that I was first attracted by the intellectual challenge of taxation, seeing it as a set of complex rules which first needed to be mastered and applied, but which thereafter gave scope to be used more creatively. After qualifying I worked for several accounting firms, including KPMG, before deciding that my true vocation lay in lecturing. Leaving the accountancy profession to take my current post at Cardiff Institute of Higher Education (now Cardiff Metropolitan University) gave me the opportunity to look at taxation in a more academic manner. For many years I was aware that my background as an accountant was not ideally suited to the dominant paradigms of research in taxation, which treat it as a branch of either law or of economics. Whilst I had started to question some of the underlying principles of the UK taxation system,

it was not until about 10 years ago that, alongside Professor Rebecca Boden, I started to develop a framework for conducting tax research by treating it as a branch of the social sciences. This enabled me to question the principles of the UK taxation system and critique the contemporary debates in taxation in a much more rigorous manner. This thesis therefore represents the culmination of my thinking and work about taxation over the last 10 years.

One of the topical debates when I started my research was whether the UK should adopt some version of the flat tax and, because one of the principal claims made for the flat tax is that it would radically simplify the UK taxation system (e.g. Teather 2004; Heath 2006), this led me to research the tax simplification debate. This research made me aware that the issue was more complex than it had often been portrayed by, for example, Avery Jones (1996) and Kempster (2006) and that whilst the debate is often presented as purely technical and rational, in fact it can be highly politicized. The failure to achieve radical simplification was not simply a failure of political will or the result of lobbying by vested interests, but was caused by intractable conflicts between, for example, simplicity and equity and this resulted in a paper published in the British Tax Review (James 2008).

In July 2007 I attended the European Critical Accounting Conference in Glasgow at which Alex Arthur presented a paper (Arthur 2009) drawing on the work of Dworkin (1977) and John Braithwaite (2002), which argued that broad principles can give greater certainty than detailed rules in, for example, drawing up accounting standards by giving less scope for creative compliance. In a

similar vein, Freedman (2004) has argued that principles-based legislation, and in particular some form of General Anti-Avoidance Rule (GAAR) might reduce the scope for tax avoidance. However, my research on rules and principles in the area of taxation and avoidance demonstrated that the issue was, once again, more complex and led me to explore the covert and subjective nature of the exercise of discretion in tax systems (James 2010).

My research in these two areas made me realize that there was a broader and more profound underlying issue, which is that neither the legal nor the economic approaches to taxation address the fact that tax systems are not simply sets of objective, techno-rational rules, but result from subjective choices, and that these result from the socio-political complexities and dynamics of the relationships between various social groupings in society. Whilst conducting this research I attended conferences, such as the annual Tax Research Network conference and I became aware of the limitations of much of the research in the area of taxation. The normative and social underpinnings of taxation were therefore an under-researched area of taxation and the financial crisis which broke in the Autumn of 2008 highlighted the limitations and deficiencies of the dominant economic paradigm and the need for alternatives to be rigorously articulated.

This thesis therefore steps back from the detailed rules and the economic theory to explore taxation as a social science, arguing that tax policy (of which the detailed rules are simply a manifestation) is socially constructed through a discursive process involving all groups within society. However, the extent to

which these groups can participate in this process and influence tax policy will vary according to the degree of power which they can exercise. The tax system will therefore tend to favour the most powerful groups within society and I demonstrate that this has been evident in the UK tax systems from the Middle Ages onwards. I argue that the UK in the early 21st century strongly characterizes a neoliberal state and that the contemporary tax system therefore reflects neoliberal values and relationships.

My analysis of tax debates as manifestations of power relationships raised for me the question of how the neoliberal state evolved from earlier state forms. The transition from one state form to another is generally not abrupt, but gradual, and comes about through shifts in and the reworking of power relationships (Hall 1988). Taxation is one of the most important and direct nexuses between citizens and the state and I have charted the evolution of societal power relations from the 13th century to the present day through the development of the tax system in order to explain how neoliberalism was able to assert supremacy in the late 20th century.

These power shifts were often caused by demographic and economic factors, but the history of taxation is also the history of the development of economic ideas and thought and the construction of knowledge is one of the key means through which power may be exercised covertly (Foucault 1980). I therefore analyzed the evolution of economic thought, with particular reference to taxation, from the early publications of the 16th century onwards, but concentrated in more detail on the development of theory from the publication of

Adam Smith's *An Inquiry into the Nature and Causes of the Wealth of Nations* (Smith 2015 [1776]) onwards (hereafter referred to as *The Wealth of Nations)* in order to demonstrate that the principles upon which taxation in a neoliberal state is based are constructs deriving from neoclassical economics. These therefore provide an intellectual rationalizing discourse for the exercise of power by hegemonic groups.

This is a conceptual thesis which explores how the neoliberal state was able to emerge from its predecessors, the values and power relationships underpinning and the interests which it favours. It is not therefore essentially an empirical thesis involving the collection of primary data, because the analysis of the data requires a conceptual framework which was lacking and it was not possible to both set up the framework and apply it to empirical data within the word constraints. Since the conceptual framework is a necessary precursor for the analysis of data, this thesis aims to provide a framework which can subsequently be used to do this.

Since this was an under-researched area of taxation the theory relating to the role of power in tax policy was very limited and I therefore draw on the work of Lukes (2005) and Foucault (1978 [1976]; 1979 [1975]; 1980; 1981 [1969]) as a conceptual lens. I argue that in the neoliberal state power operates covertly through economic incentivization and auditing and accountability. Lukes's three-dimensional model of power, in which the first dimension of power is the overt operation and the third dimension the most covert, has enabled me to analyze the operation of power beyond that which is overt and thus directly observable.

Whilst Lukes (2005) has provided a high-level conceptual framework, Foucault (1978 [1976]; 1979 [1975]; 1980; 1981 [1969]) analyzes techniques, such as the use of audit and the knowledge/power, through which Lukes's third dimension of power may be put into operation. Whilst Lukes has critiqued Foucault and might not approve of being used in conjunction with him (Lukes 2005:88-107), I believe that they complement each other and writers such as Boden (2012) have successfully used them together.

Lukes (2005) concedes that it is usually difficult to observe and empirically verify the operation of the third dimension of power, since it is covert and therefore generally invisible. However, even where power operates covertly and invisibly, it can never be absolute and Lukes (2005) argues that there are always critical incidents where its operation becomes visible. Whilst this is a conceptual thesis, I have where possible used small case studies as empirical explorations of these. I did not conduct primary research to explore these, but instead relied on secondary sources, such as the national and technical press, Treasury briefings, Hansard reports and law reports of judicial decisions.

For example, the controversy which arose over the abolition of the 10p rate of tax in 2008 gave me an opportunity to explore how this exposed the power dynamics and relations of the neoliberal state. This was followed a couple of years later by the controversy surrounding alleged tax avoidance by large corporations such as Google, Amazon and Starbucks and alleged preferential treatment of Vodafone and Goldman Sachs by HMRC. This led to the emergence of UK Uncut, which is a grass-roots organization which opposes the

government austerity policies and aims to overturn the dominant neoliberal paradigm of taxation. I therefore used their emergence, and in particular the judicial review into the agreement between HMRC and Goldman Sachs for which it successfully petitioned, as a case study to explicate how hidden power relations can be made visible and challenged (James 2013).

This thesis therefore draws together complex themes and issues into an extended argument concerning the exercise of power in the formulation of tax policy rather than being based on original data collection. Chapter 3 sets out a conceptual framework of power and the evolution of neoclassical economics, which underlie my epistemological approach. Chapters 4 and 5 analyze how the neoliberal state was able to emerge from its predecessor state forms and its characteristics, whilst chapter 6 demonstrates that changes to the UK tax system since 1979 are consistent with neoliberal values and power relations. The incorporation of neoliberal values into the tax system is researched in more depth in chapters 7 and 8, in which I explore whether and how the contemporary debates concerning tax simplification and the use of principles-based legislation might be used as vehicles for this. In chapter 9 I explore whether and how resistance to the hegemonic neoliberal paradigm of taxation may still be possible. This is followed in chapter 10 by some conclusions.

CHAPTER 3: THEMES AND CONCEPTS

3.1. Introduction

In this thesis I explicate how power relationships between individuals and the state and between different groups of individuals are mediated through taxation and this raises several important issues, which I set out and discuss here to provide a framework for my later chapters. In chapter 3.2. I discuss why governing regimes (which have historically generally been nation states) need to levy taxation and the underlying principles on which it might be levied. In chapter 3.3. I set out a framework based on the work of Gramsci (1971), Foucault (1978 [1976]; 1979 [1975]; 1980; 1981 [1969]) and Lukes (2005) to explore the various ways in which power might be exercised. In chapter 3.4. I set out a summary of the evolution of economic theory from the Middle Ages to the present day in order to demonstrate how it has come to assume its current hegemonic status. This is followed by a brief summary in chapter 3.5.

3.2. Why and How Governing Regimes Levy Taxation

In his best known work *Leviathan* (Hobbes 2015 [1651]), characterized Man's natural condition as being in a perpetual state of war. In such a state there is no law and where there is no law there is no concept of justice. Survival in such circumstance can only be ensured by force or fraud, the consequences of which are that Man's life in a solitary state is, in possibly his most famous line, 'solitary, poore, nasty, brutish and short' (Hobbes 2015 [1651]: Ch. 13). It is to avoid this fate, Hobbes argued, that Man desires to live in peace and, in order to do so, it is necessary to create an organized society. This requires some form

of governing regime, which may either be ruled by an absolute ruler (who may be benevolent or despotic) or some form of democracy.

A governing regime must set up various structures and institutions in order for it to function, for example, in order to ensure collective and individual security and it therefore needs to control economic resources in order to finance these and human resources in order to staff them. Over and above these essentials, other institutions, such as public education and health care systems might be deemed desirable, as might achieving social aims such as the alleviation of poverty. The extent of the involvement of the governing regime ('the state') in the lives of individuals must therefore be agreed through discourse involving all of the various groups in society. At one end of the spectrum libertarians believe that individual choice is of paramount importance and reject the involvement of the state on the grounds that its services deny individuals this choice (Nozick 1973). A strict libertarian position is problematic as many of the basic functions of the state, such as national security are public goods, i.e. it is not possible to provide them for certain members of society without making them freely available in equal measure to all members. It is therefore not feasible for these to be provided privately, and libertarians are, in practice, willing to allow the state a minimal role in providing these public goods.

Alternatively, the relationship between individuals and the state can be regarded as a social contract in which individuals give up part of their individual liberty in return for the state providing them with collective benefits (Rousseau 1987 [1762]). Locke (1946 [1690]:5) wrote that all men and women are naturally in 'a

state of perfect freedom to order their actions, and dispose of their possessions and persons, as they think fit' and '[a] state also of equality, wherein all the power and jurisdiction is reciprocal, no one having more than another' but that God has driven men and women to associate with each other to form society. In order to do so and preserve their property and their natural state of perfect freedom, it is necessary to surrender their natural power to the community, which is empowered to resolve disputes in an impartial manner (Locke 1946 [1690]:71). Civil society is therefore where men and women live together in a body with a common established law and judicature with the power to resolve disputes. Social contract theory potentially allows the state a far more extensive role, but the amount of individual freedom to be given up must be agreed.

States and their activities need to be financed and the two options for raising the necessary funds are either that individuals make payments through individually negotiated contractual arrangements or the state makes a compulsory levy on citizens: i.e. taxation. Libertarians assert the supremacy of individual property rights and consider taxation to be a form of legalised confiscation (Nozick 1973). Locke (2015 [1690]) argued that no-one should be entitled to the fruits of another's labour and libertarians consider taxation to infringe this principle. In contrast, where activities are financed by contractual arrangements, no-one, at least in theory, makes payments unless they have freely consented to do so. However, it is not practicable to rely on individual contracting to finance public goods as they are non-exclusionary and a 'free rider' problem, i.e. where certain individuals can enjoy the benefits of goods or services without contributing towards their cost, will emerge. Libertarians are

therefore prepared to accept a minimal level of taxation to finance these. Where the relationship between individuals and the state is seen as a social contract, any consensus on the extent to which the state should set up institutions and structures above and beyond basic public goods must also include a consensus on the level of taxation necessary to provide them. This may be a ‘chicken and egg’ situation, since it might be unclear the extent to which the debate on the role of the state is driven by the consensus on the level of taxation people are willing to pay or the reverse.

Once a consensus on the amount of tax to be raised has been reached, it is necessary to agree *how* it will be raised. This determines how much tax revenue is to be contributed by different sections of society, which may, in turn, determine the income, transactions or assets to be used. Two competing principles for determining this are the benefits principle and the ability to pay principle. The former holds that those who benefit the most from government services funded by the revenue should contribute the most, whilst the latter holds that the greatest contribution should be made by those with the greatest resources, since they are best able to afford it (Stiglitz 1999).

The benefits principle is problematic for two reasons. Firstly, if the state wishes to alleviate poverty, it would be oxymoronic to insist that measures designed to achieve this should be funded predominantly by poorer members of society. Secondly, it can be difficult to ascertain the extent to which different sections of society benefit from particular institutions and services. For example, the police will protect citizens both from crimes of violence and from theft and burglary.

The former will tend to benefit poorer members of society more, since rates of violent crime tend to be higher in poorer areas, whilst the latter will tend to benefit wealthier members of society, since rates of theft and burglary tend to be higher in wealthier areas (James & Nobes 2014).

For this reason the ability to pay principle is generally preferred. Taxes may be classified as progressive, regressive or proportionate. A progressive tax is one where, as income increases, the proportion (not just the amount) of the income which is taken through taxation increases. A regressive tax is the opposite, i.e. as income increases, the proportion of the income which is taken through taxation decreases. A proportionate tax is one where the proportion of income taken by taxation remains constant, whatever the level of income (Stiglitz 1999).

Progressive taxes are therefore consistent with the ability to pay principle and progressivity is easiest to build into taxes on income, although they can also be regressive (Stiglitz 1999). In contrast, taxes on expenditure tend to be regressive, since poorer people tend to spend a larger proportion of their income than wealthier people. This can be avoided, or mitigated, by not levying tax on basic items, such as food and/or levying a higher rate of tax on goods which are typically purchased by wealthier people (a ‘luxury’ tax) (Stiglitz 1999). A tax system will generally include both progressive and regressive taxes and the overall progressivity or regressivity of the tax system will therefore depend on the proportion of the total tax revenue raised by the various taxes.

Consensus on these factors must be reached by various groups within society, who all have their own interests. The resulting tax system will therefore reflect the influence which these groups are able to exert in this debate. It will reflect both the relationship between citizens and the state and the power relationships between the various groups. Indeed, taxation is a particularly fruitful means of discerning these relationships because it is possibly the most important and direct nexus between the state and its citizens (Boden et al. 2010), since the sacrifice required of citizens results in an immediate loss of resources and any change will therefore be keenly felt (Martin et al. 2009).

A state's taxation system is therefore inextricably bound up with power relationships within society. The most explicit example of a power relationship in the area of taxation is the creation of obligations which citizens must fulfil towards the state. These must be underpinned by the exercise of power in order to ensure compliance, since the purpose of taxation will be frustrated if citizens can successfully evade their obligation to pay and become 'free riders'. Mechanisms and procedures must be put in place to determine individuals' liabilities, which will force them to make disclosures of their wealth and income to the state, and to impose sanctions on those who refuse to comply. However, the overt exercise of power by the state simply seeks to ensure compliance with the tax system which is extant at that time, but does not necessarily determine how that tax system evolved and how a consensus is arrived at in debates. This arises from the interplay of power relationships between different groups in society and, even where the power of the state

appears to be involved, it will often be the case that the state is effectively acting as an agent for a powerful group or groups in society.

These power relationships are more complex and covert than the exercise of power by the state and therefore require more sophisticated, theoretical models to unpack them. Lukes (2005) provides a three-dimensional model of power which describes the more covert means of exercising power and distinguishes them from the overt exercise of power. Lukes's model has been criticized by a number of academics (e.g. Bradshaw 1976). However, the criticisms related to the first edition of Lukes's book (1974), which was a very slim volume. The second edition (Lukes 2005) consists of the original text plus two further chapters in which he sets out to answer his critics. In doing so Lukes expands on his model of power, thereby making it more useful as a means of analyzing power.

Whilst Lukes provides a high-level model setting out the nature of power, Foucault poses the questions about the means by which it is exercised and its effects, viewing it not as an institution or structure, but as a 'complex strategical situation' or 'multiplicity of force relations' which are both intentional and nonsubjective (Poulantzas 1978 cited in Smart 2002:77). Whilst Lukes trenchantly criticized Foucault (Lukes 2005:87-107) and would therefore not approve of being bracketed together with him, other writers such as Boden (2012) regard this criticism as possibly unfair. Lukes and Foucault are therefore used together in this thesis because they complement one another; Lukes providing the high-level model and Foucault the means of operationalizing it.

3.3. Power – a Conceptual Framework

The Three Dimensions of Power

Lukes (2005) offers a three-dimensional model of power, where power is the ability of an individual or institution (A) to force or persuade another individual or institution (B) to act in a manner in which they would not do if that power did not exist. The *first dimension* is the overt exercise of power which may be through legitimate authority or force and coercion. In the context of taxation, the first dimension of power is the legal power to levy taxation and enforce compliance by passing laws to determine its form and amount, compelling taxpayers to make disclosures of their financial affairs and resources in order to make an assessment, and imposing sanctions to enforce payment, such as fines or imprisonment. Power may also operate by ensuring that an individual cannot gain the benefit of the underlying transaction without paying the tax. Examples of this are stamp duty, where a title deed does not have legal force unless the duty is paid and the document is stamped, or bonded warehouses, where an individual cannot take possession of their goods unless the duty is paid.

In the second dimension, B ostensibly has a free choice of actions, but the range of options open has been restricted by the power of A. It is not always necessary for this power to be exercised: its existence may simply inhibit certain issues being discussed publicly. Lukes, using the work of Bachrach and Baratz (1970), compares the cities of East Chicago and Gary, noting that the former passed clean air legislation roughly 15 years before the latter. Gary was a company town in which US Steel was the dominant employer, whereas there was no dominant employer in East Chicago and union power was greater. US

Steel rarely entered politics, but Bachrach and Baratz concluded that its unspoken power prevented the issue being debated.

Foucault (1981 [1969]) terms this technique, or exclusion, *prohibition*: in practice, we do not have complete freedom to speak about all topics in all circumstances and there are topics which are considered taboo and individuals holding certain views might be considered to be mad. It is unimportant that the taboo topic might in itself be unimportant, since the power resides in the ability of the dominant group to stifle discussion and control the discourse. An example of an aspect of the second dimension of power in taxation is the fiscal constitution (Daunton 2007), which is a set of written, unwritten, or even unspoken procedures and conventions setting parameters within which any debate on taxation takes place and which therefore places certain issues or solutions beyond the realm of serious consideration.

Whilst the exercise of power may not be immediately obvious to outside observers, where the second dimension of power operates, B may still be aware of the disjuncture between their chosen option and their perceived interests. This therefore means that the possibility of resistance is ever-present and the historical record suggests that the prospect of resistance to taxes which are perceived to be unfair is very real.

Power may be less observable still, and therefore even more complete, if A can eliminate this disjuncture by influencing the way in which B thinks (Lukes 2005), which will reduce, if not completely eliminate, the possibility of resistance. In the

third dimension of power, B therefore again ostensibly has a free choice, but has been conditioned to believe that their interests are aligned with those of A. B will therefore choose the option A wishes, without being aware of any disjuncture between this and their own perceived interests. Indeed, even A may not be aware that they are exercising power because they might also have internalized a particular paradigm or way of thinking so thoroughly that they regard it as simply 'common sense' rather than an opinion or ideology.

Power is at its most effective when it is least observable, because it is by no means always a straightforward task to identify whether power is being exercised at all, and, if it is, how and by whom it is being exercised. If A did not exercise power over B, B might still not be able to exercise free will since A may simply be the most powerful of numerous sources exercising power over B and if A did not do so, B might act in accordance with the wishes of the second most powerful source. Whilst Bradshaw (1976:122) admits that Lukes does not claim that this is possible, it therefore becomes impossible to imagine a 'best of all possible worlds' in which B can identify their 'real interests'.

The assumption that an outside observer can therefore identify the 'real interests' of an individual or group better than the individual or group themselves and thereby attribute their actual views to a false consciousness is problematic. For example, the failure of the citizens of Gary to press for clean air legislation (Bachrach & Baratz 1970 cited in Lukes 2005) does not necessarily imply *inaction* on their part, but may be a conscious decision *not* to

act on the grounds that pollution control would bring unemployment (Bradshaw 1976:122 & 123)

Lukes terms a decision to prioritize air pollution over unemployment an ‘adaptive preference’, i.e. the best or least unsatisfactory option that they believe is realistically open to them, rather than what they would ideally like (Elster 1983, cited in Lukes 2005:134). This rests on two assumptions, both of which are reasonable in this scenario. Firstly, the citizens of Gary would prefer clean air to polluted air and, secondly, they were aware that it was possible to have both clean air and employment since they had the example of the nearby town of East Chicago. The fact that they felt that they must choose between the two was due to the power and influence of US Steel. This therefore can be contrasted with situations where a decision *must* be made, such as a decision on the balance between career and family, since it is impossible to spend the same time at work and with the family.

It may be difficult to identify whether B truly believes that their interests correspond with those of A or whether they are simply expressing an ‘adaptive preference’. However, where the second dimension of power operates (for example, people simply getting on with their lives under a tyrannical regime and making small accommodations with it) there is simply resignation and a researcher can therefore discover signs of covert dissent in the form of, for example, jokes and conversations in a safe environment (Scott 1990, cited in Lukes 2005:126). Where the third dimension of power operates, citizens

subservient to the dominant ideology are unaware of the hidden power which keeps them in their place, and these signs of dissent are absent.

The difference between the second and third dimensions may be more subtle and complicated than whether there is an awareness of the disjuncture between one's beliefs and what one can publicly discuss and advocate. Although no power can be absolute, a tyranny or hegemonic ideology may become so normalized that there appears to be no prospect of an end to it and no way of voicing effective resistance. Opposition may become internalized and hidden behind apparent support for the regime. Individuals may therefore simultaneously accept an ideology and be aware subconsciously that it is a lie and of the interests behind it (Žižek 2008:23). Žižek terms this an 'enlightened false consciousness' and regards it as a positive reaction in the sense that individuals may no longer feel downtrodden, but also argues that regimes are ill-advised to rely on this; for example, the rapid collapse of communist regimes in Eastern Europe in the late 1980s and early 1990s indicates that once a certain tipping point is reached, the latent opposition asserts itself.

This absence of dissent presents researchers with a further problem with the third dimension of power. If B truly believes that their interests correspond with those of A, B is, by definition, unaware of any disjuncture. Bradshaw (1976) criticizes Lukes on the grounds that, by asserting that the third dimension of power is operating, a researcher is attributing B's views to a 'false consciousness' and thus denying B free moral agency. For example, where a choice must be made between, for example, prioritizing career or family, a

researcher can attribute a choice which they disapprove of to a false consciousness. However, such an assertion can therefore reveal as much about the ontology of the observer as the individual or society observed (Lukes 2005). If a researcher is viewing their own society, they have been conditioned in accordance with its social values and it is questionable the extent to which they are able to remove themselves from it and view it from the outside, even if they claim to be able to do so. If they are observing a different society, whilst they are viewing it from outside, they are still imbued with the values of their own society. Either way, it is doubtful whether an observer can be objective, which can give rise to what Bordieu (1998:26) calls 'the conspiratorial fantasy which so often haunts critical thinking'.

The question of the extent of the agency of those over whom power is being exercised is therefore one of the most important issues in an analysis of the operation of power. Lukes (2005:148) accepts that there is no 'canonical set of...interests', but that these can be a function of the researcher's framework, purpose and method and therefore need to be justified. The term 'false consciousness' refers, not to an assertion that the researcher has privileged access to truths unavailable to others, but to a recognition of the power to mislead (Murphy & Nagel 2002; Lukes 2005). In this thesis I therefore argue that the knowledge created by neoclassical economics has been used to create a false consciousness by misleading individuals about the consequences of particular decisions or that a particular course of action is the only realistic one.

In the field of taxation, power operates by incentivizing individuals to pay taxes: literature on this topic has generally focussed on the tax compliance aspect of this, which is the exercise of the first dimension of power. There have been two contrasting approaches to this issue: the deterrence and the accommodative enforcement models. The former, which can be traced back to the utilitarian doctrine of Bentham and Cesare Beccaria, treats taxpayers as rational actors who base their tax compliance decisions on the trade-off between the gain from non-disclosure and the risks and penalties of detection (Murphy K. 2008). The accommodative model recognizes that, whilst the deterrent model may have some effect, it may also be counter-productive if legal coercion is regarded as illegitimate, giving rise to non-compliance, creative compliance or overt resistance (Murphy K. 2008).

The accommodative approach treats tax compliance as a socially constructed phenomenon (Boll 2011), which relies on the concept of ‘tax morale’. This encompasses a collection of factors which make taxpayers more or less disposed to comply with their tax obligations and governments and tax authorities should deploy strategies to maximize these. For example, Boll’s (2011) assertion that Danes pay their taxes, if not with pleasure, then certainly with appreciation, or the fact that according to a 2013 survey 83% of Swedes are satisfied with the performance of the tax authority (Sweden 2015) would indicate a high tax morale in Denmark and Sweden, despite the high levels of taxation in these countries. Tax morale encompasses a number of factors such as trust in the government and the respectful treatment of taxpayers by the tax authorities (Torgler & Schaltegger 2005) and demographic factors such as age

and gender (OECD 2013). Whilst governments can pursue policies to engender trust in its institutions and respectful treatment of taxpayers (Torgler & Schaltegger 2005), the OECD (2013) has found that individuals who identify fiscal redistribution as an essential characteristic of democracy have higher tax morale than those who do not. The level of tax morale is therefore also, in part, a factor of the prevailing notion of the relationship between individuals and the state. Where there is a strong sense of this relationship being a social contract, of which taxation is a part, there is likely to be a higher level of tax morale than where the libertarian view prevails.

Engendering high tax morale, so that individuals pay their tax liabilities willingly, might be characterized as the third dimension of power on the grounds that they are being persuaded to act against their best interests. However, this view can be criticized on the grounds that it depends on accepting the view that taxation is a form of confiscation. However, wealthy individuals might argue that funding state services and reducing inequality brings increased levels of trust in society and greater peace of mind through reductions in crime and is therefore in their best interests (Wilkinson & Pickett 2009).

Not only is the characterization of high tax morale as the operation of the third dimension of power debatable, but neoliberal policies might also tend to lower tax morale. Indeed Davies (2014:8) has described neoliberalism as ‘the disenchantment of politics through economics’, meaning that neoliberal policies are deliberately designed to undermine democratic institutions, and therefore trust in them, through the creation of a ‘shadow state’ (Williams 2013). In the

neoliberal state, incentivizing individuals involves not so much persuading them to comply with their tax obligations willingly, but incentivizing them to work and undertake economic activity in order to earn the income on which tax becomes due. I demonstrate in chapter 5 that the neoliberal state is an economic state in which policy is driven by economic theory, and in particular neoclassical economic theory, to incentivize individuals to put themselves at the service of capital. However, in order to characterize this as the operation of the third dimension of power it is necessary to surmount the difficulty which might bedevil characterizing high tax morale in this way and demonstrate that these economic policies persuade individuals to act against their best interests. The following section therefore discusses how this might be achieved.

Harnessing the Biopower

Foucault's exposition of biopower[1] facilitates an explanation of how the third dimension of power might operate and how 'power relations can materially penetrate the body in depth, without depending even on the mediation of the subject's own representations' (Foucault 1980:186). Entire populations can therefore be controlled at a distance by affecting the ways in which they think through structures of coercion where techniques of domination are integrated with 'techniques of the self', whereby individuals are encouraged to regulate their own conduct in a certain way (Foucault 1980). Daily practice is institutionalized and individuals must repeatedly follow detailed, precise rituals, where 'correct comportment' is rewarded and deviations from this are punished (Foucault 1979 [1975]).

[1] Techniques for achieving the subjugation of bodies and the control of population (Foucault 1978 {1976]:140)

Foucault termed these techniques of indirect control *governmentality*, a portmanteau word whose derivation from government and mentality clearly describes these combinations of techniques. These represent a diffusion of the power of the state, since, whilst they use institutions and rationalities of sovereignty and discipline, they also use 'regimes of practices' which shape the behaviour of individuals through reward and punishment which is institutionalized in daily practice (Foucault 1979 [1975]). The logic of these regimes is 'irreducible to the explicit intentions of any one actor, but yet evinces an orientation toward a particular matrix of ends and purposes' (Dean 2010:32) and is only evident by understanding the whole 'as an intentional but non-subjective assemblage of all its elements' (Gordon 1980 cited in Dean 2010:32). The exercise of power through an assemblage reinforces its operation, partly because it becomes all-enveloping, but also because it is only possible to attack and disable one small part of the power regime at a time.

Whilst techniques of governmentality aim to exercise power in the third dimension and influence normative beliefs through the micro-management of behaviour, it might not be clear whether it has achieved this, or whether it has only exercised power in the second dimension, since individuals may act in the desired manner because that is in their own short-term interests without buying into the underlying ideology. Indeed, it is possible to buy into the ideology up to a point, such as agreeing that students' views should be heard or that universities' research should be evaluated, but being against these being used as crude mechanisms of control.

The third dimension of power operates by influencing normative beliefs and this is possible to achieve particularly where they arise from beliefs about *what* might happen in certain sets of circumstances rather than which of a number of options is considered preferable. The third dimension of power therefore operates through the interweaving of power and knowledge (Foucault 1980), since the validation of what constitutes knowledge is socially constructed through discourse. Specific interests within society do not therefore assert dominance in an overt and structural fashion, but instead seek to use the knowledge/power nexus, i.e. other groups in society acquiesce in the interests of the dominant group by internalizing the truths and knowledge which the dominant group has socially constructed in a manner which benefits their interests, and hegemonic interests will construct institutions which impose and renew these truths, such as pedagogies, books and libraries (Foucault 1981 [1969]).

In this thesis I demonstrate that in the neoliberal state economics has become the means through which the third dimension of power operates by creating beliefs about *what* will or might happen, rather than whether certain outcomes are fair or desirable. Murphy & Nagel (2002) argue that it is not necessary to convince individuals that certain outcomes are fair, but simply that they will be favourable to them, or that other options will lead to less favourable outcomes. Economics has generated a set of theoretical models which purport to explain how the financial and economic world operates and taxation forms an important part of these. The power of economics therefore derives from its ability to plausibly state that certain future outcomes will follow inevitably from certain

current actions, and this power may be bolstered by the social, cultural and intellectual capitals of those putting the ideas forward, and this is further facilitated by the fact that it is not possible to conduct controlled experiments in the social sciences (Blaug 1997). This can therefore be contrasted with the argument that high tax morale is the result of the operation of the third dimension of power. The trade-off between paying higher levels of tax and the provision of better public services is far more transparent and the argument becomes a normative one of whether this trade-off is worthwhile.

Once a discourse becomes hegemonic, it generates unconscious consent through the moral and intellectual leadership conferred by its position, prestige and function in society and through which institutions such as the law, police and courts issue a combination of commands (Gramsci 1971). The ‘rules of the game’ appear to be fixed and immutable, whereas they have been constructed by powerful actors to benefit them (Oats & Morris 2015) and the operation of power is therefore hidden. It becomes implicitly manifest in all areas of economics, law, art and culture and permeates the system of values, beliefs and morality through all structures of society, such as schools, churches and the family (Infanti 2008). The consent to this world-view is felt to be ‘spontaneous’ in the sense that subordinated groups do not feel that it has been forced or coerced, because it has been internalized to the extent that it feels natural to them and has been connected with ‘common sense’ so as to appeal to both intellectuals and the masses (Infanti 2008). This hegemony performs a function which guns and tanks cannot, since it mystifies power relationships and

encourages a passivity and fatalism towards political action, justifying every type of system-serving sacrifice and deprivation (Infanti 2008).

In this thesis I demonstrate that in the neoliberal state the knowledge created by the ideology of economics has achieved a Gramscian hegemony, making it, if not impossible, then certainly difficult to conceive of alternatives. However, power can never be absolute and there is always the potential for resistance (Foucault 1978 [1976]); Lukes 2005). Alternative discourses can never be eliminated entirely, and their very existence means that it is possible to undermine, or even to break a hegemony and offer counter-hegemonic discourse. Instances of resistance to the hegemonic discourse therefore provide critical windows which allow the normally hidden operation of power to be glimpsed.

However, the hegemonic interest will deploy various strategies to try to prevent this. They may lead allied and kindred interests and neutralize them by incorporating them into itself. They may attempt to subjugate or 'liquidate' antagonistic interests, which need not necessarily require force if they can instead be 'organized out', i.e. marginalized, so that their alternative world-views are seen as eccentric or unfeasibly utopian. By deeming a person to be mad, their contribution can be dismissed as null and void and therefore not worthy of serious consideration; for example, their evidence may be considered worthless in a court of law or in the authentication of deeds (Foucault 1981 [1969]) and the phrase 'loony left' can be seen as a strategy to marginalize those who

believe in alternative taxation systems which incorporate notions of social justice.

Finally, the hegemonic interest may attempt to prevent resistance by making concessions to those who might be troublesome in order to make their position within the assemblage sufficiently comfortable, but these concessions will only be at the margins and will not threaten its hegemony (Infanti 2008). However, there is therefore no guarantee that the above strategies will be effective indefinitely and the possibility of change always remains. Although I demonstrate in this thesis that the economic view of taxation has achieved a Gramscian hegemony so that individuals are unable to seriously conceive of alternatives, I also demonstrate that there are still elements of resistance, which have forced concessions from the hegemonic group and which might still have the potential to overturn this and create a new knowledge.

In summary, Lukes (2005), Foucault (1978 [1976]; 1979 [1975]; 1980, 1981 [1969]) and Gramsci (1971) offer a conceptual, critical lens through which power can be analyzed and they offer two especially important insights. First, power need not be exercised simply through a traditional hierarchical structure, but may instead operate in a capillary fashion, whereby power flows in various directions between different interests within an assemblage, although different interests may exercise unequal amounts of power, with some being more influential than others. Second, power need not be exercised through overt means of coercion, but by discursively framing the ways in which others think through the leadership of ideas and the regulation of everyday conduct. In this

way these ideas may assume a hegemonic position in which they come to be seen as self-evident truths, rather than as ideologies which provide a rationalizing discourse for powerful interests.

In chapter 5 I argue that, particularly in the UK, neoliberalism has become a hegemonic ideology, whose knowledge has been constructed from economic, and, in particular, neoclassical economic, principles. Social history can be viewed in terms of a battle between social movements which seek to use power to make society better for human beings, and artificial entities, such as corporations, which use power to give themselves absolute freedom to do whatever will earn them the greatest profits, whatever the social costs, and neoliberalism represents the triumph of the latter over the former. Economics has played a crucial role in this battle by providing corporations with a theoretical justification for their interests and obscures power by portraying the market as an efficient system of voluntary transactions. Economics portrays the power of the market or the power of competition as a *deus ex machina*, thereby obscuring the role of corporate power (Perelman 2015). However, hegemonic ideologies do not suddenly emerge fully formed, but evolve gradually through the development and reinterpretation of earlier theories and in the following section I explore how economics became the hegemonic knowledge which underpins the neoliberal state.

3.4. The Evolution of the Neoclassical Paradigm of Taxation

In this section I trace the evolution of the economic ideas which underpin the neoliberal paradigm of taxation, which is founded on the principles of

neoclassical economics. This cannot be, and does not set out to be, a comprehensive history of economic thought, but concentrates on how the ideas which are relevant to this thesis evolved through the development and reinterpretation (sometimes a highly selective reinterpretation) of earlier theories. I argue that ideas which were originally put forward as part of a moral philosophy have, over time, evolved into a set of non-contextual mathematical models. The motivation for this shift was the desire of economics to join the canon of natural sciences, but this shift slowly cut away the very ground it stood upon (Larkin 2014:99), which resulted in moral or philosophical aspects being expunged from it.

These models are concerned with notions, such as *economic efficiency*, where efficiency means a Pareto optimal economic allocation such that an individual's utility cannot be increased without decreasing the utility of another individual and therefore has a very different, more technical meaning than its everyday usage (Makdissi 2006). These models have become the basis of economic theory, which is the generation of economic models in order to test hypotheses (Pass et al. 1988) which engenders political notions of the ways of distributing resources. These can therefore provide a rationalization for the redistribution of resources in favour of particular sections of society and taxation is one means of doing this.

Neoclassical economics has become the dominant economic paradigm, but history is generally written by the victors in any war or conflict, and by the dominant groups in society in general. This history will therefore justify their

actions and positions and this has led more recently to alternative histories which consider history from the viewpoint of ‘forgotten’ or more disadvantaged groups in society (e.g. feminist or black history). Similarly Bachelard (1965) (cited in Tribe 1978) has argued that

> each science reworks its history as a history of its progress, producing a double recurrent history: a sanctioned history of the positive acts producing the knowledge, and a continually augmented peripheral history constituted by the elements that are discarded in the progress of the science
> (Tribe 1978:7)

and this peripheral history ‘lurks in monographs and journals, a record of “forgotten men” ' (Tribe 1978:7).

Neoclassical economics is therefore not the only form of economic theory and there exist many alternative forms, such as heterodox economics, institutional economics, Marxist economics, feminist economics and green economics. However, the fact that these other schools of thought have become largely marginalized is a demonstration of Lukes’s (2005) third dimension of power through the construction of knowledge and the Foucauldian (1981 [1969]) distinction between reason and madness, whereby the alternative paradigms are dismissed as unfeasibly utopian.

In this section I concentrate on four distinct features of the development of economic thinking which have a traceable impact on the subsequent emergence of neoliberal ideology. However, these topics are only discussed in outline and the scope of the discussion is limited and the insights provided are those which are relevant to this thesis. The first is the reinvention of Smith's *Wealth of Nations* (2015 [1776]) as a blueprint for laissez-faire industrial capitalism, which is a misrepresentation of his actual views. The second is Ricardo's rent theory (1815) which was the first theorization of the opposition of the interests of capital and labour and that the former should be prioritized over the latter. The third is the marginal analysis of labour which assumes that, in order to incentivize taxpayers to work and undertake entrepreneurial activity, poorer taxpayers must be paid less and wealthier taxpayers must be paid more. The fourth is Böhm-Bawerk's theory of capital which was a key theory leading to the monetarist theory that the economy operates according to quasi-scientific laws, which governments cannot control.

Scholastic philosophy of the 13th century was explicitly linked to Aristotelian philosophy, which it attempted to assimilate into Christianity. The theory of the 'just wage' (Screpanti & Zamagni 1993:17) was a moral and philosophical principle, being a wage which would guarantee a worker a standard of living commensurate with their social condition and there was a 'just price' theory which relied on the 'exchange of equivalents' and was connected to the cost of production (Screpanti & Zamagni 1993:17). Any profit must be 'fair and moderate' and commerce was only considered legitimate if it benefitted the collective. The prefix eco- in economics derives from the Greek word *oikos,*

meaning family or household (Tribe 1978), and in the Middle Ages economics, or *oeconomia*, was largely concerned with the government of the household. It therefore belonged to the realm of the private sphere of human action and was subordinate to ethics and political philosophy (Screpanti & Zamagni 1993).

The rise of mercantile trading created a triadic economic structure of land, which was owned by the aristocracy, capital, which was owned by the new mercantile class, and labour, which was provided by the peasants (Roll 1973). Each of these groups sought to obtain a return from their assets, being respectively rent, profits and wages. This created the potential for conflict, in which each group might seek to maximize their return at the expense of other groups and mercantile trading created a new set of economic relationships where individuals started dealing with others who were more remote from them, both geographically and in terms of kinship (Roll 1973).

Economic theorists responded by starting to separate economics from moral philosophy and concerning itself with the state in order to explain these relationships (Hunt 1979). In the 16th and 17th centuries the Protestant ethic also ceased to condemn egoistic and acquisitive behaviours and thus legitimated economic activity (Screpanti & Zamagni 1993). *A Discourse of the Commonweal of This Realm in England,* written by, it is believed, Sir Thomas Smith[2] in 1549 has been called 'the beginning of British political economy' (Beer 1938 cited in McNally 1988:27). It set out a theoretical treatment of monetary phenomena, such as price inflation under conditions of plenty, rather than

[2] This is according to McNally. Screpanti and Zamagni (1993) cite the author as John Hales.

scarcity, and developed a central theme of English mercantilism, which was that imports and exports had to be kept in balance in order to maintain the wealth of the nation. It also developed rudimentary notions of the 'circular flow' of economic life and marked a break with earlier thinking that a flow of money to certain agents automatically resulted in a loss to others (McNally 1988:28). Its moral underpinnings can be deduced from the fact that, at that time, Smith was a member of the Commonwealth Party, which advocated a just social order, the preservation of which was the responsibility of the monarch and their advisers (McNally 1988:25-26).

In the 17th century the economic theory set out in the *Discourse* was developed by, for example, Thomas Mun and William Petty. In the 1620s Mun formulated laws which sought to explain the interaction of prices, the balance of trade and specie flows in *England's Treasure by Forraign Trade* (Spiegel 1991) and has been described as 'the most influential economic doctrine before Adam Smith' (Supple 1959 cited in McNally 1988:31), whilst in the 1640s in *A Treatise of Taxes and Contributions* Petty sought to apply a strictly scientific and empirical method of analyzing economic phenomena inspired by the spirit of social Baconism which became popular at that time (Screpanti & Zamagni 1993). Again, this indicates a moral basis, since Baconism was republican and antiauthoritarian in outlook and became a rallying point for Puritan intellectuals. Baconism set out to reformulate science on radically new foundations, fearing that adherence to old doctrines might prevent science from fulfilling the new possibilities opened up by this period of change (McNally 1988).

Petty's *Treatise* was one of earliest to concern itself with taxation and contained, in embryonic form, some canons of taxation such as clarity, certainty, economy in collection, convenience of payment and proportionality (Screpanti & Zamagni 1993). He argued that, since the basis of taxation was landed property, the phenomenon of rent was the surplus physical product of the land after production expenses. This definition, which was novel for its time, was based on a labour theory of value which would determine the value of the land and from this he sought to formulate the money value of this 'real rent' (Hunt 1973). He believed that government intervention was necessary in order to provide employment for the unemployed, so that their expenditure could create additional demand for goods from Ireland, thereby relieving the burden of taxation on landowners there such as Petty (Murphy A.E. 2008). The *Treatise* therefore contains ideas which would be taken up by Marx nearly 200 years later and which anticipate the fundamentals of the Keynesian multiplier by about 300 years (Murphy A.E. 2008).

Whilst mercantile trading had become more important, Britain was still predominantly an agricultural society and the economic model formulated in the 16th and 17th centuries was an agrarian capitalist one. Although the various treatises sought to establish economic laws relating to mercantilism, they all viewed agriculture as the main source and driver of prosperity and wealth. In the *Discourse* Thomas Smith viewed the ultimate purpose of trade and industry as to stimulate agricultural production to overcome poverty and unemployment and Petty regarded rent, rather than capital, as the central feature of the capitalist economy (Spiegel 1991).

Britain continued to be a predominantly agricultural society up to the Industrial Revolution and it is in this context that Adam Smith's *The Wealth of Nations* (Smith 2015 [1776]) should be understood. This contradicts much of conventional academic wisdom, which has regarded Smith as 'the prophet of the commercial society of modern capitalism' (Spiegel 1991), or that he provided 'a theoretical formulation of the phenomena of rising industrial capitalism' (Rubin 1979 cited in McNally 1988:152). However, the facts that the start of the Industrial Revolution can be dated to roughly 1760 and that *The Wealth of Nations* was written over a period of 10 years and was drawn from notes compiled over a period of 17 years do not support this view (Smith 2007 [1776]). Whilst the period over which it was written was one of great innovation, the book reflected the predominance of agriculture.

Furthermore, whilst Smith is today primarily regarded as an economist and *The Wealth of Nations* (2015 [1776]) as a work of economics (Tribe 1981), his approach has its origins in jurisprudence, ethics and philosophy (Larkin 2014) and contemporary commentators such as Stewart (1811, cited in Tribe 1978:101-2) regarded it rather as a work of *legislation*, relating to the branch of legislation known as *political economy*, or *political oeconomy*. Oeconomy emphasizes the derivation of the word from the Greek *oikonomia*, and the work was therefore read as practical advice to rulers on how a natural order could be maintained (Tribe 1978). Smith had allied himself to the French physiocratic tradition, which held that there existed a natural order operating according to natural laws and that the various components of society, such as the economy, social order and the state, would only function if they too adhered to these.

However, the Physiocrats relied on an absolute monarch to establish the necessary framework and Smith faced the problem of how this could be achieved in the absence of such a figure (Tribe 1978). Smith and his contemporaries believed that it was possible to find the same sort of natural order and harmony governing society that scientists and philosophers such as Newton had found in the natural world (Landreth & Colander 2002). In examining the social sphere, Smith was therefore looking for order rather than chaos and was, in particular, looking for means by which order could be maintained without it being imposed from above by an autocratic ruler or sovereign. Smith's concept of the 'invisible hand' was not an economic concept, but an expression of the autonomous force generated by Man's natural benevolence towards his fellows that would guide individual self-interest into a natural harmony through the competitive market without the need for the ruler, sovereign or deity to actively produce this (Tribe 1981; Musgrave 1996).

Whilst Smith advocated the competitive market, it was put forward simply as an alternative to the domination of industries by monopolies (Sim 2012) and he still saw a role for the state in overcoming the problem of the 'free-rider' in the provision of public goods, such as protection against foreign invasion, protecting members against injustice from others, and public works which provide benefit to society, but which individuals would not consider worthwhile funding privately (Musgrave 1996).

In *The Wealth of Nations* Smith was seeking a social order which would reconcile the interests of land, capital and labour and his views reflect the fact

that his capitalist system was an agrarian one. He was sharply critical of merchants in many places, condemning their ‘mean rapacity’, ‘monopolizing spirit’ and ‘impertinent jealousy’ (Smith 2015 [1776]: Book IV) and regarded the basic principle of the mercantile system as a monopoly, believing that merchants and manufacturers had deceived the public by convincing them that what served the interests of merchants and manufacturers also served the interests of society as a whole. In Book II he stated that the most productive employment of capital was agriculture, followed by manufacture, then wholesale trade and lastly retail trade, and that not only country gentlemen, but also rural labourers, were superior to their urban counterparts. The superiority of rural labourers stemmed partly from the notion that the division of labour in industrial processes rendered labourers incapable of judging the best interests of society (Smith 2015 [1776] Book V).

Smith’s denunciation of the self-interest of mercantilism and view of rural labour as being morally superior to industrial labour also gives the lie to the notion that Smith was an advocate of a laissez-faire economic system. On the contrary, Smith had a profoundly moral concept of society and his economic theory was based on how this moral concept could best be realized and maintained. The state had an important role in maintaining the principles of justice and creating an institutional framework in which it was impossible for self-interested market relationships to distort society (Landreth & Colander 2002).

Seen in this light, the four canons of taxation (Smith 2015 [1776]: Book V Ch. 2.25) are not economic concepts, but instructions to statesmen on how to

construct and administer a tax system without upsetting the natural harmony, so that citizens pay their taxes willingly out of a sense of duty, rather than mere obedience brought about by fear. For example, citizens are more likely to pay taxes willingly if they are levied in a manner which is generally perceived as equitable and if they are certain, i.e. codified, rather than subject to the arbitrary whim of an official. Smith's views on the merits of various tax bases were not related to theorized economic models but were rooted in the same concern with the maintenance of harmony, even though he addressed issues such as the effect of taxation on incentives and the economic incidence of taxes, which became very important in the techno-rational model of taxation (Smith 2015 [1776]: Book V, Ch. 2:72, 2:75 & 2:76).

Crucially, Smith did not view the interests of labour as being antagonistic to those of capital and believed that labourers should be adequately remunerated so that they were able to raise 'numerous families' (Smith 2015 [1776]: Book I Ch. 8:23). Indeed, he viewed both rent and profit as deductions from 'natural' wages, which arise from the power of landlords and capitalists (Schumpeter 1986). He therefore opposed taxation on wages or a consumption tax on 'necessary articles of subsistence' (Smith 2015 [1776]: Book V, Ch. 2:149) on the grounds that the tax would lead to higher prices and a reduction in the return on capital, which, in turn, would reduce the amount of labour which a capitalist could employ with a given level of capital. For Smith, rent was not a device for apportioning profit between the landlord and the tenant. The farmer should only be allowed to retain such profit as is necessary to re-invest and rent was linked to what the farmer could afford to pay (Smith 2015 [1776]: Book V

2:58). It was therefore not the precursor of rent theory, as it is presented by, for example, Ricardo (Tribe 1981).

Smith's economic theory therefore had a profoundly moral basis and Blaug (1997:60) regards any attempt to enlist him in support of the 'fundamental theorems of welfare economics' (quotation marks in Blaug) is a 'historical travesty of major proportions'. Nevertheless, whilst he articulated these principles within a moral philosophy, rather than as a logical or mathematical discipline, by selective reading and praising his pro-market positions, whilst ignoring his criticisms of the abuses of power (Perelman 2015) the principles provided the template for an abstract deductive science which proceeds from a few general principles of a philosophical, rather than an empirically verifiable nature (Deane 1978). Smith's successors were therefore able to use his principles to transform economics from a branch of moral philosophy into a branch of mathematics, even if they were misrepresenting Smith's intentions by doing so.

The process of reinventing Smith started in the early 19th century and one of the most important developments at this time was the publication by David Ricardo of his rent theory in 1815 in his pamphlet *Essay on the Influence of a Low Price of Corn on the Profits of Stock* (1815). This is one of the earliest statements of classical rent theory (Tribe 1978) and, whilst many of its themes are recognizable from Smith, they are given a decisive new twist. This pamphlet was published only 40 years after the publication of *The Wealth of Nations,* but in this period Britain had been transformed from a predominantly agricultural

into a predominantly industrial society. The balance of power between land and capital had therefore shifted decisively towards capital and relations between the two were at a low ebb (Daunton 2002a) and Ricardo's rent theory can be seen as a theoretical justification of this antagonism.

Ricardo's rent theory related agricultural prices to the costs of production on the least productive land and the payment of rent became a device to reduce the return made by those farming on more productive land and to enable all farmers to make the same rate of return. It was derived from Malthus's (1798) concept of diminishing returns, which was, in turn, derived from his population theories and was based on a number of assumptions (Spiegel 1991). The underlying assumption of Malthus's population theory was that population grows in the manner of a geometric progression, whereas agricultural food production can only grow in the manner of an arithmetic progression. Unless checked, population growth would therefore overwhelm the population's capacity to feed itself. From this, Ricardo derived a theory that, as the population grew, it became necessary to bring less fertile land into agricultural production. The return on capital was lower on the less fertile land, therefore farmers who worked the more fertile land paid rent to their landlords in order to equalize the rates of return on different plots of land of varying fertility. That rate was determined by the rate on the least fertile land under cultivation, therefore the more land under cultivation, the lower the rate of return on capital and the higher the rent paid to landlords of more fertile land (Tribe 1978).

An increase in wages exacerbated this problem by encouraging population growth. It was therefore in the interests of society to depress wages in order to reduce population growth and thereby reduce the amount of land needed for cultivation, thus creating an antagonism between labour and capital (Landreth & Colander 2002). This also minimized the level of rent paid to landlords, who were regarded as passive rentiers, and maximized capitalists' return on their capital (Roll 1973), creating an antagonism between rent and capital. The checks might either be preventive, with the lowering of births through 'moral restraint' (Blaug 1997:67), or through the raising of the death rate due to famine.

Ricardo did not address the issue of taxation in his rent theory, but he was advocating distributing, or redistributing, resources in favour of capital at the expense of land and labour and, in the neoliberal state, taxation has become a technology for doing this. The relationship between land, capital and labour was formulated as an economic model, thereby giving them an objective, scientific appearance, divorcing the economic from the social domain and giving precedence to the former.

The assumptions of Ricardo's rent theory are open to question and Schumpeter (1986:668) accuses him of

> infect[ing] his followers with the Ricardian vice, that is, with the habit of establishing simple causal relations between aggregates that then acquire a spurious halo of causal importance, whereas all the important (and, unfortunately,

> complicated) things are being bundled away in or behind these aggregates.

For example, Malthus, on whose population theory it was based, ignored the fact that mankind has never reproduced at anything like the maximum biological rate and, relying on American data, which did not distinguish between population increase due to reproduction and due to immigration, postulated that a population would double every 25 years, implying a growth rate of approximately 3% p.a. However, Blaug (1997:68) cites a calculation that if the world's population had grown from a single couple in 10000 BC at a rate of just 1% p.a., the population would currently be approximately 1.5×10^{52} or 15 followed by 51 zeros. This compares with an actual population of approximately 7.2bn or 7.2×10^{9} (Population Reference Bureau 2015). Not only has Malthus's argument concerning population growth proven to be erroneous, but his assumption concerning the limitations to the rate of increase in food production, from which his law of diminishing returns derives, is similarly flawed, and failed to consider the impact of improved technology (Hunt 1979).

In the first edition, Malthus relied solely on famine and hunger as a means of checking population growth, however, in the second edition, he added a new check of 'the [moral] restraint of marriage which is not followed by irregular gratification', i.e. the postponement of, and complete abstinence before, marriage. Malthus was therefore able to assert that rising living standards proved that the population was exercising moral restraint, thus making his argument completely circular (Blaug 1997).

Ricardo's rent theory was highly influential in the evolution of the techno-rational school of economics and even those, such as J.S. Mill and Alfred Marshall, who were temperamental allies of Smith, were attracted by the intellectual rigour of the theory and attempted to incorporate it into a larger moral philosophy (Landreth & Colander 2002). However, another highly influential economic theorist of the mid 19th century was Karl Marx, whose theory of labour value was built on classical value theory, which held that it derived from *production*, i.e. raw materials and the labour expended in order to transform them into products (Häring & Douglas 2012). For classical theorists, such as Smith, wages were determined by the relative bargaining positions of workers and capitalists (Häring & Douglas 2012) and exploitation arose because labourers did not have control of the means of production. Labour therefore became a commodity which could be traded by and for the benefit of capitalists (Schumpeter 1986). In an era when organized labour was starting to assert itself political power classical theory therefore became a threat to capitalists.

In the last 30 years of the 19th century, economists such as Jevons and Menger transformed classical economics into neoclassical economics and one of the most important tools which they developed was marginal analysis (Landreth & Colander 2002). This increased the use of mathematics in economic analysis and therefore became a tool for the development of theoretical, non-contextual, mathematical models along the lines of Ricardo's rent theory. This allowed economists to give the impression that they could predict the future by just using numbers and helped to neutralize the threat of organized labour by taking the issue of power out of economics (Häring & Douglas 2012). Marginal

analysis switched its focus from production to consumption, holding that goods are allocated to uses and users for whom they have the highest utility. The economic theory of labour therefore posited that wages were determined by the marginal utility of labour to consumers.

Marginal analysis also theorizes that an individual's willingness to provide labour is determined by their choice between work and leisure. This depends on the extent to which they are prepared to substitute leisure for work, or *vice versa*, which, in turn, depends on the marginal utility of the income which they gain from substituting work for leisure, or forgo from substituting leisure for work (Stiglitz 1999). In general, people have a declining marginal utility of income, meaning that the utility of additional income is likely to be greater for those on lower incomes since it might be used to purchase essentials rather than luxuries (Stiglitz 1999). This suggests that lower income groups are more likely to substitute work for leisure and higher income groups are more likely to substitute leisure for work (Murphy & Nagel 2002).

The work incentive is therefore maximized by decreasing the remuneration of lower income groups and increasing the remuneration of higher income groups, which runs counter to notions of social justice. Increasing the tax burden on the former, whilst decreasing the tax burden on the latter is therefore one means of achieving this redistribution. However, this assumes that money and consumption are the only motivations for work and ignore personal preferences and I discuss the economic theory of incentivization in more detail in chapter 6.3.

The marginal theory of labour is open to a number of criticisms. Firstly, the marginal theory of labour assumes a perfectly competitive market. Secondly, this conclusion is based on the assumption that utility can be measured and Jevons, Menger and Walras all in fact assumed this (Spiegel 1991). Thirdly, like Ricardo, the marginal analysts posited an opposition between the interests of capital and labour, but assumed that it was possible to separate the marginal products of the contributing factors and Taussig (1924 cited in Landreth & Colander 2002:259) asserted that it was impossible to separate the product of the tool and of the labour using that tool.

The marginal analysts' view of labour was therefore diametrically opposed to that of Marx and draws on Petty and Smith. In the USA economists from the Institutionalist school of economics such as John Commons, Richard Ely and Edward Ross opposed marginal analysis theory in the late 19th and early 20th century, but wealthy benefactors successfully brought pressure to bear on universities to marginalize them and ensure that only the economic theories which served their interests were taught at universities (Häring & Douglas 2012).

The transformation of economics into a mathematical discipline was further developed by Leon Walras and Vilfredo Pareto. Walras's major contribution to economic theory was the development of the general equilibrium theory in his *Elements of Pure Economics (1874)* (Roll 1973). Previous economists had modelled partial equilibrium by considering the relationship between price, supply and demand in a single market, but Walras sought to develop an

equilibrium theory in a world in which there were multiple markets and actors played different roles in different markets. Pareto's best known contribution to economic theory is the concept of the Pareto-optimum, which states that an optimum allocation of resources occurs when it is impossible to increase the utility and welfare of society as a whole, i.e. it is not possible to increase the utility of an individual without decreasing the utility of another individual (Hunt 1979).

Both Walras and Pareto have been subject to much criticism. For example, Blaug considers Walrasian economics in general to be 'thin in substance, stressing form at the expense of substance' (Blaug 1997:568) and the general equilibrium theory in particular to be a cul-de-sac with no empirical contact (1997:570). He qualifies the latter argument by stating that highly aggregated general equilibrium models are neither necessarily pointless nor cannot be illuminating, but simply that the Walrasian approach of reducing an economic multi-market problem to a series of simultaneous equations has proven to be sterile.

Similarly Häring & Douglas (2012) accuse Walras of having formulated a theoretical means of finding the equilibrium, if it existed. Landreth and Colander (2002:313) accuse Walras of not having answered a number of questions concerning general equilibrium satisfactorily, such as whether a general equilibrium solution of the equations is possible, whether the conditions necessary for general equilibrium in the various sectors of the economy are consistent with those necessary for general equilibrium in the whole economy,

how production fits into the model and whether a general equilibrium solution is unique, stable or determinate.

With the Pareto optimum economics reached the culmination of a process which removed all considerations of fairness or wisdom from decisions concerning the allocation of resources on the grounds that it was impossible to make inter-personal comparisons of preferences. It instead focused on maximizing the economy as a whole on the grounds that 'a rising tide lifts all boats' (Häring & Douglas 2012:13). In order to determine a Pareto-efficient allocation of resources it is necessary to aggregate the utility functions of all members of society and the Benthamite postulate that aggregate welfare is simply the sum of the welfare of all individual members of society evades the problem of inter-personal comparison by assuming the one case in which comparison raises no problems, i.e. that the welfare function of all individuals is identical (Schumpeter 1986). However, Bentham also recognised the declining marginal utility of income, which means that even if all individuals did have an identical welfare function, the marginal utility of income would vary unless the incomes of all individuals were identical. Blaug argues that Pareto (1906, cited in Blaug 1997:571) departed from this by rejecting additive utility functions, but that in order to do so it was necessary to confine himself to situations which do not depend on inter-personal comparisons. The concept of the Pareto optimum is therefore restricted to a model in which the optimum conditions of exchange depend purely on intra-personal comparisons of utility.

If the marginal analysts developed the theory of an equilibrium wage rate which provided a justification for reducing the return on labour, Böhm-Bawerk's theory of capital (which greatly influenced Hayek) and the Austrian school of economics provided a similar justification for protecting the interests of capital (Landreth & Colander 2002) and one means of doing this is by minimizing the level of taxation on profits. Böhm-Bawerk held that the economic cycle is caused not by changes in aggregate demand or in the quantity of capital, but in the *structure* of the capital stock (Schumpeter 1986).

Instead of capital being simply an aggregate of capital assets, such as buildings and machinery, it is related to time, because it enables production to take place over a longer period and to be more capital intensive. Labour-intensive production simply requires a short time of preparation during which simple tools are manufactured, whereas capital-intensive production methods require a longer preparatory period during which time sophisticated machinery is produced, which, in turn, also requires a preparatory period during which the components are manufactured. If the output from both methods were identical, entrepreneurs would always choose labour-intensive methods of production, therefore capital-intensive methods of production are only worthwhile if they result in increased productivity and, the higher the rate of interest, the greater the productivity gains which are necessary to make capital-intensive production methods worthwhile (Backhouse 2006).

Böhm-Bawerk argues that agents not only take current prices into account when planning production, but also correctly anticipate changes in prices over

the production period and he was, in particular, concerned with the situation where the price of a good fell over time due to technological progress. The corollary of this is that attempts to stabilize prices will interfere with the establishment of this equilibrium and have damaging consequences. He later extended this principle to postulate the existence of a natural rate of interest to which market forces would ensure the interest rate would return, and that any attempt to change this rate was counter-productive.

Following Böhm-Bawerk Hayek therefore regarded the price system as a quasi-natural law and that depressions occurred when government monetary policy attempted to interfere with this because it interfered with the natural equilibrium of relative prices (Backhouse 2006). The principle that it was impossible for the government to regulate the economy and that it therefore should not attempt to do so was developed into the economic theory of monetarism in the 1960s by the Chicago School led by Milton Friedman. Monetarists argued that changes in the amount of money in the economy are the source of all other changes and that controlling the money supply was the only means by which governments could control the economy, all other changes following ineluctably from this (Smith 1987).

Böhm-Bawerk's theory requires a rigorous theory of how capital stock and production might change in a dynamic economy. For example, his assumption that agents both take current prices into account and correctly anticipate future changes is questionable, since it assumes that they are rational and can infallibly predict the future. The problems of intertemporal equilibrium in a

dynamic economy would require mathematical techniques which would not have been available to him at the time. It is therefore impossible to prove the results he wanted to prove, and, in particular, it can be shown that it is impossible to prove a negative relationship between the rate of interest and the period of capital intensity, a relationship which is important to his theory.

Furthermore, he assumed that capital goods were heterogeneous and that they would become obsolete when production methods changed. Whilst this is true in many cases, there are also many occasions when capital goods can be adapted to new methods, but it is impossible to estimate accurately the proportions which fall in each category (Backhouse 2006). Blaug (1985:545) accuses Hayek (and therefore Böhm-Bawerk) of being guilty of the 'vice of neoclassical economics; the hasty application of static theorems to the real world' and a more useful explanation might be achieved by relaxing any one of his basic assumptions, such as equipment being perfectly divisible and money wage rates and machine prices being constant.

If the marginal analysts, Walras, Pareto and Böhm-Bawerk had completed the transformation of economics into a branch of mathematics based on the use of theoretical, non-contextual models, the economic theories of Keynes provided a contrasting alternative. In his *General Theory (1936)* Keynes saw a significant role for government in regulating the economy and redistributing resources and wealth through interventions such as taxation and public spending (Schumpeter 1986). In the wake of the Great Depression and World War II Keynesian economics became hegemonic and formed the basis of the post-war social

contract (Blaug 1997), but the economic difficulties of the 1970s led to a resurgence of neoclassical economics, which forms the economic basis of neoliberalism and the story of how it was able to triumph is detailed in chapter 5.3.

Both classical and neoclassical economics are constituted by a set of theoretical, economic models which favour the interests of capital over the interests of rent and labour (Harvey 2007). However, if these lead to poverty amongst the labouring class and poverty is regarded as a result of misfortune and/or lack of opportunity this might give rise to a moral imperative to alleviate it through the transfer of resources from wealthier to poorer individuals and taxation is one means of doing this. The economic models favouring capital therefore need to be accompanied by a justification, which ensures that society does not feel guilty about not doing so. This is based on one or both of the arguments that poverty is a result of an individual's personal traits and poor decisions in life, and that the market is inherently efficient, so that any attempt to interfere with its working will be counter-productive in the long run.

The first moral justification for not alleviating poverty was widely held in the 19th century (Davis & Sanchez-Martinez 2014) and can be found, for example, in the writings of J.S.Mill (1909 [1848]), who distinguished between the deserving and the undeserving poor. Whilst he supported using taxation as a means of reducing inequality, he added the qualification that it should not 'relieve the prodigal at the expense of the prudent' and that 'to tax larger incomes at a percentage than the smaller is to lay a tax on industry and economy' (Mill 1909

[1848] V.2.14.). Mill's distinction between the two categories begs the question of what criteria are used to determine who deserves assistance and who does not, which allows the distinction to be discursively framed. In more recent times, Gary Becker (e.g. Becker 1964) has subjected many everyday areas of life, such as choice of career and marriage partner, to a similar rational choice analysis using an economic calculus, meaning that unfavourable outcomes are the result of foolish or irresponsible choices.

The justification for not alleviating poverty on the grounds that any attempt to do so interferes with the working of the market and is therefore counter-productive derives from neoclassical economic theory, which stresses the role of unequal endowments of skills in determining the productivity of an individual in a market-based economic system, although market failure also plays a part. Whilst some targeted measures to alleviate poverty might be justified, neoclassical economists generally regard the efficiency costs of transferring resources to poorer individuals as too high in most practical situations. This principle is encapsulated in the Kaldor-Hicks criterion, which states that

> public policy was justified if it produced gains in excess of losses so that it was possible for winners from the policy to compensate losers, even if [such] compensation did not actually occur
> (cited in Jung & Smith 2007:32-33)

and neoclassical economics generally prioritizes economic efficiency over equality (Davis & Sanchez-Martinez 2014).

In this section I have argued that economics and, in particular, neoclassical economics is not a set of self-evident truths, but a set of constructs which have evolved since the late 18th century. These form the basis of the hegemonic knowledge which underpins the neoliberal state and in chapter 5 I demonstrate how they have been used to enable neoliberalism to assume its current position and in chapter 5 I demonstrate that the tax system has been reformed over the last 35 years to conform far more closely to these.

3.5. Summary

In this chapter I have set out some basic concepts and themes which I develop in later chapters. First, I demonstrate that in order to live in peace and harmony and avoid a brutal and solitary existence Man needs to put in place some form of governing regime (state) which requires certain structures, such as arrangements to ensure national and personal security. The state may, if there is a consensus, operate in other areas of individuals' lives, such as education, healthcare or the alleviation of poverty and reduction in inequality. These structures are generally financed by levying taxation on individuals and the debate on the extent of the state's role therefore becomes inseparable from the debate on how much tax must be raised and the amount of revenue which each individual or group of individuals should contribute. Consensus is reached through a discursive process and I argue that this is heavily influenced by power relationships between individuals and the state and between different groups of individuals. Power relationships between individuals are mediated through taxation, since this involves a transfer of resources between individuals and the state. Furthermore, power relationships between different groups within society

may also be mediated through taxation, insofar as a dominant group can persuade the state to act in its interests and at the expense of other groups in society. In chapter 4 I use a series of historical vignettes to illustrate that the connection between taxation and power relationships has been evident in all state forms in Britain since the 12th century.

In any state form the state will exercise power in an overt fashion through the legitimate authority granted as a result of the above discursive process. However, power may also operate covertly and I have used a three dimensional model of power (Lukes 2005) as a framework for analyzing its operation. Whilst the covert operation of power may be found in any state form, in chapter 5 I demonstrate the UK in the late 20th and early 21st centuries strongly characterizes a neoliberal state in which covert exercise of power has assumed a particularly important role and economic, and in particular neoclassical economic, theory is a principal means of doing so. In this chapter I have set out the principles from which it derives to demonstrate that this rests on assumptions which can either be shown to be false or are, at least, questionable. I therefore argue that neoclassical economics is a set of constructs rather than immutable laws and that its hegemonic status in the neoliberal state is an example of the construction of knowledge.

CHAPTER 4: STATE FORMS AND TAXATION

4.1. Introduction

> *The spirit of a people, its cultural level, its social structure, the deeds its policy may prepare – all this and more is written in its fiscal history, stripped of all phrases. He who knows how to listen to its messages here discerns the thunder of world history more clearly than anywhere else (Schumpeter 1991 [1918])*

In chapter 3 I argued that taxation is the most direct and one of the most important nexuses between citizens and the state and that the taxation system will therefore reflect the power relationships between different groups in a particular society. In this chapter I demonstrate this by presenting a series of historical vignettes from the 12th century to the present day to illustrate the evolution of the state and its relationship with individuals as mediated through taxation.

As well as demonstrating power relationships between various groups, these vignettes also illustrate how knowledge has been constructed to hold these relationships in place, and that, despite this, power can never be absolute. Power relationships are therefore never immutable, and these vignettes illustrate how these have shifted over the ages. There is a dynamic relationship between these shifts and the construction of knowledge, since the shifts create pressures on and tensions within the existing society and new forms of

knowledge are proposed to legitimize these, providing rationalizations for the actions and aspirations of newly emergent classes and the new power relations.

This chapter has the following sections. In chapter 4.2. I start this historical review with the feudal state and the signing of Magna Carta in 1215. This is followed by the emergence of the mercantile class in the Middle Ages, which led to the long decline of the feudal state until it was finally swept away by the Industrial Revolution. In chapters 4.3. to 4.5 I concentrate on the liberal state in the late 18th and 19th centuries, leading to the emergence of welfarism in the late 19th and early 20th centuries and the establishment of the Welfare State in 1948.

The liberal state was a doctrine of a limited state, which held that individuals are motivated by self-interest, rather than any notion of the common good and that they are the best judges of this self-interest (Dryzek 2000). The welfare state, in contrast, envisioned a significant, interventionist role for the state, fulfilling social functions such as the provision of education and healthcare and the alleviation of poverty (Jones 2000). The neoliberal state is in many ways, as its name suggests, a return to the liberal concept of the minimal state with a rejection of the idea of state planning and the notion that the state should intervene in areas such as social justice and a belief that the regulation of society should be left to market forces (Plant 2004). Chapter 4.5. ends by briefly discussing the economic and political forces which led to the overturning of the post-war consensus and the emergence of the neoliberal state. Like the liberal state, the neoliberal state is a state form in which the formal role of the state is limited but,

unlike its predecessor, it seeks to exercise power covertly (see chapter 3.3.) through the construction of a hegemonic knowledge based on neoclassical economics (see chapter 3.4.) and I develop this further in chapter 5. This is followed by a summary in chapter 4.6.

4.2. The Feudal State and Its Decline

Feudalism in England, Scotland and Wales evolved from the Roman slave economy and was a set of mutual obligations between serfs and feudal landlords, whereby the serf was protected by the landlord in return for certain economic and social provisions. The system was controlled by the monarch, who had the power to transfer feuds[1] from one lord to another (Gill 2003). Rulers required resources in order, for example, to run the royal household and conduct military campaigns. When, in the 12th and 13th centuries, revenue derived from the ruler's own estates became insufficient to finance these ambitions, taxation became a means of raising the additional revenue (Frecknall-Hughes & Oats 2007). For example, feudal overlords were obligated, amongst other things, to supply knights to form part of the ruler's army and the system of *scutage* allowed knights to buy their way out of this obligation by paying a sum of money which enabled the ruler to hire mercenaries in their place.

The feudal state was strictly socially hierarchical in nature and the taxation system reflected this structure, since the obligation to pay dues arose by virtue of an individual's position in that hierarchy (Gill 2003). The payments, which

[1] A fief or land held on condition of service (Chambers 1988)

were often in kind, therefore represented the monetarization of social obligations. The payment of these feudal dues is an early example of Lukes's (2005) first dimension of power, since this obligation was backed by the threat of coercion with the monarch able to deploy soldiers to enforce payment. The justification for this system was that the hierarchy was ordained by God and that the sovereign and feudal overlords occupied their respective positions by Divine Right and therefore this is also an early example of the exercise of power through the construction of knowledge.

This system was also an early demonstration that power can never be absolute (Foucault 1978 [1976]). Firstly, practical considerations of collecting the various dues required the monarch to gain access to the general populace. This required the consent of the landed magnates, although once consent had been given the monarch could determine the nature of the taxes, how they should be collected and who should be exempt. The need to gain the consent of the magnates opened the way to the development of Parliament and its emergence stimulated the development of state administrative institutions (Gill 2003). By the end of the 12th century the state could run even in the absence of the monarch when he was away on an extended military campaign (Gill 2003).

Secondly, there always exists the potential for resistance if those on whom the dues are imposed are prepared to resist in an organized fashion. Taxation has often been the issue behind which a general sense of grievance has coalesced into resistance. The signing of Magna Carta in 1215 is an early example of this; whilst the general view of Magna Carta as a watershed in the development of

the rule of law in the UK is justifiable, in its time the document was intended to redress specific, largely financial, grievances of the barons (Frecknall-Hughes & Oats 2007). For example, the barons opposed the doubling of the rate of *scutage* from 20 shillings (£1) in 1209 to 40 shillings (£2) in 1211. This was widely viewed purely as extortion, particularly since many of King John's later campaigns were of doubtful military value and the campaigns of 1204 and 1215, for which *scutages* were collected, never took place (Sabine 1980). A hypothecated feudal due had therefore become a regular and arbitrary levy, and clause 16 of Magna Carta stipulated that the consent of the common council of the kingdom be obtained for the levying of *scutages* and laid down the procedure for summoning its members. The effectiveness of this clause in limiting the power of the monarch can be seen by comparing the eleven *scutages* of King John's 17-year reign with the ten *scutages* levied during the 56-year reign of his successor, Henry III (Sabine 1980).

Magna Carta is therefore an early example of how power between elite citizens and the state is mediated through taxation since the disposition of power between the monarch and the barons centred around the amount of the barons' financial obligations and the manner in which they could be imposed. However, it did not alter either of the central characteristics of the feudal state: that mutual obligations between individuals were determined by their respective social positions and that the apparatus of administration formed part of the royal household. The modern state began to emerge when these conditions started to weaken and a sense began to evolve of the state as an entity separate from the ruler, whose legitimacy rested in its institutions (Gill 2003). The following

section analyses the forces which led to the decline of feudalism and the start of the emergence of the modern state.

The Decline of Feudalism

If Magna Carta brought about a shift in power from the sovereign to the feudal barons, the Black Death, which reduced the population of Europe by an estimated half in the 14th century, seriously weakened the feudal system, because it left very few peasants to work the land in many areas (McNally 1988). This greatly increased the bargaining power of those who survived, with wages rising and property prices falling as a consequence (Bragg 2003). By the 15th century, peasants succeeded in obtaining stable long-term leases and food prices rose substantially, enabling them to accumulate surpluses during good years as protection against the bad years. The more economically successful peasants were able to buy more land and livestock and improved implements.

This process was accelerated after 1536 when large tracts of land seized from the Church were sold by the Crown and by the early 17th century successful peasants had emerged as a new class of landed gentry. Furthermore, the increasing specialization of the larger farms and the emergence of industries such as tanners, weavers, clothworkers and ironmongers, particularly in less arable areas, such as the Midlands, gave the market an increasingly important role in determining prices, wages and conditions (McNally 1988) and the treatises of Mun and Petty, which I discussed in chapter 3.4. provided a theoretical underpinning for the relationships between these.

As the economy moved away from a purely agrarian feudal structure, taxation evolved from the payment of feudal dues, although the capacity of the state to raise taxes was largely limited to the taxation of land and commodities and levies and tolls on the transport of goods (McNally 1988). Once again, the taxation system reflected power relationships in society, since low levels of taxation were one of the concessions offered to the new gentry class by the Tudor monarchs, who reigned from 1485 to 1603, in order to gain their support as a balance to the power of the major nobles (McNally 1988). This was therefore not underpinned by any knowledge as a rationalizing discourse, but was a purely pragmatic move to 'buy off' and gain the support of an increasingly influential class in society. This illustrates the Gramscian (1971) principle that a dominant group will often cede some of its power in order to ensure its continued dominance.

If dominant groups refuse to cede any power the result will often be conflict. In 1603 the Tudor dynasty was succeeded by the Stuarts, who reigned until 1714 and this period saw both the English Civil War and the Glorious Revolution of 1688. These can be viewed as rebellions by the gentry against attempts by the Stuart dynasty to wrest back power from them (McNally 1988); such conflict can force the dominant group to cede power anyway. For example, out of the Glorious Revolution emerged the Bill of Rights in 1688, a charter which, like Magna Carta, enshrined a transfer of power to Parliament and therefore represented the institutionalization, rather than the personalization, of power (Cruickshanks 2000).

Once again, like Magna Carta, taxation issues were central to the Bill of Rights. It stipulated, amongst other things, that the sovereign could not levy taxes or raise a standing army, which was one of the most important items of expenditure for a sovereign, without the consent of Parliament, and that Parliament must be held frequently (Cruickshanks 2000). The restrictions on the sovereign levying taxes or raising a standing army represented a limitation on the exercise of power through taxation by decree, whilst the requirement to summon Parliament frequently prevented the sovereign from frustrating Parliament from exercising its power to raise, vary or repeal taxes by refusing to summon it. Although the Bill of Rights represented a significant transfer of power from the sovereign to Parliament, certain clauses, such as preventing the sovereign from shortening or prolonging periods of Parliament, or judges holding office on condition of good behaviour rather than royal pleasure were dropped. The reforms therefore fell far short of what the Whig radicals had desired and the sovereign remained in a strong position. (Cruickshanks 2000).

Whilst the Bill of Rights had great symbolic importance, a more significant power shift was the emergence of the mercantile class in the late 16th and early 17th centuries, which created a new power base through its wealth. This process began around the middle of the 15th century and one of the major factors was the flow of gold from the Americas, the prices in Europe tripling between 1500 to 1650 (Screpanti & Zamagni 1993). However, it gathered pace in this period due to the exigencies of financing wars, since Britain was at war for 29 of the 68 years between 1688 and 1756 and it was the new mercantile class who largely financed the wars by lending money to the state, which

somewhat usurped the power of the landed gentry. Furthermore, foreign trade, particularly with the Americas, was increasing, and trade in general came to be seen as the driver of the economy (Dickson 1993).

The growing importance of trade brought with it a need for a peaceful and stable state which was governed by the rule of law and this brought about a shift in power relations to the mercantile class. Civil society is based on repeated acts of obedience and the emergence of the mercantile class therefore posed the problems of how civil society can be achieved where this class has wrested a large measure of power from an absolute monarch and how it can be reconciled with egoistic and acquisitive economic behaviour (Screpanti & Zamagni 1993). In the 17th century new forms of knowledge therefore emerged to address this problem.

A result of the desire for stability and the rule of law was that philosophers started to conceive of alternative models of statehood from one in which monarchs and feudal overlords ruled over their subjects by Divine Right and, in return, had a duty to govern in a benevolent manner. This was a philosophy which was often known as the ‘Christian Prince’ and was espoused by, amongst others, Erasmus (1997 [1532]). In countries which retained absolute monarchies, such as France, the concept of ‘natural law’ evolved, which circumscribed the monarch’s absolute power by positing the existence of natural laws of divine origin to which all, including the monarch, were subject (Screpanti & Zamagni 1993).

Philosophers such as Hume and Locke argued that Man experiences a natural 'benevolence' or 'moral sentiment' towards his fellows, meaning that there is no need for an external actor, such as God or the state, to impose order (Screpanti & Zamagni 1993:55-56). However, Hume and Locke disagreed on the role of the state. Hume (2015 [1748]) argued that governments are founded on violence rather than contractual agreement, but Locke (1946 [1690]) wrote that all men are naturally in 'a state of perfect freedom to order their actions, and dispose of their possessions and persons, as they think fit' and '[a] state also of equality, wherein all the power and jurisdiction is reciprocal, no one having more than another' (Locke 1946 [1690]:5). However, God has driven men to associate with each other to form society, and that, in order to do so and preserve their natural state of perfect freedom and their property, it is necessary to surrender their natural power to the community, which is empowered to resolve disputes in an impartial manner (Locke 1946 [1690]:71). Civil government is therefore where individuals live together in a body with a common established law and judicature with the power to resolve disputes. Individuals therefore possessed inalienable rights of liberty and equality and the relationship between the state and its subjects was a *social contract*, governed by the rule of law, under which both rulers and subjects had rights and obligations.

This disagreement over the role and nature of the state meant that Hume and Locke had very different views on the nature of taxation. Hume's concept of a state being founded on violence means that it had no legitimate right to levy taxation, but under Locke's social contract theory taxation can became part of a

system of reciprocal rights and obligations. Locke (2015 [1690]) wrote that, whilst under the principles of natural law, Man has a right to retain to retain the product of his own labours, the act of uniting into a community means that individuals must be prepared to surrender part of their power to the will of the majority in return for enjoying its benefits and that they must therefore be prepared to pay for these in the form of taxes.

This difference has had a profound influence on debates on the relationship between individuals and the state, from which the state's right to levy taxation is derived. The Lockean concept of the state might provide a basis for an extensive role for the state and a redistributive tax system such as the Welfare State which I discuss in chapter 4.5., whilst under the Humean concept the role of the state and the scope of taxation is much more limited. The liberal state discussed in chapter 4.3 and the neoliberal state discussed in chapter 5 are therefore much closer to the Humean concept and it is also a philosophical basis for libertarianism, which provides a moral justification for tax avoidance, which I discuss in chapter 8.4.

The transformation of the nature of the state accelerated at the end of the 18th century, when in the space of roughly 40 years, the Industrial Revolution transformed Britain from an agricultural country into a predominantly industrial one. This brought about the migration of a large proportion of the population from the countryside to the new industrial towns and cities, which seriously weakened the structures of pre-industrial society and created a new class of

wealthy industrial entrepreneur, many of whom had risen from humble origins (Tanzi 2011).

Whereas in America a new state could be established without the traditional power bases, in Europe the new mercantile and industrial class either had to overthrow them or find a way of coexisting with them. The political history of continental Europe in the late 18th and 19th centuries was dominated by cycles of revolution and counter-revolution, however these cycles were conspicuously absent in Britain in this period. Whilst there was a certain amount of civil unrest, for example in the 1830s, this was minor compared to the turmoil in Europe (Daunton 2002a).

This did not mean that in the early 19th century there was widespread contentment amongst the working and middle classes in Britain and a consensus concerning the legitimacy of the state, but the political elite dealt with these problems in a very different way from those in Europe. There was no revolution in distributive power relations and this period saw only gradual representative reform. The British story is therefore one of how the aristocracy, once again, heeded the Gramscian (1971) principle discussed in chapter 3.3. of neutralizing resistance in order to ensure that their hegemony was not threatened. There was conflict between the aristocratic ‘old regime’ and the petite bourgeoisie, but by the 1840s the two classes had largely merged to form a single capitalist ruling class (Mann 1993) The aristocracy did not so much ‘buy off’ the new mercantile class as absorb it into itself, since industrialists and financiers tended to distance themselves from industry and commerce once

they had made their fortune and aspired to a life as English country gentlemen (Wiener 1980).

The coexistence of the aristocracy and the mercantile class was made possible by the creation of a liberal state, which was a pragmatic compromise between the established and the emergent classes, rather than being underpinned by any theoretical justification. The separation of the economic from the political and social spheres was central to this compromise and they therefore sought to achieve this by compartmentalizing life, separating the economy from the state and the church from the polity (Daunton 2002a). In this way liberty could be achieved by limiting the power of any particular group (Crouch 2011), so that no group could dominate others. The imposition and administration of taxation is the prerogative of the state and was potentially a means by which the state could exercise power over other spheres through the redistribution of resources. Section 4.3. therefore analyzes how the issue of taxation was managed in the liberal state as part of this compromise.

4.3. Taxation in the Liberal State

> *If we want things to stay as they are, things will have to change.*
>
> *(Lampedusa 2007 [1958])*

This quotation comes from Lampedusa's only novel and best known work *The Leopard* (2007 [1958]), which chronicles the struggles of the Sicilian aristocracy to cling onto power during the *Risorgimento*. The character Tancredi here recognizes that if an elite is to remain in power it cannot do so through force

alone, but must attain legitimacy in the eyes of those they rule over. In order to do so, it is necessary make changes or concessions to the general population, whilst trying to ensure that their hegemony is not threatened. I argue that the contrasting histories of the relationship between the people and state during the 19th century in Britain and Europe illustrate that the British aristocracy understood this better than their counterparts in Europe.

At the start of the 19th century relations between the aristocracy and the bourgeoisie were not harmonious. Daunton (2002a) depicts a cartoon entitled 'State of the Nation' published in 1829 showing a wooden beam labelled 'Manufactures and Commerce' which had broken under the strain of the number of people who were dependent on it. Clinging to the broken beam were four labourers dressed in rags, clinging to the legs of the labourers were two prosperous businessmen and, at the bottom of the cartoon clinging onto the coat-tails of the businessmen was a plump individual wearing the robes and mitre of a bishop and peer. If the cartoon itself did not spell out the message clearly enough, the caption was quite explicit and read:

> Manufactures and commerce support the
> workmen, they the merchants and Masters who
> are the chief taxpayers and thereby support the
> great tax eater Church and State
>
> (Daunton 2002a:318)

The Industrial Revolution had increased the influence of the mercantile class at the expense of the aristocracy and this cartoon indicates the emergence of an antagonism between these classes, or between the interests of capitalists and landlords, an antagonism for which the economic theories of Ricardo (1815) (see chapter 3.4.) provided a theoretical justification. The mercantile class became resentful that the aristocracy were being favoured at their expense and one area where this had become apparent was taxation.

During the 18th century there were few political problems and a high level of tax compliance despite the emergence of a 'fiscal-military state' in which Britain became one of the most heavily taxed and indebted countries in Europe (Daunton 2002a). During this period the share of national income which was appropriated as taxation remained low, rising from 8.8% in 1700 to 12.9% in 1800 (O'Brien 1988) and the fact that this did not cause political problems may be attributed to the credibility of the state's commitment to repay the loans taken out to finance the Napoleonic wars and a high level of convergence between the purposes of the state and the interests of political and economic elites. This trust gave the state the capacity to levy higher rates of tax without encountering resistance (Hoppitt 2002), but it started to weaken during the wars with France in the late 18th and early 19th centuries and the return to peace.

During this period taxes rose to 23% of national income, which raised alarm, but could be fairly easily justified whilst hostilities continued. By 1815 this justification was no longer available and disquiet over the threat to liberty from the fiscal-military state and the level of debt and taxation increased, despite the

reduction in defence expenditure. The blame for this now turned inwards towards the costs of sustaining the menace of militarism and a luxurious court and rich financiers and landowners who benefitted from pensions and sinecures and who subverted the social order. This view could unite the working and middle classes and those who might have little sympathy for radicalism. This engendered a lack of trust in the taxation system and it became necessary to renegotiate the fiscal constitution to restore trust in the state and the legitimacy of the tax system (Daunton 2002a).

The result of this renegotiation was the emergence of the liberal state in which power was diffused between the aristocracy and the bourgeoisie through the separation of the political and the economic spheres, with the aristocracy being allowed to largely retain control of the former, but control of the latter being ceded to the new industrial and mercantile bourgeoisie. This is reminiscent of Gramsci's (1971) argument (see chapter 3.3.) that hegemonic groups will often make concessions and cede some of their power in order to retain their position. This also meant that economic activity was not directed by a superior authority and Smith's (2015 [1776]) concept of the invisible hand provided the theoretical justification for what was, in practice, a pragmatic compromise and the evolution of the tax system reflected these power relationships.

In the early 19th century, not only did taxation levels rise but the newly-influential mercantile class started to challenge the structure of the tax system. During the 18th century the share of direct taxes as a proportion of total taxes was never higher than 30%, but had fallen to roughly 20% by the 1790s (Institute of

Historical Research 1993). The greater part of tax revenue in this period was therefore levied through indirect commodity taxes, largely for practical reasons, however the newly-influential mercantile class felt that this level of indirect taxation was detrimental to their interests. The campaign against indirect taxes and, in particular, against the Corn Laws which were enacted in 1815 to impose a protective tariff on imported corn, was a key conflict between these classes. The tariff raised the price of food, which was detrimental particularly to the interests of labourers, but also created upwards pressure on wages, which was detrimental to the interests of capital (Perelman 2015) and the tariff therefore privileged the interests of the landed aristocracy.

The victory of the Free Trade Movement and, in particular, the Anti-Corn Law League, led to their repeal, which confirmed the economic ascendancy of the new mercantile class. The consequences for taxation policy were profound, since the repeal of the Corn Laws successfully prevented serious consideration of the introduction of a broad-based consumption tax for the next 100 years and meant that the state was forced to reintroduce income tax in 1842 (Howe 1997). This is an illustration of Lukes's (2005) second dimension of power, since taxation options which were antithetical to the interests of the mercantile class could not be seriously discussed. Pitt had introduced income tax in 1799 in order to fund the war with France, but it was seen as a special levy which was widely denounced as inequitable and inquisitorial (Redford 1960:185), and it was repealed in 1816 after cessation of hostilities. This made the state increasingly reliant on direct taxes. Between 1831 and 1835 direct taxes

accounted for 25.2% of total central government revenue, but by 1911-14 this had risen to 52.3% (Daunton 2002a).

Peel did not view the reintroduction of income tax primarily as a means of increasing government revenue, but as a means of creating political and social stabilization by creating balance in the tax system so that it was seen as neutral between interests. He believed that his statesmanship lay in a progressive freeing of the state from the power of vested groups and that the most powerful state was the minimal state, which was free from class interests and patronage (Howe 1997). He was careful to establish trust by controlling public spending and constraining the role of the state and established administrative principles to achieve this, such as the rejection of the hypothecation of taxes and *virement* (where a surplus in one area could be used to fund a deficit in another area) (Daunton 2002a).

His model of taxation aimed to raise maximum revenue from relatively few, but very productive, sources and offer as little encouragement as possible to vested interests. By abolishing sources of indirect taxation, he purposely sought to restrict the resources available to the government (Howe 1997). Income tax was conceived as a temporary tax, which was a socially equitable means of covering additional expenditure until tax revenues increased through economic growth in a free market, at which point it could be abolished. The restriction of the franchise also meant that voters were also taxpayers which meant that they had to finance the policies they voted for and would therefore be very aware of the costs of supporting particular policies, rather than simply the benefits. It was

therefore also a means of creating political responsibility which would help to constrain the state (Daunton 2002a).

In this section I have demonstrated that by the mid 19th century the industrial bourgeoisie had triumphed over the landowner class in many areas of life, with the establishment of the principle of free trade as well as reforms in the major institutions such as the Civil Service, the church, Oxford and Cambridge and public schools. However, unlike in countries such as France, the aristocracy managed to retain political power and the state was still dominated politically by the old regime (Mann 1993) and the restriction of the franchise was one of the main means of achieving this.

This compromise was reflected in the tax system, which reflected the priorities and interests of the mercantile class. For example, there was a reliance on direct taxes, with broad-based consumption taxes being abolished, and the level of taxation, particularly on capital, was kept low and this reflects Ricardian rent theory which I discussed in chapter 3.4. However, the old regime of landowners was not able to retain power without making any political concessions, and the result of this was the extension of the franchise in 1832 and again in 1867. The latter of these marked the start of the rise of the power of the working class, which threatened the compromise between the aristocracy and the bourgeoisie and led to the emergence of welfarism. Once again, the shift in power relations was reflected in the evolution of the tax system and the loosening of the connection between taxation and the franchise was one of the factors which put pressure on the fiscal constitution. Chapter 4.4. therefore

examines the forces leading to the rise of welfarism and the consequences of this for the tax system.

4.4. The Rise of Welfarism

By the latter part of the 19th century the mercantile class had progressed from being parvenus challenging the power of the establishment to being themselves part of the establishment and sources of domination. From the latter part of the 19th century workers sought greater power in the same way that the mercantile and industrial classes had done previously and social critics started to criticize the domination of money and commercial values over social life (Crouch 2011). This created a dichotomy in the liberal tradition between the pursuit of rights and equality, which tended to bring liberals into a sometimes uncomfortable alliance with the socialists, and economic liberalism, which emphasized the liberties of property ownership and market transactions. This brought liberals into an alliance with the traditional power bases it had originally opposed (Crouch 2011).

Although the industrial bourgeoisie had achieved economic power by the 1860s, the franchise had not been significantly widened since the beginning of the 19th century and political power was therefore still concentrated in the hands of the aristocracy (Daunton 2001). In 1867 Gladstone introduced electoral reform which aimed to give the vote to skilled workers who could show ‘self-command, self-control, respect for order, patience under suffering, confidence in the law [and] regard for superiors’ (Parliamentary Debates 1863 cited in Daunton

2001:152). However, these proposals failed and the franchise was extended much further than Gladstone had intended, thereby giving the vote to many non-taxpayers, which created circumstances where public choices and private costs might become separated, since non-taxpaying voters could vote for policies which would be financed by others. This threatened the reliance on income tax and the deliberate policies of keeping the burden on middle class incomes at a modest level. A democratic state dominated by the propertyless working class might therefore loosen the shackles of the state by pursuing policies designed to reduce inequality and threaten the separation of economics and the state for which liberals had fought (Crouch 2011).

Welfarism in the UK began with the introduction of universal, compulsory education in 1870 and reached its highpoint in the UK in 1948 with the creation of the Welfare State and the National Health Service. Although philosophers such as Mill supported many welfarist aims, such as universal education, much of the impetus for welfarism came from practical necessity. As early as 1832 the reformer James Kay-Shuttleworth (cited in Daunton 2007:488) remarked that '[t]he preservation of internal peace…depends on the education of the working classes'. There was still lingering opposition to the education of the lower classes and a belief that their education should be distinct from that of their social betters. The church saw state education as a threat to its vested interests as a provider of education, others feared that encouraging the working classes to think would lead to dissatisfaction and revolution (Daunton 2007), whilst others, such as William Godwin (1793), did not oppose mass education itself, but saw state education as a form of indoctrination. However, by the mid 19th

century there was a general acceptance amongst the dominant classes that the masses should be educated (Stephens 1998). Practical reasons for the establishment of universal education included the increase in mechanization, which meant that Britain would be at a competitive and military disadvantage if it did not have an educated workforce (Murphy et al. 2008). The provision of universal education was therefore an expenditure choice motivated partly by liberal, welfarist ideals and partly by the need to make workers economically useful and this instrumentalist rationale is a key feature of the neoliberal state which I discuss in chapters 5 and 6.

The establishment of mass education was the first great welfarist reform, but this was followed in the early part of the 20th century by the introduction of national insurance, pensions and social welfare payments. Once again, the reasons for these were a combination of the political and the pragmatic. The late 19th and early 20th centuries saw the power of the aristocracy and the bourgeoisie coming under threat from the rise of the Labour movement in the UK and of Communism in many parts of Europe. This again illustrates that power is not absolute and power relationships are not immutable (Foucault 1978 [1976]). This gave rise to fears that revolution could spread if the lives of the working classes were not improved, once again illustrating that hegemonic groups might make concessions by ensuring that the position of potential troublesome groups was made comfortable enough to neutralize resistance (Gramsci 1971).

On a more practical level, the realization dawned that the very high infant mortality rate (the proportion of infants dying before their first birthday), which peaked at 163 per 1,000 live births in 1899 was detrimental to Britain's interests. It required 'fit young men' to fight in the Boer War and, in its early stages 35% of those enlisting were found to be unfit for service. Germany was also known to be preparing for war, which potentially required more men to enlist. Furthermore, the expansion of the British Empire meant that men were required to serve in its colonies (Jones 2000). The Balfour Commission set up in 1904 to investigate this problem found that the main reasons for this included insanitary home conditions and malnutrition and that many of those who survived grew up to be sickly adults (Jones 2000). Social reform and the relief of poverty therefore became a priority and the Liberal government of Campbell-Bannerman and later Asquith, which was elected in 1906 with a majority of 356, enacted a number of measures which demonstrated a commitment to social reform, including the introduction of pensions and national insurance (Jones 2000).

The expansion of social provision by the state was therefore motivated partly by practical considerations, enabling the aristocracy and bourgeoisie to make the workers economically and militarily useful. However, a normative debate also started as to the extent to which income and resources *should* be redistributed, and the redistribution of income was advocated by, amongst others, Adolphe Wagner (Tanzi 2011). In the 18th and 19th centuries the attitude was that the wealthy were the only section of society which could accumulate wealth and,

whilst a minimal level of support for the poor was contemplated[2], it was largely accepted that the entitlement to earnings was akin to a natural law and that this distribution should be left to the market, a view shared by both Smith and Mill (Musgrave 1996). However, in the 20th century the rise of the labour movement and the Labour party gave rise to the notion that the distribution of income largely arose from social factors and that taxation had a role in redistributing wealth more fairly. Whereas the 19th century was concerned with equality of *opportunity*, the 20th century became more concerned with equality of *outcomes* (Tanzi 2011).

The late 19th and early 20th centuries had seen a rise in the power of the working class and the desire to improve their conditions arose partly from the realization that poverty caused problems which affected the whole of society and partly from the rise of the Labour movement and the threat of revolution. This shift in power relations was reflected in a redistribution of resources in favour of the working class, since the expansion of the role of the state meant that it became necessary to raise a higher level of tax revenue, most of which was paid by the upper and middle classes, and this financed a higher level of social provision, which largely benefitted the working class. Taxation became inextricably linked with welfare economics and the construction of a social welfare function (Musgrave 1996).

Despite the increases in tax rates, the structure of the tax system remained largely unchanged through the early 20th century and the inter-war period with a

[2] In 1834 Parliament voted in the Poor Law and soon after one sixth of the population was receiving some form of assistance (Tanzi 2011:40).

heavy reliance on direct taxation. In 1910 tax rates were still relatively low, but these rose significantly over the following 10 or 20 years, although the highest marginal rates were paid by only a very small percentage of taxpayers. These changes are summarized in the following table.

Table 4.1: Summary of Tax Rates and Thresholds 1910-1930

	1910	**1920**	**1930**
Basic rate	6%	30%	22.5%
Number of higher rates	1	9	12
Top marginal rate	8.5%	60%	60%
Threshold of top marginal rate	£5,000	£30,000	£50,000
2015 equivalent (approx[3])	£200,000	£1,200,000	£2,000,000

(Finance Acts 1910, 1920, 1930)

The balance of direct and indirect taxes also changed significantly in this period. In 1913/14 indirect taxes accounted for 42.5% of total tax revenue, but this fell to 24.9% in 1919/20, although this rose to 35% by 1929/30 (Daunton 2002b). The yield from income tax rose from £34m before World War I to £585m in 1918 (Sabine 1980) and between 1913/14 and 1925/26 the proportion of tax revenue raised by income tax and super-tax had risen from 27% to 43%, even though commentators at the start of the war had said that the trend toward direct taxes had already reached its limit (Daunton 2002b).

[3] Based on RPI figures from Office for National Statistics (2015a).

Whilst the increase in military expenditure necessitated by World War I was a major cause of the increase in the level of taxation, the fact that taxation did not fall significantly when peace returned cannot be separated from two events which significantly shifted the balance of power. Firstly, the Parliament Act 1911 curtailed the power of the House of Lords and gave the House of Commons legislative supremacy for the first time, which was a result of the House of Lords' opposition to Lloyd George's 'people's Budget' of 1909 (Daunton 2002a). This shift in Parliamentary power allowed the Liberals to introduce both differentiation, i.e. different rates were imposed on different types of income, and graduation, i.e. progressive rates (Daunton 2002a). This drastically curtailed the power of the aristocracy, again illustrating that power can never be absolute (Foucault 1978 [1976]) and the success of the Gramscian (1971) strategy of hegemonic groups making concessions to ensure continuation of their hegemony cannot necessarily be relied upon indefinitely.

Differentiation and graduation both allowed the government to ensure that the burden of increased taxation was largely borne by specific groups in society and, together with the introduction of new land taxes and increased death duties, this was part of an attack on inherited wealth and unearned income (Daunton 2001). This marked a break with the 19th century fiscal constitution and established the 'ability to pay' principle. Unearned income could thereby be differentiated from morally superior, productive earned income and could therefore fund increased social expenditure whilst retaining the support of the middle classes. The interests of capital were therefore largely protected and the redistribution of resources was mainly from the landed aristocracy to the

working class. Income tax was made more politically acceptable by having a broad base which enabled rates to be kept relatively low for the majority of taxpayers. By increasing children's allowances and introducing wives' allowances, the increased burden fell largely on bachelors earning more than £3 a week (Daunton 2002b) and the government thereby reduced the tax burden on families, whose votes were crucial (Daunton 2002b).

Secondly, in 1918 electoral reform meant that, for the first time, not only that women had the vote (albeit not on equal terms with men, which was not achieved until 1928), but also that there was universal male suffrage. The combination of the two meant that the aristocracy, who had been so successful in retaining power through the 19th century had ceded much of it in the first two decades of the 20th and the last vestige of the link between suffrage and property ownership had been broken (Daunton 2002b). Paying tax could no longer be viewed as an insurance premium for the protection of one's property, but became inextricably linked to welfare politics and post-war fiscal policy therefore needed to take account of the fact that that the working classes were now both taxpayers and voters.

Although tax rates increased, the reliance on direct taxation remained because a number of alternatives to raising revenue through income tax were all rejected for various reasons. A capital levy was rejected because it was feared that property-owners would be forced to sell assets, thereby disrupting capital markets and adversely affecting workers. It was also feared that accepting payment in shares or land might be seen as Labour trying to achieve a

collectivist ideal by stealth (Daunton 2002b). A levy on increases in war wealth was seen as a politically safer alternative than a levy on all wealth, but this was similarly rejected when the post-war boom turned into a depression (Daunton 2002b). The one type of capital levy which was felt to be politically feasible was death duties and the highest rate of estate duty increased from 20% in 1914 to 40% in 1919 and 50% in 1930 (Practical Law 2015). In 1922 the MP Leo Amery advocated the introduction of an indirect tax on consumption and a reduction in income tax on the grounds that reliance on income tax discouraged thrift in every class and broke down the whole capitalist or individualistic economic system (cited in Daunton 2002b), but this was rejected when the election of 1923 suggested that such a shift was unpopular.

The expansion of welfare provision was made possible by the ability to raise sufficient tax revenue without alienating electorally important sections of society. The taxation system therefore largely transferred resources to the working class from the aristocracy by taxing their wealth, thus protecting the interests of capital and the bourgeoisie. However, World War II brought changes to the tax system and a demand for greater equality and welfare provision, which resulted in the creation of the Welfare State in 1948. These changes threatened the inter-war consensus (Daunton 2002b:174-5) since they were concerned less with keeping workers content and ensuring that they were economically useful and more with the egalitarian notion of the redistribution of income. Section 4.5. therefore examines the factors which led to the creation of the Welfare State in 1948 and how a new consensus was established which allowed the state to raise the tax revenue necessary to finance it.

4.5. The Welfare State

During the 1920s and 1930s the world economy went into a depression which threatened the capitalist order and led to the rise of fascism in Europe and Japan, which, in turn, led to World War II (Harvey 2007). After the war, fascism had been crushed and the two overriding considerations in the reconstruction of economies and state institutions were ending the geopolitical rivalries which had caused two world wars within the space of 30 years and preventing a return to the economic conditions which had caused the catastrophic slump of the 1930s (Harvey 2007). These events reinforced the egalitarian principles which emerged before World War II and there was a widespread belief that, in order to ensure peace and prosperity, it was necessary to reach a compromise between the interests of capital and labour. For example, Dahl & Lindblom (1953 cited in Harvey 2007) argued that both communism and capitalism had failed and the solution was to create a blend of state, market and democratic institutions.

There was a commitment to free trade with fixed exchange rates, underpinned by the US dollar. However, domestically a variety of social-democratic parties emerged in Europe in this period, whilst in Japan the USA helped to create a nominally democratic but, in practice, highly bureaucratic state (Harvey 2007). In all of these states there was a consensus that the main priorities were full employment and economic growth and that the state should play a significant role by intervening in, or even replacing, the market, for example in industrial policy and ensuring a high level of social and welfare provision.

In the UK the establishment of the Welfare State in 1948 also had its origins in a change in social attitudes, which can be attributed to both a long delayed response to the Balfour Commission, which was set up in 1905 to investigate reform of the Poor Laws, and to social changes brought about by the depression of the 1930s and World War II. The Balfour Commission deliberated for five years and split into two irreconcilable factions, each producing their own report. The majority faction advocated that the Poor Laws should be reformed, but that the state should only provide a bare minimum, with voluntary agencies providing additional support for the 'more deserving' (Jones 2000:76). The minority faction, led by Beatrice Webb, rejected the idea that poverty was caused by personal failings, arguing that it was caused instead by capitalist society. Their report therefore advocated the abolition of 'the poor' as a class and proposed the principle of 'Administrative Functionalism', meaning that the state should address the underlying causes of poverty, rather than simply alleviating its effects (Jones 2000).

The conflict between these two views had profound implications for the taxation system, since the minority view advocated transferring resources from wealthier to less wealthy taxpayers in order to alleviate poverty, whereas the majority view rejected this redistribution. Neither report's recommendations were acted upon when they were published, but the minority report was a significant influence in the establishment of the Welfare State in 1948 (Jones 2000).
The recommendations of the Balfour Commission also struck a chord with the changes in attitudes which occurred as a result of World War II. This change arose from a belief that '[i]f dangers were to be shared, then resources should

also be shared' and that the shared experience of hardship and danger had reduced the barriers between the classes and had been a 'great engine of social advance' (Jones 2000:104). Furthermore, the aftermath of World War I and the 1930s was at that time still a recent memory and there was a feeling that society had failed the soldiers who had fought in the earlier war and had been promised 'Homes for Heroes'. There was therefore a determination that the broken promises of World War I would not be repeated (Jones 2000).

Wartime conditions had of necessity brought about fundamental changes to much social provision and measures such as the provision of free milk and school meals, was no longer a relief measure for those on low incomes, but a basic social service (Jones 2000). However, wartime conditions also distorted social change, since the war effort took priority over all else and those considered vital to it, such as the armed forces, miners and those working in heavy industry were given preferential treatment, with the sick and elderly low on the list of priorities, but this also engendered a desire to plan for a better society after the war (Jones 2000). The result of this desire was the Beveridge report in 1942 (National Archives 2015 [1942]), which paved the way for the establishment of the Welfare State in 1948. The transition to a new social order faced considerable difficulties, since the immediate post-war period was a time of considerable austerity and food rationing did not cease completely until 1954. In this period and for many years there was a consensus that the Welfare State was a priority and the underlying principles were not questioned (Jones 2000).

However, this level of welfare provision had a price. The inter-war years had seen the level of direct taxation rise to unprecedented levels, but a combination of World War II and the establishment of the Welfare State in 1948 saw tax levels rise ever further. The Finance Act 1945 set the basic rate of tax at 45% and higher rates of tax culminated in a top rate of tax of 97.5%, albeit only payable on income over £20,000 (equivalent to around £700,000 at 2015 values[4]) (Finance Act 1945) and these rates remained high for many years.

Furthermore, not only did direct taxes rise to unprecedented levels, but in 1942 the need to discourage spending made it necessary to introduce a purchase tax along with duties on 'optional expenditure', such as alcohol, tobacco and entertainment, thus breaking the century-old taboo which had existed since the repeal of the Corn Laws in 1846 (see chapter 4.3.). Even Labour and the trade unions, who had traditionally opposed such a tax on the grounds that it disproportionately affected poorer people, decided that income tax could no longer generate sufficient tax revenue and that it was therefore no longer possible to oppose the reintroduction of a broad-based consumption tax (Daunton 2002b). Whereas in the inter-war years governments had been careful to ensure that the burden of taxation fell largely on a few wealthy taxpayers, the post-war era was one of mass taxation and the fact that there was widespread consent to such levels of taxation can be explained by rising post-war prosperity, which meant that after-tax incomes rose, despite the high levels of taxation (Campbell 2009), and a widespread belief in the redistributive principles of the Welfare State (Daunton 2002b).

[4] Based on Retail Price Index (RPI) figures of 7.4 in May 1945 and 258.0 in April 2015 (Office of National Statistics 2015a).

Daunton (2002b) argues that a combination of bureaucratic and political inertia and a consensus amongst the main political parties that the principle of the welfare state was sacrosanct which meant that policies of high government spending and high levels of taxation continued throughout the 1950s and 1960s, although Glennerster (2007) believes that analysts have tended to overstate the degree of political consensus. However, tax rates were not reduced substantially, even when the Conservatives were in power from 1951 to 1964 (Steinmo 2003). The fiscal constitution therefore supported a high level of redistribution of resources from wealthier taxpayers to the less wealthy which could not be seriously questioned. Differences between the two major political parties were merely ones of emphasis, with the Conservatives tending to emphasize personal incentives and Labour tending to prioritize equality and social justice, however the Conservatives were concerned to find ways in which the pursuit of self-interest could be contained within an integrated, cohesive society, which could respond to economic problems and define agreement between different interest groups (Daunton 2002b).

This consensus was not restricted to the UK and elsewhere in Europe, such as in Germany and Sweden, even mainstream centre-left parties abandoned objectives of replacing capitalism with socialism, aiming instead to work within a capitalist system to pursue social goals and minimize shocks to the system through state intervention and Keynesian market management. This was most explicit in Germany, where in 1959 the social democratic party (SPD) adopted the slogan '*So viel Markt wie möglich; so viel Staat wie nötig'* ('As much market as possible, as much state as necessary') (Crouch 2011:7-8).

However, despite the apparent dominance of the welfarist ideals the seeds of its decline or destruction could already be identified and certain strands of the debate on economic policy which emerged in the 1940s assumed greater importance from the 1970s onwards (see chapter 3.4.), providing much of the intellectual justification for the establishment of the neoliberal state, which I discuss in chapter 4. The consensus concerning the high level of taxation required to fund the Welfare State emerged alongside rising post-war prosperity. However, it started to be questioned from the 1960s onwards and, in particular during the economic slowdown of the 1970s. From the end of World War II to the late 1960s inflation was low. The RPI in December 1947 was 30.0 and had risen to 63.2 by December 1967 (Jan 1974 100), giving an inflation rate of 3.5-4% p.a. (Office of National Statistics 2015). However, in late 1967 the Wilson government was forced to devalue sterling and the 1970s was a period when the world economy started to slow down. In the 1970s in the UK a combination of sluggish economic performance, industrial unrest, poor labour relations and the quadrupling of oil prices following the outbreak of the Arab-Israeli War in 1973 led to sharp rises in inflation. This peaked in the UK at 27% in 1975 resulting in taxpayers experiencing decreasing prosperity and ‘bracket creep’, where inflation reduced the real levels of income at which higher rates of tax became payable (Daunton 2002b).

The economic slowdown led to public sentiment increasingly opposing high rates of taxation and an increasing reluctance to fund the Welfare State, with both the Left and the Right abandoning the principle of universalism (Jones 2000). Tanzi (2011:11) describes welfare provision by government as a form of

fiscal illusion, where through propaganda and lack of good information, most citizens viewed it as a bargain, since the benefits were visible and the costs rather less so. In the 1970s the economic downturn made taxpayers more aware of the costs. One of the problems was that the demand for resources was self-expanding. For example, improved healthcare meant that the acute medical problems of middle age were gradually replaced by the more chronic problems of old age (Jones 2000). The problems which beset the post-war consensus and the social values which it embodied therefore left the way open for a new economic and social philosophy which became the basis of neoliberalism to suggest a solution and I discuss the manner in which it achieved its current hegemonic position in chapter 5.

4.6. Summary

In this chapter I have argued that throughout history power relationships in society have been mediated through the tax system and that these have both been justified by the construction of knowledge. In the feudal state dues having the nature of taxation were payable from the peasants to their feudal overlords and from the overlords to the monarch simply by virtue of their respective social positions and power was exercised in an overt manner in order to ensure compliance. The long decline of the feudal state led to the emergence of the new mercantile bourgeoisie class and by the 19th century a liberal state had emerged in which the tax system reflected their ascendancy by privileging their interests by levying low rates of taxation and the absence of a broad-based consumption tax. Similarly, the rise in the power of the working class in the late 19th and early 20th centuries led to the rise of the welfarist state in which high

marginal rates of taxation and a high level of social provision favoured their interests. In the liberal and welfarist states power not only operated overtly, but the second dimension of power also operated because the fiscal constitution effectively debarred serious discussion of a broad-based consumption tax and, in the welfarist state, serious criticism of the high rates of taxation required to finance the social provision.

Whereas the pressure which led to the emergence of liberalism and welfarism came from the rise of a new social class, the emergence of neoliberalism was a counter-revolution, which aimed to recreate an economic order restoring the entrepreneurial bourgeoisie, which had been crushed by communism, fascism and the interventionist policies of the democratic state (Crouch 2011). However, whereas the mercantile and working classes could use Lukes's (2005) first dimension of power and rely on demographics and weight of numbers to threaten violent revolution, neoliberalism involved the wresting of power from the majority by a minority. To do this it was necessary to obtain the consent of the majority and this could be achieved by using the second and third dimensions of power by constructing knowledge to harness the discontent.

CHAPTER 5: THE NEOLIBERAL STATE

5.1. Introduction

In chapter 4 I demonstrated that throughout history taxation has been a nexus between individuals and the state. It therefore forms part of the operation of power and tax policies are an expression and agent of these power relationships. However, the nature of this relationship can change over time and Britain changed from being a liberal state in the 19th century to being a welfarist state in the mid 20th century. However, by the 1970s the consensus in favour of the Welfare State was being challenged and the election of the Conservative government in 1979 led by Margaret Thatcher paved the way for the transformation of the UK into a neoliberal state. In this chapter I analyze how the neoliberal state differs from its predecessors, identifying the actors who benefit from it and explaining how power operates, firstly, to overturn the post-war Keynesian consensus in favour of welfarism, and, secondly, to hold the neoliberal state in place by making resistance problematic. This chapter therefore provides a conceptual framework for chapter 6, in which I analyze how these power relationships are reflected in and mediated through taxation.

This chapter has the following sections. In chapter 5.2. I set out the characteristics of the neoliberal state, arguing that it has used this nexus to divorce the economic and social domains and give priority to the former. The neoliberal state is therefore a state in which relations between individuals and

the state and between individuals have become based on techno-rational, economic principles.

The structures and institutions which allow the neoliberal state to retain and consolidate its position can only be put in place once neoliberalism has assumed power, but does not explain how it was able to overturn the post-war Keynesian consensus. In chapter 5.3. I therefore demonstrate that the emergence of neoliberalism was neither an accident nor the only possible response to the economic difficulties of the 1970s by analyzing how these actors used their financial and lobbying power to construct knowledge about the way in which society and the economy operates in a manner which benefitted them and how political parties espousing these principles have used the knowledge/power nexus to gain sufficient support for them to permit them to gain power. This is followed by a brief summary in chapter 5.4.

5.2. The Nature of the Neoliberal State

The neoliberal state is a state form which emerged from the perceived economic difficulties which beset the highly interventionist Welfare State in the 1970s and in which power is organized in a fundamentally different manner from its predecessors. As I demonstrated in chapter 4, in the liberal state, whilst political power largely remained with the aristocracy, the state had a limited role and delegated responsibility for domains such as the economy, education and the law to the bourgeoisie. The role of the state was therefore constrained and allowed individuals to organize their lives with the minimum of government

intervention. In the welfarist state the state's role was more interventionist, taking responsibility for areas such as education and healthcare.

In many ways the neoliberal state is, as its name suggests, a reversion to the liberal state, in which the state takes a more limited role. For example, formerly nationalized industries, such as the railway and steel, have been privatized, the banking and financial systems have been deregulated and the Bank of England has become independent, with political control having been removed (Harvey 2007). The formal power of the state has therefore been constrained by the creation of a 'shadow state' (Williams 2013), in which key areas of policy-making have been delegated to elites and 'experts' in undemocratic and unaccountable outside bodies (Hay 2004). Examples of these are international trade agreements brokered by the World Trade Organisation (WTO) and the delegation of the power to determine interest rates to the Bank of England.

Not only has the formal power of states been constrained, but they are also discouraged from using their formal powers by the spectre of international competition and globalization (Harvey 2007). Neoliberal structural reforms, such as the removal of exchange controls to permit free movement of capital in 1979 and the deregulation of the banking sector in 1986, have removed barriers to the international mobility of capital. Capital can therefore respond to any threat in a particular country by threatening to move to a country where it is treated more favourably and economic prosperity can therefore only be achieved by acquiescing with the interests of business and, in particular, large multinational corporations (Harvey 2007). For example, it has been reported that Starbucks

relocated its European headquarters from Amsterdam to London in 2014 at least in part due to a dispute over corporate tax avoidance with the Dutch tax authorities (Bowers 2014).

The neoliberal state places the state at the service of capital, but, in order to do so, it must harness the biopower, i.e. persuade individuals not only to behave in ways which benefit capital, but also to consent to this and 'buy into' the underlying ideology (Foucault 1978 [1976]). Up to the mid 1980s the Conservative government believed that these goals could be achieved by simply reducing the role of the state in order to allow markets and people's natural entrepreneurial spirit to flower. The priority of early neoliberalism was therefore to reduce the size of the state, so that 'the little platoons of civil society' could flourish, unhampered by state intervention (Giddens 1998:11-12). It was therefore considered unnecessary for the state to attempt to regulate individuals' conduct because individuals should act in the desired manner if the shackles of the state were removed. The reduction in the role of the state was therefore the motivation for the policies of the first two Conservative administrations between 1979 and 1987, such as the reduction in the levels of personal and corporate taxation and the privatization of nationalized industries such as British Telecom, British Gas and British Airways. Margaret Thatcher expressed her belief in the minimal state clearly in an interview with the *Sunday Times* in May 1981 (Butt 1981) in which she said that her objective was to 'change the soul' to make people less dependent on the state.

The attempt to ‘change the soul’ to allow capital to flourish simply by reducing the size of the state did not prove to be particularly effective (Brown 2005) and government spending as a proportion of gross domestic product did not fall in this period (Glennerster 2007). In the late 1980s and 1990s government policy therefore became more interventionist in order to actively create the ‘right’ conditions for capital. However, government did not intervene directly in the manner of the welfarist state, but did so indirectly. The role of government was therefore reinvented as that of being one actor in a partnership with the market and civil society in a mixed economy (Giddens 2000), a relationship which is often referred to as the ‘Third Way’.

Whilst the ideology of minimal government ignores the limitations of the market, such as the inadequate provision of public goods, a priority of the Third Way is to reconstruct public institutions and the confidence in their performance and to make government as effective and ‘quick on their feet’ as business (Giddens 2000:57-58). Advocates of the Third Way, such as Giddens, regard this arrangement as a partnership, whilst critics such as Brown (2005) regard it as a take-over of the state by the market, in which the state openly serves the needs of the market, not only in monetary and fiscal policy, but also in areas such as immigration and public education, which has to a great extent been restored to its ‘traditional’ function of producing passive workers with just sufficient skills to serve the needs of capital (Hill 2006).

Neoliberal rationality therefore links the state’s success to its ability to sustain and foster the market (Brown 2005) and integrates state decision making into

the dynamics of capital accumulation and networks of class power associated with this (Harvey 2007). Examples of this are the privatisation of public utilities and institutions, such as the railways, which allows rents to be extracted from activities which had previously been carried out on a social basis and private finance initiatives (PFIs), in which the private sector funds major construction projects, such as schools, hospitals and transport infrastructure, in a manner which permits the private sector to benefit from the gains. In return the private sector should bear the risks, but in practice the public sector often retains the risks and bears the losses (Froud 2003). Froud cites the example of the Skye bridge, where before the Scottish government purchased it in late 2004, the PFI company had been awarded a monopoly to prevent competition from ferry companies or a possible alternative bridge to ensure that they made the requisite return on their investment. The financial crisis of 2008 onwards demonstrated how far this has permeated society, since, when the financial system threatened to collapse, the whole apparatus of the state was forced to intervene to support private capital (Davies 2014).

Since individuals do not put themselves at the service of capital of their own accord, the state must coerce them into cooperating in creating the right conditions for capital to flourish. In order to put the state at the service of capital, power in the neoliberal state is therefore deployed in a very different manner to its predecessors. Liberal and welfarist states relied on Lukes's (2005) first dimension of power, which operated in a hierarchical and overt manner through the various state apparatuses, such as parliament and the judiciary.

However, in a neoliberal state, the fact that the state's formal role is more limited means that it cannot use overt means of coercion to the same extent, but must rely on more covert means to achieve its aims by utilizing Lukes's (2005) second and third dimensions of power. Indeed, whilst the more limited nature of the neoliberal state does not mean that it has relinquished power, the absence of hierarchical power forms, such as feudalism or the institutions like class or nation under liberalism, means that new ideological formations are required to permit power to operate and traditional conceptualizations of power are inadequate to explicate them (Dean 2010).

In the neoliberal state, the state has become simply one element in an assemblage and notions of the separate domains of society, economy and government have dissolved into assemblages of interconnected and interpenetrated actors and interests as the economic has been interpolated into the social and into formal government itself (Dean 2010). Power therefore operates in a capillary manner, resulting from the relationship between actors, such as the state, large corporations, international organizations and quangos, and can flow in many different directions (Foucault 1979 [1975]). For example, the state is bound by the terms of trade agreements, but the state has the formal power (and a degree of real power) to determine the terms of these, whilst the real power of the state is circumscribed by the influence of large corporations. This results in a network of indirect relations of regulation and persuasion, which do not recognize the boundaries between the state and the civil, the public and the private and the community and the market (Miller & Rose 2008).

The neoliberal state does not intervene directly in the lives of its citizens, but instead exercises power covertly by governing at a distance without recourse to direct forms of repression (Rose 1996; Lukes 2005). Whilst individuals are held personally responsible for their own actions and well-being (Harvey 2007), it seeks to make individuals subjects of responsibility, autonomy and choice and to shape and utilize their freedom through techniques such as audit, accounting and management. Conduct may therefore be regulated by internalizing and embodying daily practice and setting measurable targets, so that the state can monitor deviations from these. By aligning these generalized norms with the interests of the neoliberal state it therefore becomes possible to influence the actions of individuals without having to monitor their daily actions and violate their formally private status (Miller & Rose 2008).

The exercise of power through assemblages makes resistance more problematic, since it is only possible to attack one small part of the power framework at any one time, and the micro-regulation of behaviour through targets etc. might generate consent to the underlying neoliberal ideology. Where individuals allow their conduct to be regulated by these techniques and practices, this is an example of either Lukes's (2005) second or third dimension of power, depending on whether they 'buy into' the neoliberal ideology or comply simply because it is expedient to do so. However, the knowledge/power nexus has also been used to generate consent for the discursive reframing of the function of the state.

The neoliberal state is an economic state, in which economics has been reframed as a science, distinct and separate from the moral domain. 20th century historians of economic thought, such as Polanyi (1944 cited in Miller & Rose 2008) and Schumpeter (1954 cited in Miller & Rose 2008), had demonstrated that the economic domain was not one with its own natural laws, but one which had been brought into existence by intellectual and historical events as a particular way of thinking and acting and that it had evolved as these ways of thinking and acting had evolved (Miller & Rose 2008).

The welfarist state prioritized the elimination or mitigation of socially adverse consequences of economic policies and decisions. However, the neoliberal state has discursively codified and constructed truths around the problem of government and of the relationship between ‘political spheres’ and ‘non-political spheres’ (Rose & Miller 2010) and these are based on economic concepts such as the marginal theory of labour and Hayek’s theory of capital discussed in chapter 3.4. The techno-rational, economic paradigm regards ‘economic’ matters as constituting a separate domain from the ‘moral’ and in possession of objective 'scientific' qualities. Government cannot therefore govern the economy by determining policy; rather government policy is determined by the laws of economics (Rose 1999).

This has given governments the power to formulate economic policies which divorce the economic domain from the social and give priority to the former, without needing to be concerned with the implications of their policies on social justice and equity. The social and economic domains are seen as antagonistic

and the role of government is to regulate the conduct of individuals to maximize their entrepreneurial potential by desocializing economic policy (Rose 1999). Individuals therefore become economic actors and economic reward and punishment becomes a technique of Foucauldian discipline and control. Relationships between citizens and between citizens and the state are financialized and marketized, becoming largely governed by economic principles, thereby entrenching and strengthening the nature of markets (Miller & Rose 2008).

The neoliberal state aims to mould the entrepreneurial potential of individuals by active economic intervention to create the right conditions for entrepreneurship, such as the privatization of publicly owned enterprises and the minimization of rigidities in the labour market. The economy is therefore restructured to remove as many of the incentives to inactivity and dependency as possible and to make social support conditional on demonstrating the attitudes necessary to becoming an ‘entrepreneur of his or her self’ (Rose 1999:142).

This restructuring is justified on two grounds. First, in a global competitive economy, only countries with a flexible labour market can succeed, implying that governments must abrogate responsibility for the economy and, second, the provision of security by the government does not benefit individuals and only through economic activity and becoming entrepreneurs of themselves can individuals realize themselves (Rose 1999). The concept of citizenship has been transformed from a passive, dependent concept to an active and individualistic one, which is manifested through the exercise of choice.

Government policies are evaluated by the extent to which they further these objectives and the language of social obligations and solidarity has been replaced by the language of choice, individual responsibility and self-fulfilment across the political spectrum and amongst pressure groups and civil libertarians (Miller & Rose 2008).

The concept of citizenship being manifested through exercising choices means that social problems such as poverty and inequality do not need to be justified simply as the regrettable, but unavoidable and inexorable consequences of economics, but as the consequences of choices made by individuals (e.g. Becker 1964). Poverty therefore acquires a moral dimension and attempts by the state to alleviate it are not so much futile, since they contravene economic principles, but rather morally irresponsible, since they encourage individuals to make undesirable choices. Such measures can only be justified if they are explicitly linked to the promotion of employment and entrepreneurship. For example, benefits such as the Jobseekers' Allowance are explicitly linked to the individual receiving them improving their employability by acquiring skills (Rose 1999).

In this section I have argued that neoliberalism has put the state at the service of capital, which is held in place by exercising power in a capillary fashion through assemblages of multiple actors. However, this does not necessarily generate 'buy in' to the underlying ideology, nor does it explain how neoliberalism came to assume such a dominant position. In contrast, the knowledge/power nexus has the ability to harness the third dimension of power

(Lukes 2005) and hence the biopower (Foucault 1978 [1976]) by generating belief in the truths which have been constructed through neoclassical economics. However, ideologies do not emerge and immediately assume a hegemonic position and it is only possible to exercise power in a capillary fashion once it is possible to put the necessary reforms and structures in place. It does not emerge fully formed as an alternative social order at the appropriate time, but works on pre-existing social forces and alters the balance of their relations (Hall 1988). Power must therefore be exercised by sowing a seed in such a way that it takes root before the state of hegemony is reached. The following section therefore analyzes how neoliberalism was able to exploit the economic conditions of the 1970s in order for parties espousing it to gain power.

5.3. The Construction of the Economic State

The neoliberal state has not emerged as a result of 'erroneous game theory gone wild' or the 'senseless pursuit of a false utopia', but from a deliberate and successful attempt to destroy the post-war compromise between capital and labour and thereby reassert the dominance of capital and the (Duménil & Levy 2011). Whilst the neoliberal state has claimed to be about the supremacy of the market, it has actually enabled big corporations to reassert their dominance through non-market means (Crouch 2011). The major substantive achievement of neoliberalism has been the redistribution, rather than the creation of wealth (Harvey 2007), whilst Duménil and Lévy (2011) characterize neoliberalism as a social order aimed at the generation of income for the upper classes.

The UK government adopted neoliberal policies with the election of a Conservative government under the leadership of Margaret Thatcher in 1979, with the USA following suit in 1980 with the election of Ronald Reagan as President. However, neither of these countries, nor the Latin ones which had neoliberalism imposed on them under the 'Chicago boys' (a group of Latin American economists who had been trained at the University of Chicago under Milton Friedman) in the 1970s performed particularly well economically as a result. In Latin America the results of neoliberal policies were 'a whole "lost decade" of economic stagnation and political turmoil' (Harvey 2007:88). Whilst Jones (2000) argues that productivity increased and average wages increased by more than the rate of inflation, by mid 1980 the UK. had gone into a deep recession. Inflation had risen to 20%, the Public Sector Borrowing Requirement for 1979/80 stood at £10bn, as opposed to a target of £8.25bn, and unemployment, which had been about 1.3 million and falling when Thatcher took office, reached 2 million by November 1980 (Harvey 2007). Furthermore, key indicators have shown an increase in relative poverty and inequality and, for example, the number of people in the UK living in households whose income was less than half the national average rose from 5 million in 1979 to 13.9 million in 1991 (MacGregor 2005).

In contrast, countries such as Sweden, Japan and West Germany which only later adopted a different form of neoliberalism, performed better than countries, such as the UK, which had adopted it enthusiastically (Harvey 2007). The fact that Germany and Japan experienced economic difficulties during the 1990s can partly be attributed to the specific circumstances of the hasty reunification

of Germany in 1990 (Menz 2005) and to the fact that both countries lost their technological advantage as other countries caught up . However, by this time they could no longer resist the influence of neoliberalism elsewhere in the world, particularly in the USA (Cerny 2005). By the mid 1990s neoliberalism and monetarism had come to dominate institutions such as the International Monetary Fund (IMF) and the World Bank, culminating in the 'Washington consensus', which defined neoliberalism as the solution to world problems (Stiglitz 2002). The WTO, which was set up in 1995, set neoliberal standards and rules for the operation of the global economy and its primary function was to open up as much of the world as possible to unhindered capital flow to allow the USA, along with Europe and Japan, to 'exact tribute from the rest of the world' (Harvey 2007:93). This consensus did not go unchallenged and the late 1990s started to see opposition to neoliberalism start to emerge with, for example, the appointment of Joseph Stiglitz as chief economist of the World Bank in 1997. Even though he was ousted from this post two years later in 1999 he remains influential and was awarded the Nobel prize for economics in 2001 (Saad-Filho 2005).

Furthermore, unlike, for example, Keynesianism, neoliberalism is not a unified philosophy in the sense that it has been conceived of as a whole (Davies 2014). Rose (1999:27) describes the policies of the Conservative governments in the UK in the 1980s as:

> contingent lash-ups of thought and action, in which various problems of governing were resolved through drawing upon instruments and procedures that happened to be available

and out of these instruments a rationality evolved to link them and develop them into a coherent philosophy, which became known as neoliberalism. For example, as I have argued in chapter 5.2., Thatcherism initially espoused the philosophy of the minimal state, but when simply reducing the role of the state did not have the desired result of facilitating capital, this evolved into a more interventionist role for the state in order to achieve this aim.

The fact that neoliberalism is not a unified philosophy means that there is, at its heart, a contradiction where the rhetoric of freedom and choice masks the reality that a neoliberal state must coerce individuals into being complicit in the economic state and the exercise of power by corporations. There is a belief in minimal government and the disciplines of the free market taking the place of the guiding hand of the state, but the rights of private property, individual liberties and entrepreneurial freedoms must be defended by a strong and, if necessary, coercive state (Harvey 2007).

Similarly, whilst individuals should be free to choose, they should do so, to paraphrase Karl Marx, not in conditions of their own choosing and should not choose to form or join strong collective institutions, such as trade unions or political parties which oppose neoliberal policies and seek to reduce the role of the market and institutions which might effectively oppose neoliberal policies

must be attacked (Harvey 2007). Therefore, despite championing individual liberty, Thatcher was a great centraliser, who sought greater control over institutions such as local government, universities and the Church of England (Riddell 2003). Opposition to neoliberalism is also discouraged by the threat of globalization and international competition, i.e. economic prosperity can only be achieved by acquiescing with the interests of business and, in particular, large multinational corporations (Harvey 2007).

Whilst championing individual choice, neoliberalism is distrustful of democracy and removes as much activity as possible from the political realm (MacEwan 2005). It prefers to entrust key areas of policy-making to elites and ‘experts’ in undemocratic and unaccountable institutions, such as the IMF, WTO and the Bank of England (Harvey 2007). Elections therefore become an exercise in determining which party is most competent to administer these policies, rather than opportunities to debate and choose policies, and politicians are cast into the role of civil servants carrying out purely technical functions (Hay 2004).

The facts that the economic performance of neoliberal states in the 1970s and 1980s was not particularly strong and that neoliberalism contains fundamental contradictions suggest that it is an ideological construct, whose objectives are to transfer wealth to capital and restore class power (Duménil & Levy 2011). However, to do so it first had to overturn the hegemonic post-war paradigms of welfarism and Keynesianism and in the following section I discuss how this was achieved

The Overturning of Keynesianism

As I have set out in chapter 3, Lukes (2005), Foucault (1978 [1976]; 1979 [1975]; 1980; 1981 [1969]) and Gramsci (1971) provide a theoretical lens through which the operation of power may be analyzed. The construction of neoliberal ideology through the reworking of classical and neoclassical economics demonstrates how the third dimension of power was exercised through the construction of knowledge in order to persuade individuals and governments to put themselves at the service of capital (see chapter 5.2.).

The origins of neoliberalism are often traced to the founding of the Mont Pélérin Society (MPS) in 1947 by a small group of academics and historians led by Friedrich von Hayek, and which included Milton Friedman, in order to oppose the prevailing ideologies of state intervention and Keynesian economics (e.g. Harvey 2007), although it can be traced back even further to the opposition to President Roosevelt's New Deal by a number of influential American organizations, such as the National Association of Manufacturers (NAM) (Roehner 2007). Its founding statement made its ideological antipathy to the welfarist and interventionist spirit of the age clear, stating that the 'central values of civilization are in danger...from the development of current tendencies in policy' (cited in Harvey 2007:20). The central argument of *The Road to Serfdom* (Hayek 1944) was not that welfarism and economic planning were economically unsustainable, but the ideological one that, since those who have a significant degree of power are inevitably tempted to misuse it, and, since welfarism concentrates power in the hands of the state, welfarism will therefore inevitably lead to totalitarianism (Roehner 2007). However, instead of advocating a

balance of power between states, corporations and employees to ensure that none of them take precedence over the others, Hayek advocated allowing corporations to concentrate power in their hands, thus leading to the same danger of abuse that he had identified when states had arrogated considerable power to themselves (Roehner 2007).

The Road to Serfdom (Hayek 1944) provided a blueprint for the principle of neoliberalism and the promotion of the book, along with the establishment of a large number of think-tanks promoting free-market ideals (Roehner 2007), were good examples of the construction of knowledge through lobbying by these organizations. The MPS funded book reviews, translations and an abridged version widely circulated through the *Readers' Digest,* which went far beyond what might have been expected, given that Hayek was a relatively obscure academic at the time (Roehner 2007).

By the late 1970s the principles of the Welfare State were coming attack from a number of directions. The industrial conglomerates were starting to increase their influence, organizations such as the Institute for Economic Affairs and the Adam Smith Institute issued literature which was based on the philosophy of Milton Friedman. Hayek also attacked state services not only on economic ground, but also on moral and social grounds that are inherently paternalistic, stifle personal independence and self-reliance and give too much power to professionals such as social workers, doctors and teachers (Jones 2000).

Politicians need simple ideas to sell to voters (Smith 1987) and these are easier to sell if they have an intuitive appeal. It is much easier for a paradigm to become accepted if ideas can be vague and open to a variety of interpretations and political slogans can become rhetorical devices to mask specific strategies (Harvey 2007). For example, the notion of 'freedom' resonates very widely within the understanding of common sense and is therefore a very powerful notion which can be inserted into many political discourses, but which also may contain many contradictory ideas (Hall 1988). Neoliberalism emphasizes the idea of individual liberty, therefore in any society which views this to be paramount neoliberal values can appeal to a mass base and disguise the agenda of the restoration of class power (Harvey 2007).

The knowledge/power nexus may therefore exercise the third dimension of power by reinventing ideas with an intuitive appeal to give them a technocratic meaning. Economists and politicians can therefore mean one thing when they refer to these, whilst voters think they actually mean something else. For example, the economic meaning of efficiency is very different from its everyday meaning (Makdissi 2006) and the principle of competition espoused by *The Road to Serfdom* and the MPS was different from its neoliberal versions (Roehner 2007).

Hayek idealistically regarded the impersonal and anonymous nature of markets, which had the function of coordinating social activity without the need for intervention by political authorities, as a bulwark against egalitarian and idealistic concepts of the common good, which he believed would lead to

tyranny (Davies 2014) and the MPS initially advocated *Ordoliberalismus,* in which open, decentralised markets, supported by a strong rule of law were considered to be the best guarantors of a free, competitive society. The MPS was aware of the limitations of the market in public goods, such as transport infrastructure and of its possible corrosive social effects and in such a system, no individual firm could exert power over others (Davies 2014).

However, in the 1970s the Chicago School of economists redefined competition in a manner which benefitted large corporations and influenced lawyers to interpret anti-trust law in accordance with this interpretation (Davies 2014). Instead of being a *process,* it was redefined in a narrow, technocratic manner as an *outcome*, which would lead to the destruction of small and medium-sized businesses and the dominance of large corporations. The principle of consumer choice evolved into the economic concept of maximizing 'consumer welfare', which meant engineering an economic situation in which consumers are most likely to have a choice and this situation will occur where wealth in the economy is maximized. If a large corporation buying out its smaller rivals leads to an efficiency gain, this will lead to increased consumer welfare, even if there is a reduced consumer choice (Crouch 2011).

The knowledge/power nexus has led to the economic domain becoming understood through these models with their abstractions and assumptions, despite their flaws and despite the fact that they privilege certain interests, partly because it is possible to use assumptions for so long that we lose sight of the fact that they are merely that – assumptions (Frankfurter & McGoun 2002).

Once these assumptions have become internalized the models of techno-rational economics therefore exercise a Gramscian (1971) hegemony and become the lens through which the economic domain is viewed without any awareness of its limitations, either by those against whom this power is exercised or, even, by those exercising it.

Whilst this may partly explain its success, there are also other factors. For ideas to take root they must be, at least superficially, plausible and actors such as the MPS constructed a narrative which provided both an explanation for the economic problems of the 1970s and an alternative. At such times people are often attracted to such alternatives without being fully aware of their full implications. For example, Margaret Thatcher's election as leader of the Conservative party was viewed less as a sign that the party agreed with, or even understood, her philosophy, but rather that she was the only person willing to challenge Edward Heath at a time when Conservative MPs wanted a change and her opponent, William Whitelaw, was rejected as being too closely identified with past failures (Seldon & Collings 2000). Similarly, the Conservative victory in 1979 was due to a discredited Government losing the election rather than the electorate endorsing Thatcher's philosophy (Seldon & Collings 2000). Neoliberalism could therefore harness a spirit of discontent and offered an intuitively attractive solution to problems, whilst remaining vague on the specifics (Smith 1987) and, as I have demonstrated earlier in this section, neoliberalism was not even a fully-formed ideology at this time.

A group may be more receptive to an idea if it makes them feel superior to other groups, provides a scapegoat for their problems or promises an easy way to improve their situation. For example, Daunton (2002b) observes that the enfranchisement of women in 1918 gave the Conservatives the opportunity to enlist their support by portraying housewives as bastions of common sense because they had experience of running a household. Conservative values were therefore connected with common sense, in contrast to men, who were portrayed as hot-headed, militant trade unionists and socialists. Similarly, the minimal government doctrine of early neoliberalism argued that the state was inherently wasteful and inefficient (Harvey 2007), implying that people were innately resourceful and able to solve the nation's problems if they were not held back by the government.

Neoliberalism could also tap into the upwardly-mobile aspirations of many of the traditional working class in the 1970s. Working class identity and loyalty, of which trade unionism had been an important part, had been very strong and self-contained since the end of the 19th century, but this was starting to change and weaken with trade unionism moving into white-collar occupations and weakening in affluent industrial areas. It was therefore becoming more difficult for Labour to rely purely on working-class support in order to form a government (Daunton 2002b) and the Conservatives sought to capitalize on their aspirations. Policies of redistribution were therefore less likely to appeal to more affluent workers, who were abandoning their old cultural loyalties and middle class progressives were realising that poverty was less an issue of wages and

more a problem of the unorganized, immigrants, children, single parents and the elderly (Daunton 2002b).

5.4. Summary

In this chapter I have demonstrated that the UK in the late 20th and early 21st centuries strongly characterizes a neoliberal state, in which power is exercised overtly to a much lesser extent than in its predecessors. In its place, power operates covertly through assemblages of multiple actors, of which the government is simply one and includes, for example, quangos and corporations. In the neoliberal state relations between individuals and the state have become financialized and marketized and have become governed by the principles of neoclassical economics.

However, in chapter 3 I demonstrated that neoclassical economics is a set of constructs and in this chapter I demonstrate that neoliberalism is an ideology which privileges the interests of capital and seeks to place other sections of society at its service. It has exploited the nexus between knowledge and power in order to assume its current hegemonic position and, since the tax system is a primary means for the state to propagate the prevailing 'truths' concerning the relationship between citizens and the state, it might be expected that over the last 35 years the tax system has been reformed to serve the interests of capital. In chapter 6 I therefore demonstrate that this has, in fact, occurred and that the principles of neoclassical economics have often been used as a rationalizing discourse for this.

CHAPTER 6: TAXATION IN THE NEOLIBERAL STATE

6.1. Introduction

In chapter 5 I argued that the UK can be characterized as a neoliberal state which has been reconfigured to serve the needs of capital and in which the economic has precedence over the social domain, with relations between citizens and the state being largely organized according to the principles of neoclassical economics (Boden et al. 2010). Taxation is an important nexus between citizens and the state, and the taxation systems of neoliberal states are likely to reflect these underlying principles and relationships. Consequently, I argue that, in a neoliberal state, taxation has tended to be viewed less as a common fund into which citizens pay according to their ability and more as a tool for furthering neoliberal economic policy by protecting and furthering the interests of capital and promoting the incentive to work and undertake entrepreneurial activity. In this chapter I explicate how much of UK taxation policy from 1979 onwards has been informed by neoclassical economic principles.

This chapter has the following sections. In chapter 6.2 I examine how neoliberal economic principles inform tax policy in neoliberal states. In chapter 6.3. I demonstrate that UK income tax policy has been motivated by neoclassical theory relating to incentivization, which results in the transfer of resources to wealthier taxpayers. In chapter 6.4 I demonstrate that UK policy relating to the taxation of business profits (principally corporation tax) was initially similarly motivated by theories of incentivization, but has more recently

been motivated by the need to incentivize inward investment through a 'competitive' tax regime. In chapter 6.5. I use the controversy surrounding the abolition of the 10p tax rate in 2008 as a critical incident which exposes the normally hidden operation of power, since it forced ministers and officials to publicly defend the measure, which demonstrated that much of UK tax policy is based on techno-rational considerations. However, the ensuing controversy, which led to concessions being made by the government, also demonstrated that, however hegemonic a particular paradigm might appear to be, the possibility of resistance cannot be entirely extinguished and the theme of resistance is developed further in chapter 9. This is followed by a summary in chapter 6.6.

6.2. Taxation in the Neoliberal State

In chapter 4 I demonstrated that in both the liberal and welfarist UK the tax system reflected the prevailing relationship between individuals and the state. The liberal state separated the political and economic domains and remained circumscribed. Taxation therefore represented payments to the state to enable it to function and the limited nature of the state meant that the level of taxation could be kept low (Daunton 2001). In contrast, the welfarist state conceptualized taxation as a common fund into which individuals paid according to their ability and received benefits and welfare according to their needs (Daunton 2002b). The taxation system was one of the principal tools of social welfare, with high marginal rates of taxation reducing inequality and financing social provision.

In chapter 5 I demonstrated that the neoliberal state is an economic state in which neoclassical economics is deployed as a rationalizing discourse for reconfiguring the state to further the interests of capital and restore class power (Harvey 2007) and coercing other sections of society to be complicit in this. Whilst neoliberalism might claim to be about the supremacy of the market, it actually aims to reassert the dominance of big corporations (Crouch 2011). In chapter 3 I set out the evolution of neoclassical economics from the late 18th century onwards to demonstrate that the economic theory which underpins this derives from Ricardo's rent theory and marginal analysis. The former set up an antagonism between the interests of capital and labour, so that the interests of capital must be favoured at the expense of labour, and the latter formulated principles which determine how individuals can be encouraged to work and become entrepreneurs of themselves and thereby serve the needs of capital (Rose 1999).

In a neoliberal state, tax policy has become a tool of achieving these objectives and a means of Foucauldian control through reward and discipline (Foucault 1979 [1975]). This reconfiguration is designed to further and protect the interests of capital (Brown 2005) and is rationalized by neoclassical economic theory, which opines that, since the economic domain is governed by immutable, quasi-scientific laws and is therefore completely separate from the social domain, economic decision-making cannot therefore take considerations of social equity into account (Miller & Rose 2008). In the neoliberal state, government becomes a largely technocratic exercise (Hay 2004) and the fact that taxation embodies subjective, value-based choices is therefore obscured.

Not only is the transfer of the tax burden to poorer taxpayers inevitable, but also desirable, because whether an individual is more or less wealthy is therefore seen as a result of their choices in education, work and even marriage (e.g. Becker 1964). Citizenship has therefore become an individualistic concept which is manifested through the exercise of choice (Miller & Rose 2008) and, by favouring richer over poorer taxpayers, the tax system rewards individuals for desirable choices or penalizes them for undesirable ones.

This reconfiguration of the state has been achieved, firstly, by reducing taxes on capital and, secondly, by reducing the tax burden on high earners and increasing that on poorer taxpayers. The economic assumption underpinning the reduction of taxes on capital is that entrepreneurial activity will thereby be facilitated. The assumption underpinning the shift in individual tax burdens is that in order to maximize the incentive to work, high earners need to be rewarded whereas poorer taxpayers must be penalized (Murphy & Nagel 2002). It is therefore assumed that poorer taxpayers are likely to prioritize the *income* effect of an increase in taxation, which reduces their after-tax income, and work additional hours to make up the shortfall, whilst wealthier taxpayers are likely to prioritize the *substitution* effect, which reduces the after-tax return from additional hours worked, and therefore work less (Stiglitz 1999). However, these assumptions are contestable and I discuss them in chapter 6.3.

The connection between taxation and incentives was not a new concept in neoliberal states, since politicians began to concern themselves with the extent to which taxation might affect incentives from the 1940s onwards (Daunton

2002b). However, it was not a dominant consideration at this time and high levels of taxation in order to fund the Welfare State continued largely unchallenged. For example, in the years immediately following the end of World War II there was concern about the effect on incentives of various government policies, such as the taxation of goods, high rates of personal taxation, and the imposition of higher rates of company taxation on distributed profits in order to discourage consumption. However, the priority of the Attlee Labour government between 1945 and 1951 was to use taxation to stimulate production and damp down pent up demand, which might otherwise crowd out exports and suck in imports (Daunton 2002b).

Since the principles of the Welfare State were sacrosanct, the Conservatives were concerned in the 1950s and 1960s to find ways in which the pursuit of self-interest could be contained within an integrated, cohesive society, which could respond to economic problems and generate agreement between different interest groups (Daunton 2002b). Hayek's conclusion concerning 'natural' price levels and rates of interest provided Conservatives with the insight (or rationalizing discourse, depending on point of view) that their attempts in the 1950s and 1960s to reconcile the two were fruitless, leaving the way clear to develop a fiscal policy which emphasized economic principles at the expense of social justice (Daunton 2002b). In this section I have outlined the principles underlying the taxation system in a neoliberal state and in the following two sections I set out how the UK taxation system has been remodelled since 1979 in accordance with neoliberal objectives.

6.3. Getting People to Work – the Taxation of Labour

One of the key indicators of the shift from a liberal to a welfarist state was the long-term increase in the rates of income tax (see table 4.1. in chapter 4.4). In this era corporation tax and capital gains tax did not exist, and national insurance and consumption taxes were relatively insignificant, therefore changes in the rate of income tax illustrate shifts in the tax burden more clearly than they would today. By the late 20th century the picture had become much more complex and the role of taxation in the shift from a welfarist to a neoliberal state encompasses changes to a variety of taxes. One way of capturing these is to detail changes in the proportion of tax revenue raised from various types of taxes and this is set out in table 6.1. These figures need to be used with a degree of caution, since tax receipts from different sources are likely to be affected to varying degrees by changes in the economic cycle, with corporation tax receipts being the most volatile. For example, the 2008 figure reflected receipts from profits earned in 2007, the last year of the economic boom, and the figure fell to 8.1% in 2009.

Table 6.1. Tax Receipts Analysed by Source for Selected Years 1979-2013

	1979	1985	1988	1998	2008	2013
Individuals	32.0.%	25.4%	25.0%	27.6%	29.0%	27.2%
Corporations	7.7%	12.5%	10.9%	11.0%	10.0%	7.7%
National Insurance						
Employee contributions	6.7%	8.4%	7.8%	7.2%	7.4%	7.4%
Employer contributions	N/A	N/A	9.3%	9.2%	11.1%	11.0%
Consumption						
VAT	12.5%[1]	15.9%	16.7%	18.3%	17.8%	21.0%
Excise duties	12.7%	11.2%	10.4%	11.1%	8.1%	8.3%

(OECD 2015)

1. The increase in the rate of VAT took effect in June 1979, therefore the 1979 figure partially reflects the old rate of 8% and partially the new rate of 15%. The figures for 1978 and 1980 were 9.4% and 14.7% respectively.
2. This table only includes major categories and the figures do not therefore sum to 100%.

However, a couple of trends can be discerned. The first is a sharp rise in the reliance on consumption taxes and in particular VAT. This is consistent with increases in the rate, which rose from 8% in 1978/79, with a higher rate on luxury goods of 12.5%, to 20% in 2011, the higher rate on luxury goods having been abolished in 1979. The second is a fall in the proportion of revenue raised by income tax, although this is partially offset by a rise in the proportion contributed by national insurance. Since consumption taxes tend to be regressive, increased reliance on them will tend to make the tax system as a whole more regressive, but the effect of the changes to income tax and national

insurance are more complex and these are set out in more detail in tables 6.2. and 6.3.

Table 6.2. summarizes changes to income tax between 1978/79 and 2014/15. 1978/79 was the last tax year for which tax rates and thresholds were set by James Callaghan's Labour government, 1979/80 was the first tax year for which tax rates and thresholds were set by the incoming Conservative government under Margaret Thatcher and 1988/89 was the tax year in which Nigel Lawson's tax reductions in the Finance Act 1988 (Finance Act 1988) took effect. The years between 1988 and 2014, which included the Labour governments of 1997 to 2010, saw a gradual reduction in the basic rate from 25% to 20% and the periodic introduction and abolition of a small starting rate band (see chapter 6.5. for the details on the abolition of the 10% starting rate band in 2008).

Table 6.2. Summary of Income Tax Rates and Thresholds 1978-2014

	1978/79	**1979/80**	**1988/89**	**2014/15**
Basic rate	33%	30%	25%	20%
Number of higher rates	8	5	1	2
Top marginal rate	83%	60%	40%	45%
Threshold of top marginal rate	£24,000	£25,000	£19,300	£150,000
Apr 2015 equivalent (approx)[1]	£127,000	£118,000	£47,000	£150,000

(Institute of Fiscal Studies 2015)

[1] Based on RPI figures from Office for National Statistics (2015a)

Whilst income tax rates have been reduced for all taxpayers, the changes clearly demonstrate the policy objective of favouring high earners. It should be noted that the 45% tax rate on income over £150,000 is relatively new, having been introduced in 2010/11 at a rate of 50% and reduced to 45% in 2013/14. Not only has income tax become less progressive in the last 30 years, but national insurance, which is a regressive tax, has assumed greater importance. Table 6.3. summarizes the changes between 1978/79 and 2014/15 in class 1 national insurance contributions payable by employees[2] where the occupational pension scheme is not contracted out of the state second pension.

Table 6.3. Summary of Class 1 Employee National Insurance Rates and Thresholds 1978-2014

	1978/79	**1979/80**	**1988/89**	**2014/15**
Rate between lower and upper thresholds (not contracted out)	6.5%	6.5%	9%	12%
Rate above upper threshold	0%	0%	0%	2%
Upper threshold	£6,250	£7,000	£15,860	£41,865
Apr 2015 equivalent (approx)[3]	£32,500	£33,000	£38,500	£41,865

(Institute of Fiscal Studies 2015)

This table therefore shows that, in the same period, as the top rate on earned income fell from 83% to 40%, the rate of national insurance contributions rose from 6.5% to 12%.

[2] Employers also pay national insurance contributions, which are therefore a form of payroll tax.
[3] Based on RPI figures from Office for National Statistics (2015a)

The increased importance of consumption taxes and national insurance transfer the tax burden from wealthier to poorer taxpayers, although the overall package of changes particularly relating to poorer taxpayers has been more complicated and I discuss these later. An analysis of the rhetoric when these changes were introduced shows that the neoliberal principle of incentivization was used as a rationalizing discourse, since the intention to reduce marginal income tax rates and shift the burden of taxation to taxes on spending and the motivation for doing so were made clear in the Conservative Party 1979 general election manifesto.

> We shall cut income at all levels to reward hard work, responsibility and success...It is particularly important to cut the absurdly high marginal rates of tax both at the bottom and top of the income scale. It must pay a man or woman significantly more to be in, rather than out of, work.
> (Conservative Party Net 2015 para. 3)

This approach became evident shortly after the election in an emergency budget of 12 June 1979. Monetary policy was tightened; a target for sterling M3[4] of 7-11% was set for the remainder of the 1979/80 fiscal year (which compared with Labour's target of 8-12% in 1978/79) and the minimum lending rate was raised from 12% to 14%. Public sector spending cuts of £1.5bn were

[4] A measure of money which comprises notes and coins in circulation plus private sector current and deposit accounts and private sector holdings of sterling bank certificates of deposit (Smith 1987).

announced, in addition to £1bn which was to be raised from the sale of state assets. The basic rate of income tax was reduced from 33% to 30%, the top rate was reduced from 83% (98% where the investment income surcharge of 15% applied) to 60% and the investment income surcharge was abolished (Hansard 1979).

The reason for doing this was quite explicitly to increase incentives. Before announcing any of the changes the Chancellor of the Exchequer, Geoffrey (now Lord) Howe referred to ‘a structure of taxation that might have been designed to discourage innovation and punish success’ and promised that the changes would be only the first step, but would take the UK a long way in the right direction (Hansard 1979:col. 240-241). He later described the 83% top income tax rate as ‘an absurdity’, claiming that it brought in very little revenue since it killed incentives and was ‘patently unjust’ (col. 258), a statement which extends the notion of social justice to the wealthiest members of society, rather than simply to its poorer members.

Cutting top income rates for high earners might have been easy to justify politically, particularly in 1979 when, as stated in chapter 4, public opinion was turning against high rates of taxation (and the Conservative government was still in its honeymoon period). However, increasing the tax burden on poorer taxpayers has always been harder to justify. The measure in the 1979 Budget which increased the tax burden on poorer taxpayers was the raising of VAT to a unified rate of 15% (Smith 1987), but Chancellor Howe was careful to do this only in conjunction with raising the state retirement pension by nearly 20% and

raising personal allowances and certain other social security benefits (Hansard 1979:cols. 252-253; 259). He described the shift from the taxation of earnings to the taxation of consumption as the only way to restore incentives and make it worthwhile to work (col. 250) and denied that VAT was regressive, justifying this statement by saying that poorer families tended to spend a greater proportion of their income on zero-rated goods[5] (col. 250).

Nearly ten years later, Chancellor Nigel (now Lord) Lawson reduced the top rate of income tax to 40% in his 1988 budget. Before announcing any specific income tax changes he made it clear that he believed that it was necessary to keep income tax low in order to boost incentives (Hansard 1988:col. 1006) and when he came to announce the reduction in the top rate he once again stressed that high rates of tax destroy incentives, encourage avoidance and drive talent overseas, with the result that they eventually raise less revenue rather than more (col. 1012), an argument which draws on the concept of the Laffer curve (The Heritage Foundation 2015).

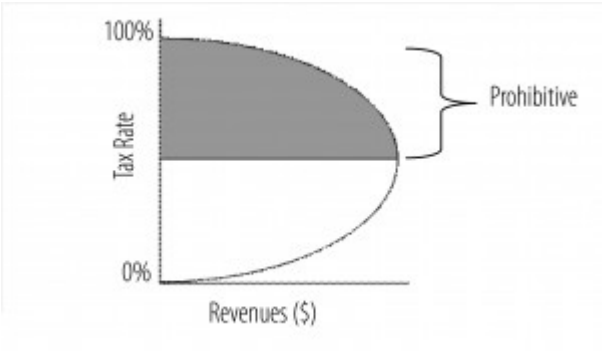
The Laffer curve, named after the American economist Arthur Laffer[6], posits that an increase in tax rates will not necessarily lead to an increase in tax revenue and that, conversely, a reduction in tax rates will not necessarily lead to

[5] Goods and services which are within the scope of VAT, but on which VAT is levied at a rate of 0% and which are therefore in practice excluded from VAT as far as the final consumer is concerned.

[6] Laffer reportedly sketched the curve on a napkin at a meeting in 1974 to illustrate why he opposed tax increases proposed by the US President Gerald Ford and he popularized it during the 1980s. He did not claim to have invented the concept and attributed it to the 14th century Muslim scholar Ibn Khaldun and also to John Maynard Keynes (The Heritage Foundation 2015).

a fall in tax revenue. It suggests that an increase in the tax rate might reduce the incentive to work and thus reduce income or profits generated and that any increase in tax revenue due to the increase in the tax rate might be outweighed by a fall due to a reduction in the level of income and an increase in tax avoidance or evasion. Conversely, a reduction in the tax rate might lead to an increase in tax revenue if the increase in income or profits generated due to the increased incentive to work and a decrease in the incentive to avoid or evade tax outweighs the fall in revenue due to the reduction in the tax rate. The Laffer curve is normally represented by taking two points at which tax revenue is assumed to be nil. The first, self-evidently, is where the tax rate is 0% and the second being where the tax rate is 100%, since it is assumed that there will be no incentive for anyone to work and generate income and profits. These two points are connected by a parabola, the highest point of which being the tax rate at which there is the optimum trade-off between the tax rate and the incentive to work (The Heritage Foundation 2015). However, the Laffer curve has been the subject of considerable criticism, which I discuss in the following subsection (p. 161)

Figure 6.1. Laffer curve



(The Heritage Foundation 2015)

Nearly 25 years after Lawson's Budget, in his 2012 Budget speech (Hansard 2012), George Osborne stated that the 50p tax rate introduced in 2010/11 had had an adverse effect on work incentives in order to justify reducing the highest rate of tax to 45p from 2013/14, supporting this argument by quoting statistics from HMRC that the 50p tax rate had raised much less revenue than had been hoped or predicted.

Chancellor Howe's 1979 Budget, giving to the poor with one hand and taking away with the other, demonstrates both the political difficulty of increasing the tax burden on the poor and the fact that assessing changes in the tax burden on poorer taxpayers is more complex and encompasses changes both to the taxation and benefits system. Certain aspects of the taxation system since 1979 have benefitted poorer taxpayers. For example, the personal allowance[7] in 1979/80 was £1,165 (Institute for Fiscal Studies 2015) (equivalent to roughly £5,500[8] in 2015), whilst this had risen to £10,000 in 2014/15, and this increase has been accompanied by a reduction in the higher rate threshold (Institute of Fiscal Studies 2015), which ensures that no tax saving accrues to higher rate taxpayers. However, this benefit must be offset against other aspects, such as rises in the rates of VAT and national insurance, and in order to analyze the overall effect of combinations of changes an alternative approach is required.

This approach involves comparing the tax burden on various sections of society. Although such comparisons can be illuminating, they have limitations,

[7] The amount of income a taxpayer is allowed to earn in a tax year before starting to pay tax.
[8] Based on RPI of 54.3 in April 1979 and 258.0 in April 2015 (Office for National Statistics 2015a).

since the results can vary depending on definitions and how the results are presented. Reliable data on tax burdens is only available from 1988 onwards, but most of the changes to income tax, national insurance and VAT rates took place between 1979 and 1988[9]. Data from the Office of National Statistics for 2013/14 show that before adjusting for direct and indirect taxes and cash and non-cash benefits, the income ratio between the top and bottom deciles of the population was 27.4, but that the post-tax ratio was reduced to 13.1 and the ratio after adjusting for benefits was 6.1 (Office for National Statistics 2015b). The fact that the ratio of post-tax incomes is half that of the pre-tax incomes might suggest that the tax system is progressive, but other statistics (Byrne and Ruane 2008) give a different impression. Table 6.4. sets out the total tax paid as a proportion of gross income (i.e. original income plus cash benefits, but excluding benefits in kind, such as healthcare) by each decile of the population for 2006/07.

This data demonstrates that households in the first decile paid a much higher proportion of their income in tax, with the other deciles bunched in a narrow range and the rate paid by the tenth decile towards the bottom end. The overall effect of the changes to the tax system has therefore made it regressive, rather than progressive and therefore plays a role in the transfer of resources from the poorest sections of society to the wealthier. The data for 2006/07 is not

[9] In early 2007 the Labour MP Alan Milburn asked the Chancellor of the Exchequer to provide information on the average tax burden on each decile of the population for each year since 1979 and the written answer from the Office of National Statistics gave this data from 1988 onwards and stated that it was not possible to go back further because this was the earliest year for which data was available on a reasonably consistent basis (Hansard 2007a). However, the Gini coefficient measuring income inequality had risen from about 0.26 in 1979 to about 0.34 in 2012/13 (Equality Trust 2015), although it is not possible to ascertain how much of this increase is attributable to changes in tax burdens and how much to changes in inequality in pre-tax incomes.

untypical, since similar data in Hansard (2007a) for the years from 1988 to 2004/05 shows that the fall in rates between the first and second deciles in this period is never less than 10% and in 2001/02 was as high as 18.6%. Byrne and Ruane (2008) attribute this to the fact that these households pay around a third of their income in indirect consumption taxes and a further 7.5% in council tax, since many of these households do not qualify for council tax benefit[10] for various reasons.

Table 6.4. Overall Tax Burden by Decile of Population – 2006/07

Decile	%age
1st (bottom)	46.1
2nd	33.7
3rd	32.9
4th	33.0
5th	34.6
6th	35.1
7th	36.6
8th	36.7
9th	36.0
10th (top)	34.2

(Byrne & Ruane 2008:2)

[10] Assistance with paying council tax, a property-based local tax, paid through the social security system.

The fact that a large proportion of the tax burden comprises consumption taxes means that it is more hidden. Power & Stacey (2014) have found that the tax burden on the lowest decile of the population is widely under-estimated. They surveyed 1,036 adults aged 16-75 in April 2014, asking them to estimate the tax burden on the top and bottom deciles and the average tax burden. Respondents were also asked to state the tax burdens which they considered to be equitable. A comparison of the perceived and preferred tax burdens with the actual burdens (calculated from Office for National Statistics Effects of Tax and Benefits on Household Income 2013 data) is presented in table 6.5:

Table 6.5. Comparison of Actual, Perceived and Preferred tax Burdens

	Actual Burden	**Perceived Burden**	**Preferred burden**
Bottom decile	42.92%	23.9%	14.8%
Average	35.39%	29.8%	22.4%
Top decile	35.43%	35.9%	38.6%

(Power & Stacey 2014:11-14)

This data suggests two things. Firstly, taxpayers would prefer a more progressive taxation system than they believe actually exists, which is the operation of Lukes's (2005) second dimension of power, since they feel that their preferences have been 'organized out' by the hegemonic group. Secondly, taxpayers are unaware of just how far the UK taxation system diverges from their preferred model and they might not resignedly accept the taxation system if they were fully aware of the true burdens. This is the operation of Lukes'

(2005) third dimension of power, since the consent has been generated by misleading taxpayers about the tax system.

This lack of awareness can stifle dissent, but when politicians need to defend treating the poorest taxpayers more harshly, they often either refer to incentives or allude to Mill's distinction between the deserving and undeserving poor (Mill 1909 [1848]). An example of the former was when Chancellor Howe raised VAT from 8% to 15% in 1979 whilst cutting direct taxes. He justified the shift from the taxation of earnings to the taxation of consumption as the only way to restore incentives and make it worthwhile to work. The distinction between the deserving and undeserving poor can be seen by contrasting remarks made much more recently in 2013 by Jacob Rees-Mogg MP in the debate on the housing benefit under-occupancy penalty (often referred to as the 'bedroom tax') and George Osborne in the Budget.

Rees-Mogg said:

> I think that people need to be able to take responsibility for themselves and to make choices for themselves...It is not for the state, putting its expenditure on the backs of hard-pressed taxpayers, to fund indefinitely people's lifestyle choices, and it is a choice if people decide to have an extra room that they are not actually using, they can choose whether to move to a smaller

> property or, under this new policy, find a way of getting the extra income they need.
>
> (Hansard 2013a: col. 387-388)

The rhetoric that those on benefits are poor because of their lifestyle choices and therefore do not deserve government sympathy contrasts with that relating to those in work and George Osborne opened his 2013 Budget speech by saying ‘Mr Deputy Speaker, this is a Budget for those who aspire to work hard and get on’ (Hansard 2013b) and he reiterated this sentiment when he announced an increase in the tax-free personal allowance by over £1,300. He stressed that it would now take over 2 million of the lowest paid out of tax, although given that the bottom quintile had an average original income of £5,436 in 2011/12 (Office for National Statistics 2013) most of them would already be paying no income tax and the increase would therefore do nothing to alleviate the high tax burden on the bottom decile.

In this section I have set out the major changes to personal income tax, national insurance and VAT since 1979 to demonstrate that they have made the taxation system as a whole more regressive and have therefore redistributed resources from poorer to wealthier taxpayers. I have also demonstrated that the rationalizing discourse for these changes has been the need to incentivize individuals to work and in the following section I discuss whether the assumptions upon which this discourse is based are well-founded.

Taxation and Incentives – Evidence of Effects

In the previous section I argued that since 1979 tax policy in the UK, or at least the rationalizing discourse for this, has largely been concerned with increasing work incentives. However, the empirical evidence suggests that the link is much more complex and subtle, varying according to gender and earning capacity, and rests on a number of assumptions.

Evidence concerning the effect, or lack of effect, of the tax changes on incentives started to emerge from the mid 1980s onwards when Brown (1986 cited in Hutton 1995) concluded that the effects of the tax changes on incentives in the early years of the Thatcher government were very small. A comparative study by Atkinson and Mogensen (1993) of the UK, Germany, Denmark and Sweden concluded that with the exception of low-paid women, many of whose pay is likely to be a second household salary, high marginal tax rates did not appear to be a deterrent to work effort and that the increase in tax revenue arising from the reduction of tax rates was due to the very significant increase in the incomes of top earners for reasons unrelated to the reduction in tax rates. Dilnot and Kell (1988) found that the tax cuts of 1985/86 gave rise to a 1% increase in labour supply of the higher paid, but were unable to conclude whether that was attributable to an increased willingness to work or to an increase in the demand for executives in that period. These findings were repeated in a survey by Bryson & McKay (1994), which also found that lower taxes increased the willingness of the very low paid to work, especially women.

These findings were largely replicated by Meghir and Philips in their contribution to the Mirrlees report (Meghir & Philips 2010). They found that, for women and less educated men, tax and benefit incentives can affect the decision whether to work or not and the number of hours worked, whilst for educated and wealthy men, the effect is negligible, although it may affect *how* they work. For example, individuals may choose to be self-employed rather than employed or may choose to operate through the medium of a company and taxation might also affect the amount of effort put in or creativity during the hours of work (Meghir & Philips 2010).

The above evidence suggests that the link is an ideological construct. Claims that reducing tax rates will increase incentives often rely on the Laffer curve (The Heritage Foundation 2015) set out in the previous section, but Hutton (1995) has argued that the Laffer curve owes more to ideology than to robust economic theory and it has been criticized (e.g. by Mirowski 1982) for making unrealistic assumptions. Individuals frequently have no choice over the hours that they work and even the self-employed will not be able to increase the amount that they work if they cannot obtain additional work. Furthermore, it assumes that the only motivation to work is financial and this is criticized by Rynes et al. (2004) and Hendry (2012).

It also only predicts that reducing tax rates will increase incentives if tax rates are located in the prohibitive range of the curve (see figure 6.1.) and this is always either explicitly or implicitly assumed (Mirowski 1982), although little research has been carried out on what the ‘optimum’ tax rate might be.

However, Brewer et al. (2010) suggest that the optimum marginal effective tax rate (METR) excluding consumption taxes and assuming a constant elasticity of 0.25, shows a U-shape, which is precisely the opposite of the Laffer curve. They calculate that the optimum METR at low incomes is 70%, falling to 36% at incomes of around £30,000, rising to 64% at incomes of £200,000. If a constant elasticity of 0.5 is assumed the optimum METRs become 50%, 20% and 45% respectively. Even if such economic models are treated with a degree of caution and the optimum METRs at the lower end of the income range are not politically achievable, this suggests, particularly if taken with the findings of Meghir and Phillips (2010), that the income elasticity for men is negligible and that the top tax rates in the UK have been located on the left hand side of the Laffer curve since 1979.

Meghir and Phillips (2010) also observe that individuals who value leisure less are likely to work more hours and to have invested more in human capital accumulation. They will therefore command a higher wage rate and, under a progressive tax system, pay tax at a higher marginal rate, which makes the argument on the link between wages and incentives a circular one. This may give rise to a spurious negative correlation between wages and hours worked, giving the impression that incentives matter more than is, in fact, the case.

Whilst the findings of Brewer et al. (2010) support the theory that less wealthy and educated men can be incentivized to work through increasing taxation, there is no evidence to support the theory that higher earners can be incentivized by reducing taxation. The first part should not be a surprise, given

that income is generally used to purchase necessities and reduced after-tax income due to an increase in tax therefore needs to be recouped through working extra hours or taking a second job. The, arguably counter-intuitive, conclusion of the second part can be explained by the fact that the link assumes that remuneration is the only or overriding factor in motivation and studies by, for example, Rynes et al. (2004) and Hendry (2012) have concluded that, whilst pay is an important extrinsic motivator, it is not necessarily true that increasing wages will increase motivation. The additional income may have very little utility to the taxpayer in itself, but may be a proxy through which other attributes, such as achievement and status, may be measured and many salaried employees may strive for a pay increase or promotion for these reasons, rather than the extra money itself.

If income is a proxy for achievement and status, Rynes et al. (2004) conclude that relative pay levels are more important than absolute pay levels, and employees are very sensitive to changes which affect their standing relative to close coworkers or workers in other companies. Wage scales are also likely to be flatter than economic theory would predict, since employees may accept a lower salary than their true worth in order to be at or near the top of the informal hierarchy at their employer and employees at the bottom of an employer's hierarchy may be paid more than their true worth to compensate for their lowly status and this is particularly likely to be the case where the workforce must work as a team (Frank 1993). Rynes et al. (2004) also concluded that pay is a much greater motivator if it is strongly linked to performance. It is clear that increasing after-tax pay through a reduction in marginal tax rates neither

differentiates between individuals, and therefore does not affect the signal effect of pay differentials, nor is linked to performance, which suggests that it is, at best, of limited use in achieving this objective. This, in turn, suggests that the rhetoric relating to incentives might be a rationalizing discourse for favouring wealthier taxpayers over poorer taxpayers.

In sum I have demonstrated that since 1979 the tax system has been reconfigured to become more regressive by placing greater reliance on consumption taxes and national insurance contributions and reforming income tax to favour higher earners. The result of these changes is that the overall tax burden on the bottom decile of the population is significantly higher than on the remaining deciles, whose tax burdens are all bunched in a narrow range.

The justification for these changes is grounded in economic notions that link pay and incentives, and in particular the notion that reducing marginal tax rates for high earners will increase the incentive to work. The aim of the changes to the tax system has therefore been to incentivize taxpayers to put themselves at the service of capital. Whilst this will principally be in the form of their labour, the shift in the burden of taxation from taxes on capital to taxes on labour and consumption also means that taxpayers are being required to finance an increasing proportion of the infrastructure used by capital. For example, tax revenue will be used to finance the construction of roads or pay subsidies to train operating companies, and both the roads and the trains will be used by corporations to transport goods and thus earn profits. Furthermore the introduction of, for example, student tuition fees, requires many individuals to

pay to acquire the skills that they will use for the benefit of capital (Boden & Nedeva 2010).

However, the incentive effect is not supported by evidence and it is possible to explain why this relationship does not operate as predicted. Economic theory has therefore provided a rationalizing discourse for a transfer of resources from poorer to wealthier taxpayers through the reduction in marginal rates of income tax and the increase in the rates of consumption taxes and other taxes of a regressive nature. However, increased reliance on consumption taxes and changes to the taxation of labour have not been the only means by which resources have been transferred to capital through the tax system. Changes to corporation tax have also achieved this more directly and these changes are discussed in the following section.

6.4. Lightening the Load – the Taxation of Capital

The principal profits tax in the UK is corporation tax and in this section I set out how changes to corporation tax since 1979 have substantially reduced the burden of taxation on companies. The result of this reduction is controversial because some economists argue that companies do not actually bear the economic cost of taxation through reduced returns to their shareholders (or, at least, not the whole cost), but may transfer it to their employees and/or customers (Kay & King 1990). Kleinbard (2014;224) criticizes much of this research for failing to distinguish between corporations earning ‘normal’ profits and those which control patents, software or brand names to earn supernormal profits, but observes that ‘[u]nseemly scuffles break out when the question is

posed at academic conferences'. He attributes this controversy in part to the fact that since corporations are legal rather than natural beings the burden of taxation must be borne by some group of individuals, the question being which groups. He reports the assumptions of the nonpartisan Congressional Budget Office and the US Treasury Department that the economic incidence of corporation tax falls mainly on shareholders (the Congressional Budget Office assumes that 75% is borne by shareholders and 25% by labour and the Treasury Department assumes an 82%/18% split). He also reports that the Joint Committee on Taxation was for a long time agnostic on the issue, but now assumes a 95%/5% split. Furthermore, whatever the theoretical economic incidence might be, Sheppard (2011 cited in Tax Justice Network 2015:28) argues that companies *behave* as if they bear the economic cost when he says that 'if labor bore 80 percent of the burden of the corporate income tax, corporations wouldn't care about it at all'.

There is also empirical evidence that shareholders behave as if they bear the economic cost. In April 2011 US Uncut and the Yes Men (US-based stunt-masters) issued a hoax press release purporting to be from General Electric stating that they would be making a $3.2bn tax 'refund' as contrition for past abuses. This hoax release was not connected with any profits' announcement and was widely circulated before being exposed and General Electric's shares briefly fell by around $3.5bn, i.e. roughly the amount of the 'refund' (Tax Justice Network 2015:28).

Like any tax, the effective rate of corporation tax, i.e. tax payable as a percentage of pre-tax profits, depends on two factors – the rate of tax and the breadth of the tax base, i.e. the profits which are taxed. It is therefore possible to reduce the burden of corporation tax by either reducing the tax rate or by narrowing the tax base through various exemptions and reliefs and the burden of corporation tax has been reduced by a combination of these two methods.

When the Conservative government came to power in 1979 the main rate of corporation tax was 52% (although stock relief and generous rates of capital allowances meant that the tax base was relatively small). By the financial year 2015 this had fallen to 20%. There has also for many years been a small companies' rate (recently renamed the small profits' rate in 2010) where companies with profits below £1.5m have paid a reduced rate of corporation tax. This rate has fallen in the same period from 40% to 20%, which means that a single rate of corporation tax now applies to companies of all sizes (Institute of Fiscal Studies 2015). Whilst corporation tax rates have been reduced for all companies, the reductions have been greater for large companies, supporting Crouch's (2011) argument that neoliberalism is concerned not with the supremacy of the market but with the supremacy of large corporations.

Whilst the Conservative administration from 1979 to 1983 made substantial changes to personal taxation, corporation tax remained relatively unchanged: the small profits' rate was reduced from 40% to 38% in April 1982 and the main corporation tax rate was reduced from 52% to 50% in April 1983 (Institute of Fiscal Studies 2015). It was only in their second term of office from 1983 to

1987 that the Conservatives started to make significant changes to corporate taxation. In his 1984 Budget, Chancellor Lawson announced that by April 1986 the main rate of corporation tax would be reduced to 35% and that the small companies' rate would be reduced to 30%, a change which was back-dated to April 1983 (Hansard 1984 col. 297) and by April 1986 this rate had been reduced to 29% (Institute for Fiscal Studies 2015).

However, to counterbalance the reduction in tax rates, Chancellor Lawson broadened the tax base by abolishing stock relief and first year allowances on capital expenditure, whereby companies could write off all or most of their capital expenditure in the year it was incurred. First year allowances were 100% up to and including 1983/84, but were progressively reduced to 75% in 1984/85 and 50% in 1985/86, and by 1986/87 the only allowance available was the writing down allowance of 25% (Institute of Fiscal Studies 2015). Whilst tax revenue from the broadening of the tax base partially offset the tax lost from the reductions in the tax rates, Lawson cited calculations that the measures would cost the exchequer £280m in 1984/85 and £450m in 1985/86 (made up of a loss of £1,100m from the reduction in the rate with £650m recouped through the reduction in the first year allowance (Hansard 1984 col. 297). Like Chancellor Howe's changes to personal income tax in 1979, Lawson's rationale for these changes was explicitly to increase incentives to innovate and create jobs. The reduction in first year allowances aimed to prevent more commercially productive investments being rejected due to the favourable tax treatment of a less productive alternative (col. 297), but he stated that lower rates would result in higher after-tax profits, which would encourage and reward enterprise,

stimulate innovation and create more jobs through allowing more of the profits to be reinvested (col. 298).

After 1986/87, the Conservative government made no major changes to the corporation tax regime and by 1996/97 the main rate was 33% and the small companies' rate was 24%. However, in 1997 the incoming Labour government reduced the main rate to 31% (Hansard 1997 col. 306) and the small companies' rate to 21% (Institute of Fiscal Studies 2015) (although Gordon Brown did not mention this change in his Budget speech). The stated motivation for this change was once again to increase incentives, but Brown also stated that he wanted the UK to be the obvious first choice for new investment (Hansard 1997 col. 306).

This statement reflected the increasingly globalized nature of the economy and the objectives of the tax system, or at least the rhetoric surrounding it, them therefore shifted from the need to encourage UK taxpayers to be entrepreneurial to the need for the UK tax regime to be internationally competitive and encourage inward investment through taxing profits more lightly than its competitors. This was even more explicit in Gordon Brown's 2007 Budget, in which he reduced the main rate of corporation tax to 28% with effect from April 2008. He stated that this rate was lower than all our major competitors and would make the UK corporation tax rate the lowest of all the major economies (Hansard 2007b col. 820). Since 2007, the main rate of corporation tax has been progressively further reduced to 20%, with the

consequence that, between 1997 and 2015, it has fallen by 11%, whereas the small profits' rate has only fallen by 1% (Institute of Fiscal Studies 2015).

Whereas the reductions in tax rates in the 1980s were partially offset by a broadening of the tax base, from 2009 onwards the reductions in tax rates have been accompanied by a narrowing of the tax base. In 2009 the Labour government changed the way in which companies obtain relief for foreign tax suffered on dividends from overseas companies (Finance Act 2009 Sch.14). Prior to 2009, the UK operated a credit relief system for overseas corporation tax suffered, but in 2009 this was changed to an exemption system for foreign dividends, with the treatment of foreign branch profits following suit in 2011. This means that companies no longer need to pay UK corporation tax on dividends received from territories in which the rate of company tax is lower than that of the UK, whereas under the credit system, if tax rates in the source country were lower than in the UK, some UK corporation tax was still payable (Miller & Oats 2014).

This change was justified on a number of grounds. Firstly, it was argued that it would bring the UK into line with most other European countries and would make the UK tax system in this area more compliant with EU law, secondly, it would make the taxation of foreign dividends more economically neutral (Gammie et al. 2008:246, 248) and thirdly, it would make the taxation of these dividends simpler (Miller & Oats 2014). However, I argue that these justifications are all, at best, debatable and they are therefore a rationalizing discourse for a transfer of resources to capital. This is therefore the operation of

the third dimension of power through the power to mislead (Lukes (2005) and construct knowledge (Foucault 1981 [1969]).

The legal justification for the change arose from the objection by lawyers that the credit system treated dividends received from overseas companies resident in other EU member states less favourably than dividends received from companies resident in the UK, which have always been exempt from corporation tax. This was the subject of the test case *Test Claimants in the FII Group Litigation v IRC (2007)*. By the time that the case was heard, changes to the taxation system meant that no UK tax liability was likely to arise on dividends received from companies in which the holding company had a stake of at least 10%, and could therefore claim relief for underlying tax[11]. The court held that a tax system which could *in theory* discriminate against dividends from companies in other EU countries, but *in practice* did not do so, was not a breach of the UK's obligations as an EU member. The UK was only in breach of its EU obligation in relation to dividends received from companies in which the holding company had a stake of less than 10%, where no relief from underlying tax was available and a UK corporation tax liability would normally arise (Miller & Oats 2014:108-109). The UK tax system could therefore have been made compliant simply by extending relief for underlying tax to dividends where the holding company held a stake of less than 10%.

In 1984 the UK introduced Controlled Foreign Companies (CFC) legislation, which, subject to a number of exemptions, gave the UK the power to tax income

[11] Corporate income tax paid by the company paying the dividend, since dividends are paid out of after-tax profits.

of CFCs resident outside the UK which was not repatriated through the payment of dividends. This was an anti-avoidance measure to counteract profits being artificially retained by, or diverted into, companies resident overseas in countries in which they pay little or no tax, resulting in a loss of UK tax. However, this legislation was criticized by lawyers for contravening the fundamental principle of the EU that residents of the member states should have the right to establish their businesses in any member state without hindrance (Miller & Oats 2014). The potential effect of this challenge to the legality of the CFC regime was exacerbated by the move to an exemption system for foreign dividends, since profits would escape UK tax regardless of whether they were remitted to the UK or retained overseas (Miller & Oats 2014).

The legality of the CFC legislation has also been criticized by lawyers for contravening the rules of international taxation by taxing income and gains which have neither arisen in the UK nor have arisen to a person resident in the UK. However, the commentary to the OECD Model Tax Convention recognizes that CFC rules are a legitimate instrument to enable states to protect their tax base (Miller & Oats 2014). More specifically, in the UK, it was ruled in *Bricom Holdings Ltd v Commissioners of Inland Revenue (1997), Cadbury Schweppes Plc and another v IRC (2006)* and *Vodafone 2 v Commissioners of HMRC (2009)* that the UK CFC legislation was compatible with international law and can be invoked to counteract arrangements which are wholly artificial, but not where they have at least some commercial substance (Miller & Oats 2014).

The legal justification exploits the fundamental EU principles of freedom of establishment and freedom of movement of capital, which were enshrined in the Treaty of Rome, which originally established the Common Market in 1957. This was originally intended to create economic co-operation between its members (originally only France, Germany, Italy and the Benelux countries) and, in particular, to unify the coal and steel industries through the removal of customs duties. It also aimed to lessen the possibility of war between its members, since World War II was still a recent memory (Miller & Oats 2014).

The justification also exploits the fact that, although the EU has been successful in removing trading barriers between members (now expanded to 28 states with highly disparate economies), it has proved politically impossible to achieve the degree of harmonization of tax systems necessary to severely restrict the scope for tax avoidance. For example, whilst the EU considers that it is not possible for EU companies to fully take advantage of the single market without the Common Consolidated Corporate Tax Base, (a proposal to harmonize the rules for calculating taxable profits throughout the EU and require companies to file only one tax return and make only one payment of tax) (KPMG 2011), a survey by Deutsche Bank published in 2007 showed only muted support for the proposal, which might eventually frustrate any attempt at implementation (Miller & Oats 2014:590-591). The principles were therefore formulated in a very different age, which did not foresee the way in which they might be used in future to facilitate tax avoidance, and have only been partly realized. Construing them as immutable has created a very favourable environment for large

corporations and is the operation of the third dimension of power through the construction of knowledge.

Not only is the extent to which an exemption system is more compliant with EU law than a credit relief system debatable, but the claim that an exemption system makes taxation in this area more economically neutral greatly over-simplifies the issue (Gammie et al 2008:252-253). Economic theory distinguishes between three types of neutrality.

1. Capital import neutrality (CIN), where investments into the domestic jurisdiction from abroad are treated the same, regardless of the country of origin;
2. Capital export neutrality (CEN), where investments outside the domestic jurisdiction are treated the same for tax purposes, regardless of the destination; and
3. Capital ownership neutrality (CON), where inward or outward investments are treated the same for tax purposes regardless of who owns them.

   (Gammie et al 2008:248-249)

Gammie et al. (2008) argues that a single territory cannot achieve all three types of neutrality unilaterally, and faced with a choice between CIN and CEN, it has usually been argued that the latter should take precedence over the former. This is because if investors face the same effective tax rate on foreign and domestic investments the cross-country equalization of after-tax rates returns enforced by capital mobility also ensures that pre-tax rates of return are

equalized. CEN therefore tends to equalize the marginal productivities of capital across countries, which therefore tends to maximize world income. The change from a credit relief system to an exemption system therefore infringes against the preferred type of neutrality, which contradicts the stated argument that the change is necessary in order to make the tax system more economically neutral.

The change from a credit to an exemption system was also promoted as a simplifying measure, but Miller & Oats (2014) dispute whether this is necessarily the case. Noting that the UK exemption regime is actually very generous, they caution that, whilst the underlying concept is simple, it contains complex rules to prevent UK companies obtaining the exemption relief where it is not intended, such as where the dividend is, in fact, disguised interest. The complexity of the legislation might therefore thwart the central aim of improving competitiveness.

Finally, although the exemption regime applies to all companies (albeit with some additional conditions for small companies as anti-avoidance measures), the draft legislation applied only to large and medium-sized companies, with small companies (defined as companies with fewer than 50 employees and a turnover not exceeding €10m) (Gammie et al 2008) being subject to a modified version of the credit relief system. The inclusion of small companies in the final version of the legislation (Corporation Tax Act 2009 s.931B, inserted by Finance Act 2009 Sch. 14 para. 1) therefore appears to be an afterthought, lending credence to the view that neoliberalism is about the supremacy of large corporations rather than the market (Harvey 2007).

The third dimension of power through the construction of knowledge may also operate by fostering a belief that companies or individuals will leave the UK if their demands are not acceded to, but the evidence that will actually do so is mixed. Kaffash & Hinks (2011) reported that only 22 companies left the UK for tax reasons between 2007/08 and 2010/11, but Ahmed & Quinn (2011) reported a senior partner at Ernst & Young as saying that the firm had received enquiries from around 40 companies who were considering relocating to the UK due to increased tax competitiveness. One company which moved its headquarters from London to Dublin in 2008 as a result of the tightening of UK tax rules for offshore subsidiaries was WPP and they returned to London in 2011 when this policy was reversed (Bowers 2015). However, companies which either move their head offices into or out of the UK for tax purposes do not necessarily move their underlying economic activity and it was reported that Starbucks' decision to relocate its European headquarters from Amsterdam to London would create only a few (albeit well-paid) jobs in the City of London (Bowers 2014) and the partner quoted by Ahmed & Quinn (2011) only stated that the relocations would create roughly 2,000 executive jobs, implying that the companies were not intending to relocate their underlying economic activity. This suggests that in location decisions for economic activity 'talent trumps tax incentives' (Egan 2011) and that rhetoric concerning creating an attractive climate for business and investment is a rationalizing discourse for creating an attractive climate for diverting profits through the group structure and for highly-paid executives.

In this section I have demonstrated through examples that the burden of taxation on companies has been reduced both through the reduction in tax

rates, especially for larger companies, and also, more latterly, through the narrowing of the tax base. The justification for the reductions in the tax rates in the 1980s, partially counterbalanced by the broadening of the tax base, was the restoration of incentives. This is a similar justification to the one used for the changes to the taxation of labour and has been discussed in the previous section. However, in the 1990s, the increased globalization of the economy meant that the justification shifted to the need for the UK tax system to be internationally competitive. This has also been the justification for the narrowing of the tax base, but these changes have also been justified on the grounds of compatibility with EU law, economic neutrality and tax simplification. However, I have demonstrated that all these justifications are, at least, questionable and that they may well be simply a rationalizing discourse for transferring resources to capital and therefore the exercise of power through the construction of knowledge.

In the previous two sections I have argued that taxation policy since 1979 has been based on neoliberal economic theory, which is based on flawed assumptions and that power has been exercised by wealthy taxpayers and large corporations to construct knowledge in a way which benefits them. The fact that power operates through the third dimension means that it is usually very difficult to observe, but there are always critical incidents where the normally hidden operation of power becomes visible (Lukes 2005). In the following section I therefore use the controversy which arose in 2008 over the abolition of the 10p rate of tax as a critical incident which exposed the techno-rational, economic paradigm underpinning tax policy. The controversy also

forced concessions from the government also demonstrated that it can never be absolute and the potential for resistance always remains (Lukes 2005). This is developed further in chapter 9.

6.5. The 10p Tax Controversy – the Unmasking of Power

Announcement of Reforms

Table 6.1. summarizes changes to the basic rate since 1979, but there has periodically also been a small ‘starting’ or ‘lower’ rate band below this and in 2007/08 the first £2,230 of taxable income was taxed at 10% (the 10p tax rate), with the basic rate of 22% payable on the next £32,370 of taxable income (Institute of Fiscal Studies 2015). However, on 21 March 2007 the Chancellor of the Exchequer Gordon Brown, announced the abolition the 10p tax rate as part of the 2007 Budget (Hansard 2007b) with effect from the 2008/09 tax year. The decision was announced in the middle of the speech; Brown simply stated that the aim was to reduce the number of tax bands from three to two. Thus the simplification aspect of the change was emphasized - a point subsequently reiterated in the accompanying press notice (Treasury 2007). However, to counterbalance this change he also reduced the basic rate to 20%, also with effect from 2008/09, meaning that the first £36,000 of taxable income was taxed at 20% (although this threshold was later reduced to £34,800). The reduction in the basic rate was announced, in contrast, with a flourish as the finale of the speech along with the assertion that this measure would ‘reward work...ensure that working families are better off and...make the tax system fairer’ (Hansard 2007b).

The Institute for Fiscal Studies (IFS) (cited in House of Commons 2008) identified that the effect of the interaction of the two changes was that someone with very low earnings of just £7,755 p.a. would lose the most - £232 annually. Taxpayers earning less than £19,500 would also lose under these proposals and the biggest winners were taxpayers earning over £41,500, who gained around £450. The changes therefore shifted the tax burden from the poorest to wealthier taxpayers.

Much immediate commentary about these reforms was favourable and appears to have been grounded in a utilitarian, techno-rational paradigm of tax policy. Chote (2007), director of the influential think tank the IFS praised Chancellor Brown for not fighting shy of introducing a tax-neutral reform for fear of creating losers and for designing the reform so as to 'limit the number of losers to one household in five at a modest overall cost to the Exchequer'. The implication was that if a government is afraid of creating losers there will simply be a paralysis. He also commented favourably on the simplification dimension of the reform. Plager (2007:53), the deputy editor of *Taxation*, a leading practitioner magazine, was slightly more equivocal. Whilst she recognized the effect of the abolition on lower-income taxpayers, she also noted that 'abolishing the 10% band is largely to be welcomed, since it introduced complexity for relatively little benefit'. However, even at this early stage, Grice (2007) noted that there was discontent amongst Labour MPs, who were concerned at the effect of the reforms on poorer people.

Chote and Plager apparently viewed the reforms from a techno-rational, economic perspective and there is evidence to suggest that the reforms were motivated by such conceptualizations. In the wake of the subsequent controversy, a House of Commons Treasury Committee (House of Commons 2008:51) concluded that it was clear that ministers were aware that roughly 5.3m families would lose out, a figure first put forward by Chote (2007). Although a greater number of families would gain, there would still be a small, but significant, number of people who would be worse off, even after taking other changes to the tax credit and benefit system into account. The report by the House of Commons (2008) concluded that ministers 'were not awake to the full impact [of the changes] or were in denial about it' and that ministers appear to have believed that the 5.3m families who would lose would accept this loss. Whilst the House of Commons committee had the inestimable advantage of hindsight, the phrases 'not awake' and 'in denial' indicate that it thought that this view was misguided.

Because the changes did not take effect until 2008/09, more than a year after they were announced, they attracted little immediate comment beyond that by Chote (2007) and Plager (2007). During the debate on the Finance Bill 2007, Frank Field (MP for Birkenhead, a senior Labour MP and a former Minister of Welfare Reform) expressed concern about the effect of these changes on poorer people (Hansard 2007c), but the Chief Secretary to the Treasury, Stephen Timms, dismissed his concerns, somewhat unsatisfactorily, by stating that they would not take effect until 2008/09. With the exception of a brief follow-

up question from a Liberal Democrat MP, Julia Goldsworthy, which was similarly brushed aside, there was no further debate on the matter.

Opposition to Reforms Builds

Whilst in 2007 Field may have been a lone voice in Parliament in support of a tax policy based on principles of social justice and the ability to pay, controversy arose a year later in April 2008 when the effect of the changes became apparent to the affected taxpayers/voters through a reduction in their after-tax pay. Much of this controversy involved in-fighting amongst Labour MPs, with the leadership and loyal activists such as Powell (2008) supporting them and many backbenchers such as Field (2008) opposing the changes, believing that the Labour Party had gone too far in courting the 'yuppie vote' and that the time was right to reassert their belief in more traditional Labour values of social justice and support for the poorest sections of society.

Powell (2008), the activist (and now an MP), recognized the anger felt by many voters, but still toed the government's line.

> There's no doubt that the removal of the 10p tax rate has been an issue on the doorstep in Manchester over the last few weeks. For us as Labour politicians and Labour activists, it is an unwelcome situation to be confronted by a low-paid worker who is now taking home less pay as a result of a measure brought in by a Labour government.

She cited two anonymous examples where poorer taxpayers had recently discovered that they were worse off due to the changes. She also defended the changes by citing IFS statistics which showed that since 1997 the net income of the poorest five deciles of the population, taking into account direct and indirect taxes, had risen by between 1.5% (5th decile) and 12.4% (1st decile), whilst the net income of the richest five deciles had decreased by between 0.1% (6th decile) and 5.45% (10th decile) in order to demonstrate Labour's past record. She also mentioned various other reforms, such as targeted tax credits (in-work means-tested benefits) and increased age allowances for pensioners, which helped many of the poorest in society.

In contrast, taking up the theme of the perceived inequity of the changes, Field (2008), espousing more traditional, egalitarian Labour values, wrote a piece in *The Spectator* opposing the reform. Grover (2010) has argued that this may also have been motivated, at least in part, by a personal dislike of Gordon Brown. Field wrote that the rebellion then brewing amongst back-bench Labour MPs against the government was the result of the fact that, despite the many reforms instituted in the Labour Party and its courting of the 'yuppie vote', Labour activists had still believed that the party had remained committed to the poor. For many backbench Labour MPs, Field argued, the abolition of the 10p tax rate represented the final abandonment of the poor by New Labour. It was not therefore just those who would lose out who opposed its abolition, but also those who, whilst standing to gain financially, who felt that the inequity of the changes was objectionable. Field (2008) wrote that

> [t]he horror felt by Labour MPs is compounded when they, like so many other groups, have been made better off overall by the Budget changes, knowing that their poorest constituents are largely footing the bill

He also argued that MPs were ‘letting their decent instincts be known’ because the issue struck at the very heart of being a centre-left MP. He asked the rhetorical question ‘[w]hat is the point of us being Labour MPs if we cannot protect the poorest?’.

Field’s argument that many Labour MPs, had refrained from opposing previous measures, even if they conflicted with their own socialist principles, recalls McCaffery’s (1996) argument that utilitarianism, i.e. attaining the greatest good for the greatest number of people, abandons tax policy to the politics of self-interest and becomes a rationalizing discourse for favouring powerful groups in society. In this case, the power was largely political rather than financial, but the ‘yuppie vote’ had been courted by Labour because it was the largest and most powerful faction in key marginal seats (closely fought seats which assume very great significance in the UK electoral system under which simply the candidate winning the most votes in a constituency is elected) which Labour needed to win in order to be re-elected.

The division between the government which advocated the techno-rational view of taxation and opposition parties and Labour backbenchers who supported a policy based on more traditional Labour values came to a head during the

second reading of the Finance Bill 2008 on 21 April 2008 (this being the first time that the bill was actually debated). The Chief Secretary to the Treasury, Yvette Cooper (Hansard 2008:col. 1066) repeated the argument that four out of five households would be better off or see no change and that only one household in five would pay more as a result of changes to the personal tax package. Cooper also repeated the argument that Labour had demonstrated its egalitarian credentials in previous years by introducing reforms which had benefitted the poor.

> As the independent Institute for Fiscal Studies has set out, the poorest third of the population will benefit most from this package because of what we have done for pensioners, for families with children and for low paid workers through allowances and tax credits. Indeed, the impact of the two [2007 and 2008] Budgets and the [2007] pre-Budget report is to raise more than 500,000 children out of poverty...As a result of these measures, households with children in the poorest fifth of the population will be on average £340 a year better off, and that will make a very big difference to them.
> (Hansard 2008:col. 1065-6)

Opposition to the reforms was expressed in speeches from members of both the Labour and Conservative parties, who expressed concern at the effect of the changes on particular sections of society. For example, Linda Gilroy (Labour) claimed that some of her constituents in Plymouth lived in the poorest

ward in England and that it is ‘some of the youngest people in the constituency, who already feel undervalued, who are losing out?’ (Hansard 2008:col. 1067).

Gilroy supported the egalitarian argument that the changes disadvantaged the poorer members of society. Her argument also indicates that the controversy had gained a symbolic significance beyond the simple financial effects of the changes, representing, in Field’s (2008) words, the ‘final abandonment of the poor’, who already felt undervalued. Other Labour MPs also echoed Field by expressing their concern for the poor and the belief that it was the purpose of a Labour government to fight for their interests. Michael Meacher said:

> What I am saying is that the incomes of the poorest tenth – the lowest decile – in society have improved significantly, which is very different from what happened after 18 years of Conservative government. I am one of those who would like them to improve considerably more……
> (Hansard 2008:col. 1134)

It was not only Labour MPs who expressed concern. John Redwood (Conservative) said:

> Is it not even odder that the people who are going to pay this extra burden through the abolition of the 10p band are exactly those who are hit most severely by the surge in food

> and energy prices and by the further big hike in fuel duty
> when they want to travel by car?
> (Hansard 2008:col. 1075-6)

Philip Hammond (Conservative) summarized the Government's attitude to the effect of the changes on the less well off as:

> By implication the Prime Minister is trying to say to people,
> "Look, don't worry about the fact that you will be £200 or
> £250 worse off this year as a result of the Finance Bill. Just
> remember that you had some good times in years gone by,
> so you shouldn't worry too much if we take this money away
> from you now."
> (Hansard 2008:col. 1078-9)

He then summarized the flaws in this reasoning, saying 'I have to tell the Hon. Lady [Yvette Cooper] and the Prime Minister that this is not how people, especially those on low incomes, think or plan their lives' (Hansard 2008:col. 1079). Although Hammond does not spell it out explicitly, he argued that a family on a low income will generally immediately budget and commit any extra money and that this will cause hardship if the money is later withdrawn.

Despite the considerable concerns raised over the reform, the second reading of the Finance Bill was passed by 298 votes to 223 (Hansard 1988; col. 1154). However, whilst there was to be no U-turn, the government was forced to make

concessions in response to the opposition to the measure. On 13 May 2008 the Chancellor of the Exchequer (who was now Alistair Darling, since Gordon Brown had in the meantime succeeded Tony Blair as Prime Minister) announced that the personal allowance would be raised from £5,435 to £6,035 in addition to the increase already announced in the Budget in order to help taxpayers on lower incomes. This increase exempted a further £600 of income from tax, which meant that taxpayers earning £7,755 were only £112 worse off, rather than £232, and the breakeven point was reduced to roughly £13,000. The higher rate threshold was decreased by £1,200 from £36,000 to £34,800 to ensure that no benefit accrued to taxpayers on higher incomes (Treasury 2008). It was in this form that the Finance Bill passed through the remaining stages of the parliamentary process and became law.

The controversy was a critical incident which allows the operation of power to be glimpsed, since it forced the government and Treasury officials to publicly justify their position. Possibly more accurately, it allows a glimpse of the failure of power through the construction of knowledge to operate, since the techno-rational arguments in favour of abolition failed to convince, and this raises the question why ministers and Treasury officials were apparently caught unawares by the controversy. The exercise of power through the construction of knowledge is the operation of Lukes's (2005) third dimension of power in which other groups are asked to 'buy into' the ideology of the hegemonic group, but it would be a mistake to necessarily assume that this was a calculated attempt to deceive these other groups. A hegemonic group may advance an ideology which furthers their interests because they have so completely enfolded

themselves in it that they have genuinely come to believe that it is in the general interest and therefore, in their eyes, incontestable and ceases to be an ideology.

The clue to this lack of awareness can be found in the report of the House of Commons Treasury Select Committee (House of Commons 2008) in the aftermath of the imbroglio. This concluded that ministers knew that 5.3m families would lose out, but were ‘not awake’ to the full implications of the change, or were ‘in denial’ (House of Commons 2008:77) about it. This suggests that ministers and Treasury officials could conceive neither of any other way of framing tax policy nor of any possibility that others might find such paradigms objectionable enough to put up resistance. Structuring the tax system according to techno-rational principles and ignoring the resulting inequity ceased therefore to be moral choices and became a necessity. Ministers and officials might personally regard the resultant inequity as regrettable, but they would not be able to conceive of any alternative.

Reasons for this may be that working with neoclassical economics involves working with abstractions and assumptions and it is possible to use these for so long that they lost sight of the fact that they are merely that – assumptions (Frankfurter & McGoun 2002). Furthermore the elegant mathematical models of economics are antithetical to the messy guesses of politics and economists see themselves as the guardians of ‘rationality’ and ‘efficiency’. They remain loyal to economic theory, partly due to their training, partly due to a desire to remain above factional interests and partly because they generally have, or have had,

alternative careers in business or academia. They do not therefore simply live for politics and do not fear falling out of favour with ministers (Markoff & Montecinos 1993).

The emergence of latent opposition may also take a hegemonic group by surprise because they have been acting in a similar manner for some time without encountering resistance, and latent resistance emerges when protestors feel that it is safe. This tax change was the continuation of a process which had begun in the late 1970s and for the first 20 years of this period the Conservatives were in power. The most dramatic changes occurred in the first ten years or so of this period, during which time the Conservative government had either comfortable or overwhelming parliamentary majorities, rendering any opposition problematic. Since 1997 the Labour party had been in power and regressive tax policies are contrary to traditional Labour values. However, many Labour MPs had been prepared to remain silent about Labour's embrace of the economic paradigm of taxation as the price of electoral success and ministers might have mistaken this grudging acceptance for agreement (Field 2008). Furthermore, MPs' behaviour is often constrained by the need or desire to maintain party discipline. This is partly due to MPs' desire for personal advancement, which is only possible by advancing within their own party's hierarchy and partly by the need for their party to be re-elected if it is to continue to put its policies into practice (Weaver 1986). Gould (2011) also identified Labour's redistributive (albeit only moderately so) tax policies as one of the key reasons why it lost the 1992 General Election, which it had expected to win right

up to polling day, and stated that they realized that they must not repeat this 'mistake' if they wanted to gain power.

Between 1997 and roughly 2007 resistance had remained dormant because conditions were not suitable, but traditional Labour values had not been fully extinguished and were reasserted once electoral support for the government appeared to be faltering and, after such a long period, it was unexpected by the Labour leadership. The counter-arguments that Labour's welfare reforms since 1997 had demonstrated their commitment to the poorer sections of society failed to convince, possibly because those previous gains had been spent or committed. Perhaps most importantly, the issue was simple and visible and attained a symbolic significance well beyond its financial impact. The changes were visible, because, even if the changes did not adversely impact higher earners, many of them would have known people who were adversely affected, such as their cleaners or child-minders. This personalized the effects of the changes, particularly as they would consider these workers to be the 'deserving poor'.

6.6. Summary

In this and the previous four chapters I have argued that taxation is a nexus between citizens and the state and tax policy is therefore shaped by the nature of that relationship. The UK now characterizes a neoliberal state in which the state has been reconfigured to put it at the service of capital and this is justified by a rationalizing discourse in which the economic domain has been separated from and been given precedence over the social domain. Power is deployed in

order to harness the biopower (see chapter 3.2.), so that individuals support or acquiesce in this.

However, in order to do this it is necessary for power operate in a very different manner from in previous state forms. Whereas power previously tended to operate in an overt, hierarchical manner, in a neoliberal state power operates covertly and in a capillary manner through assemblages made up of a number of actors, of which the state is one, but which also includes quangos, international bodies and large corporations (Dean 2010). Through these assemblages neoliberal states align individuals' personal objectives and aspirations with those of the state. Power is also deployed in a covert manner through the construction of knowledge and this knowledge is based on the principles of neoclassical economics. However, I demonstrate that these principles are constructs based on flawed assumptions and therefore argue that they are a rationalizing discourse for an ideology whose aim is to transfer resources from poorer sections of society to wealthier sections and, in particular, to capital.

Since tax policy reflects the dominant power relations in society, it should not be surprising that tax policy in a neoliberal state is based on techno-rational, economic principles, at the expense of social objectives. This chapter has therefore demonstrated how the taxation system has been reconfigured to facilitate and transfer resources to capital by reducing taxation on profits and coercing individuals to put themselves at the service of capital. This may either be by providing labour or by financing the infrastructure used by capital to earn

profits through taxation of their wages and salaries or payments for goods and services which were previously financed through taxation, such as student tuition fees (Boden & Nedeva 2010).

Whilst this chapter demonstrates the operation of power in the reconfiguration of the tax system, in the following chapters I discuss some of the key contemporary debates in taxation in order to examine how power operates, or fails to operate, through them to further this process. In chapter 7 I discuss tax simplification, arguing that, whilst this is intuitively attractive and many practitioners and academics advocate it for purely practical reasons, it may be a rationalizing discourse for still further significantly reducing the tax burdens of wealthier taxpayers and transferring resources to capital, particularly when it is advocated in the form of the adoption of the 'flat tax'. This is the operation of the second dimension of power (Lukes 2005), but despite the rhetoric progress in implementing meaningful simplification to the UK tax system has been limited. This therefore demonstrates that the second dimension of power has not been adequate to construct knowledge in favour of tax simplification as a means of transferring resources to capital and the chapter therefore analyzes the reasons for this.

In chapter 8 I discuss whether basing tax law on more general principles rather than on detailed rules, as is currently the case, might provide a more fruitful basis for the construction of knowledge in favour of a transfer of resources to capital. The use of principles is often advocated as a means of countering tax avoidance by large corporations and would therefore be a means of transferring

resources *away* from capital. However, I argue that uncertainty is inherent in both rules and principles due to imprecision in the meaning of language and therefore require the exercise of judicial discretion. In the case of rules this discretion is hidden behind an objective façade and the meaning of statue and case law arises from the *post hoc* rationalization of judicial decisions. In the case of principles the discretion is overt and in order for the overt uncertainty not to cause concern the idea of the existence of judicial discretion needs to become hegemonic, so that it seems perfectly natural, or taxpayers need to be convinced that it will only be used against schemes of which they disapprove. One way in which concern can be allayed is through issuing extra-legal guidance, but this is susceptible to the exercise of the third dimension of power, since there are fewer democratic safeguards and this guidance might be influenced by lobbying by powerful actors so that the guidance is framed to favour their interests.

In chapter 9 I discuss the controversies which have arisen since late 2010 concerning corporate tax avoidance and the use of bespoke agreements to settle tax disputes in order to illustrate the power relationships between HMRC and large taxpayers. These disputes led to the emergence of UK Uncut, a grass-roots campaigning group which opposes government spending cuts and corporate tax avoidance, which, it believes, is the root cause of them, and I use these controversies to discuss the possibility of effective popular resistance to neoliberal policies.

CHAPTER 7: TAX SIMPLIFICATION – THE LIMITS OF POWER

7.1. Introduction

In chapter 6 I argued that since the late 1970s the UK tax system has been reconfigured to become a means of transferring resources to capital from poorer to wealthier taxpayers. I have demonstrated that the neoliberal state is ideologically constructed by neoliberal economics. In this chapter I begin to explore how that economic discourse is used as a source of power to hold the dominant neoliberal ideology in place. In particular, this chapter looks at the discourse of tax simplification and is based on my published paper on this subject (James 2008).

There is no causal connection between tax simplification and the construction of a tax system which serves the interests of capital and the wealthy and many advocates of tax simplification (e.g. Avery Jones 1996; Kempster 2006) appear to be motivated by nothing more than its intuitive attractions for taxpayers and tax practitioners alike. However, tax simplification is a discourse into which other discourses can be interpolated. These may be explicit (e.g. Myddleton 2003) or tax simplification may be used as a stalking horse for a discourse which is not explicitly stated, but which can be inferred from an analysis of its likely effects. I argue in this chapter that proposals to introduce a flat tax (a tax system in which all relief and concessions are abolished, apart from an enhanced personal allowance, and all income above that threshold is taxed at a single rate) by Hall & Rabushka (1995) and Forbes (2005) in the US and Teather (2004) and Heath (2006) are examples of such a discourse. However,

despite these calls the flat tax has never gained a significant amount of support in the UK or other more developed countries. Tax simplification and in particular the flat tax will generally benefit wealthier taxpayers and the chapter concludes that the failure to construct knowledge in support of simplification demonstrates that the second dimension of power is inadequate to mobilize support in order to explore the limits of power.

This chapter has the following sections. Chapter 7.2. explores the calls for tax simplification from both practitioners and academics and the opposition which has arisen when detailed proposals for simplification have been made. Chapter 7.3. analyzes the underlying reasons why significant simplification of the tax system has so far been elusive. In both sections I use the flat tax as a case study to illustrate the barriers identified. This is followed by a concluding discussion in chapter 7.4.

7.2. Calls for Simplification and Responses to Proposals

Calls for simplification have come from a number of quarters. In the UK Peter Kempster, the then president of the UK Chartered Institute of Taxation (CIOT) wrote in a letter to the Financial Times that:

> We do not for a moment suggest that tax legislation in the UK is not in need of modernisation: our concern is that the real focus of the modernisation should be simplifying the system and making it easier to comply with its requirements. That is something the CIOT will continue to campaign for and offer

> constructive suggestions on.
>
> (Kempster 2006:19)

Other leading practitioners have used a more high-profile platform to make their calls for simplification. In the 1996 IFS annual lecture John Avery Jones said:

> The result [of the pursuit of certainty] is that tax legislation is more than four times as long as it was 25 years ago, but I do not believe that we have achieved any more certainty, rather the reverse. The time has come to do something about it.
>
> (Avery Jones 1996:63)

In the 2007 Hardman memorial lecture Mike Truman, the editor of *Taxation* called for a reduction in the total size of the Income Tax (Earnings and Pensions) Act 2003 and the Income Tax (Trading and Other Income) Act 2005 by 25% in five years (Truman 2007a:565).

Whilst Kempster, Avery Jones and Truman were all senior members of the tax profession, they were not officially writing or speaking on behalf of any professional body, even if their views were widely shared by other practitioners. Professional bodies have also called for tax simplification and these calls have not been limited to the United Kingdom; indeed, tax complexity and demands for simplification are a global concern (Sawyer 2013; Budak et al. 2014). In its memorandum submitted to the Chancellor of the Exchequer in October 2007, the Tax Faculty of the Institute of Chartered Accountants in England and Wales

(ICAEW) devoted four paragraphs to tax simplification. It stated that 'there is a wide recognition that the UK's tax system has become too complicated' and recommended that the government should make a formal commitment to tax simplification and the establishment of a steering committee, tasked with the preparation of a tax simplification action plan (ICAEW 2007:28-31 cited in Chittenden & Foster 2008). In its Tax Policy Concept Statement entitled 'Guiding Principles for Tax Simplification', the American Institute of Certified Public Accountants (AICPA) stated that

> simplification must be viewed as a priority tax policy objective and given substantial consideration in conjunction with the development of legislation and administrative guidance.
> (AICPA 2002:9)

The possible obstacles to tax simplification are summarised in three brief paragraphs at the end of the statement, but the AICPA sees these as challenges to the profession to communicate the need for simplification and its economic, social and political benefits, and the need to educate lawmakers on the causes of complexity rather than as real obstacles (AICPA 2002:12). Academics have joined this rallying cry. Kopczuk (2006), for example, whilst not calling explicitly for tax simplification, considered that the most important consequence of complexity was the extent to which it creates opportunities for tax avoidance and evasion and that a less complex system would reduce the excess burden of taxation.

More recently the director general of the Institute of Directors, Simon Walker, has connected tax simplification and corporate tax avoidance when he suggested that the loopholes that the companies were exploiting were the fault of politicians, since they had created them through faulty drafting of the legislation (in chapter 8 I argue that such uncertainty is inherent in the nature of language) and that the solution was to simplify the tax system (Barford & Holt 2013). *Taxation* magazine (2014) has also complained that the then Conservative-Liberal Democrat coalition failed to simplify the tax system, making it, on the contrary, more complex. Academics, too, have continued to call for simplification and Evans & Kerr (2012:387) have asked whether it is not 'time for simplicity to shine'.

These calls for simplification appear to have no explicit motive other than a desire for simplicity. However, calls for tax simplification can also be allied to another agenda, which might be either overt or covert. For example, Myddelton (2003:2) argues that

> Major tax reform to simplify the UK tax system is possible...Avoiding taxes on income and expenditure which are 'too high' requires major reductions in government spending, mainly on the welfare state.

Myddleton was writing in *Economic Affairs*, which is published by the Institute of Economic Affairs, a free-market think tank, and it is therefore not surprising that a call for tax simplification is allied to a call for significant reductions in

government expenditure. Whilst Myddleton makes no secret of this, later in this piece he proposes having only one positive rate of tax on all income, with the other rate being zero, i.e. a personal allowance (Myddleton 2003:4). This is a tax system which has become known as the 'flat tax', where all tax deductions and concessions except for a standard personal allowance are abolished and all income above this threshold is taxed at a single rate. Others have also called for the introduction of a flat tax, such Hall & Rabushka (1995) and Forbes (2005) in the USA and Teather (2004) and Heath (2006) in the UK. Whilst the tax simplification measures envisaged by, for example, Avery Jones (1996) and Kempster (2006) might be relatively modest reforms of the current tax system, the flat tax would be a far more radical root and branch reform.

These calls are an attempt to exercise Lukes's (2005) second dimension of power, since they seek to mobilize bias in favour of tax simplification and organize the issue onto the agenda and they attempt to mobilize support by constructing knowledge in its favour (Foucault 1980). In the case of Avery Jones (1996), Kempster (2006) and Simon Walker (Barford & Holt 2013) this knowledge is that simplicity is an inherently desirable characteristic of a tax system and that it is worth sacrificing other characteristics, such as equity, in order to achieve this.

However, it also claims that a simpler tax system will create greater certainty and reduce, or eliminate, tax avoidance. These claims attempt to exploit the difficulty in carrying out controlled experiments in the social sciences (Blaug 1997) and the fact that individuals might be convinced to support an idea simply

if they believe that it will benefit them personally (Murphy & Nagel 2002). In this case, although tax simplification will generally benefit wealthier taxpayers, individuals are asked to believe that a simpler tax system will deliver greater certainty and reduce tax avoidance and that this will benefit them through decreased compliance costs and that the additional tax revenue raised from those currently engaging in tax avoidance or evasion will enable tax rates to be lowered.

Advocates of a flat tax attempt to construct knowledge in the same ways. Myddleton (2003) is quite overt in his desire to reduce the size of the state and his argument relies partly on convincing individuals that a smaller state is inherently desirable. However, supporters of the flat tax make two claims which might appeal to individual taxpayers by exploiting the inherent uncertainties contained in adopting the flat tax. Firstly, whilst there are many different suggested versions of a flat tax, they all call for a general lowering of tax rates. For example, in the context of the United Kingdom Teather (2004:2) suggests a rate of 22% and Heath (2006:135) a rate of 28%, the latter of which also consolidates national insurance contributions. Sastry and Nugent (1998:14) accept that a simpler tax system will be less equitable, but suggest that taxpayers will accept such unfairness because the reduction in tax rates will mean that their tax liabilities will fall. The validity of this claim relies both on taxpayers' liabilities actually falling and on this reduction being sufficient to stifle any dissent over the decrease in equity, since the flat tax, in particular, favours wealthier taxpayers and will exacerbate the trend of shifting the tax burden to poorer taxpayers which I demonstrated in chapter 6.3.

Secondly, despite promising lower tax liabilities for taxpayers, proponents such as Sastry and Nugent (1998:30) generally claim that the change would be tax-neutral. The assumptions underlying this are that any reduction in tax revenue from the lower tax rate would be offset by increased revenue due to a broader tax base achieved through the elimination of 'loopholes' and an increase in voluntary compliance, caused by tax evaders and tax avoiders now believing that the tax saved by evasion or avoidance does not justify the potential penalties from getting caught in the case of tax evasion, or the costs associated with the avoidance schemes in the case of tax avoidance.

Whilst tax simplification may be intuitively attractive and make good populist politics, the rhetoric has not been matched by tangible progress towards this goal. This cannot be dismissed as a problem which is unique to the UK, since a comparison of tax simplification projects in Australia, New Zealand and the UK by Sawyer (2013) has concluded that, whilst none of them have been complete failures, their achievements have fallen far short of initial expectations and radical simplification remains elusive. For example, Australia, New Zealand and the UK have all rewritten tax legislation in simpler language, but this has not addressed issues such as the complexities of defining the tax base or the need for anti-avoidance provisions. The UK government set up the Office for Tax Simplification (OTS) as a result of the report by a working party chaired by Lord Howe (Howe 2008) to examine the existing tax code and make proposals for tax simplification. However, I commented at the time that unless it were able to address the underlying causes of complexity it would be unlikely to bring about significant simplification, however eloquently it might allow the case for it to be

made (James 2008:412) and Budak et al. (2014) have borne out these reservations.

Many proposals for tax simplification never progress beyond general proposals, but the inherent problems with them can be seen from analyzing the public response when specific measures do get to the stage of being published. The pre-Budget report of October 2007 proposed radical simplification to the capital gains tax regime by abolishing both indexation and taper relief and replacing it with a single rate of 18%. This nearly doubled the effective tax rate on the disposal of most business assets, with the result that the proposals attracted much criticism. The government responded by adding an 'entrepreneurs' relief', whereby the first £1m of lifetime gains (since raised to £10m) on the sale of a business or shares in a business are taxed at 10%. Sweetman observed that:

> The Chancellor has bowed to public pressure and added an 'entrepreneurs' relief' to his CGT proposals…and advocates of tax simplification will note that this adds about 8 pages of legislation, and we really can't blame HMRC or the government for this. Reliefs equal complexity.
>
> (Sweetman 2008)

Taxation (2014) complained that the government has ignored the OTS, but the consequences of heeding their advice were evident in 2012 when they published a 94-page report on how 'life could be made easier for the five million

pensioners currently affected by the tax system' (Huber 2012). One of their proposals was to abolish age-related allowances for taxpayers over 65 by freezing them until the standard personal allowance reached that level. Chancellor Osborne implemented this proposal in his 2012 Budget (enacted as Finance Act 2012 s.4) and the proposal was subsequently criticized as a 'granny tax' and a £2bn 'raid' on pensioners (Huber 2012).

Proposals which claim to simplify the tax system may not do so in practice. The proposal in the 2014 Autumn Statement (Gov.uk 2014) to abolish the £8,500 threshold for benefits in kind provides a recent example of this from the UK. Reminiscent of the attempt to simplify CGT in 2008, Chancellor Osborne felt it necessary, following representations, to replace this with exemptions for carers and ministers of religion. These exemptions may well be equally complex as the legislation they replace and, as Fisher (2014) observes, raises equity issues, since the above will be treated more favourably than, say, charity workers (to say nothing of which religions might qualify for the exemptions).

What the reaction would be to a proposal to adopt a version of the flat tax is speculative, since this has not been seriously considered in the UK. However, versions of the flat tax have been adopted in a number of former Communist countries in Eastern Europe and Peichl (2013) has reported that the Slovakian parliament voted to abolish the flat tax in January 2013 and that its abolition has been widely discussed in Bulgaria.

The failure of rhetoric in favour of tax simplification and related policies such as the flat tax to be translated into concrete reforms and the resistance which is often encountered when specific proposals are made both suggest that, despite their intuitive appeal, the second dimension of power is inadequate to construct knowledge and mobilize support to implement them. The following section therefore explores the barriers to simplification which the second dimension of power has been unable to overcome.

7.3. Barriers to Simplification

Barriers to tax simplification can be classified into one of two types. The first one is barriers arising from inertia and a resistance to change. Even if there are no fundamental objections to simplification, it may be difficult to mobilize support for change because taxpayers are familiar with the current system and do not feel that the benefits are sufficient to make it worthwhile campaigning for it. The second type is likely to be more intractable. These barriers arise where there appears to be a conflict, possibly irreconcilable, between simplification and other characteristics of a tax system which taxpayers value more. These barriers are therefore likely to generate resistance beyond simple inertia unless taxpayers can be either persuaded to change their preferences relating to which characteristics they value most in a tax system or by misleading them about the consequences of simplification, so that they over-estimate the advantages and under-estimate the disadvantages.

An example of the first type of barrier is that, for the great majority of individuals and for quite a lot of companies in the UK, the tax system is quite simple and most income has the right amount of tax deducted from it at source (Broke 2000). In the United Kingdom only 16% of taxpayers were required to complete a tax return in 2005, compared with 44% of taxpayers in the United States in 2004. Combined with a limited regime of withholding tax at source in the United States, this is likely to give taxpayers in the two countries very different perspectives on tax complexity (Murphy 2006). The UK tax system and tax legislation is highly complex for a minority of taxpayers and their advisors, who, unsurprisingly, have been leading the calls for tax simplification (Broke 2000). These calls are unlikely to enthuse taxpayers who do not have to submit a return.

Some provisions of the tax code may be little used in practice, with the result that abolishing them will not achieve significant simplification in practice. For example, the 2014 Autumn Statement (Gov.uk 2014) proposed abolishing the £8,500 threshold, below which employees are termed ‘lower-paid’ and many benefits in kind are not taxable (Fisher 2014), a proposal which has now been enacted in the Finance Act 2015 Sch. 1. This measure likely to help only a very few taxpayers, since in 2015 it was only necessary for individuals aged 21 or over to work 25 hours per week at the minimum wage of £6.50 in order to exceed this threshold (Gov.uk 2015). An even more anachronistic provision, most recently to be found in the Income and Corporation Taxes Act 1988 s.198(1), was a specific deduction for the costs of office and employment holders keeping a horse for the purposes of the office or employment,

notwithstanding the general stringent rules for deducting expenses from employment income. This provision was not abolished until these provisions were rewritten as the Income Tax (Earnings & Pensions) Act in 2003. It had long outlived its purpose, but was latterly simply treated as a gentle and quirky joke and did not cause any practical problems. However, abolishing such outdated provisions can be seen as easy wins for politicians and civil servants.

However, even the modest degree of simplification achieved by politically easy wins may be illusory. For example, the abolition of the £8,500 threshold may appear to simplify the taxation system, but the introduction of specific provisions targeted at carers and ministers of religion in the Finance Act 2015 (Finance Act 2015 ss.13 & 14), make it questionable whether these new specific provisions make the taxation system simpler overall (Fisher 2014). However, apparently simple and certain rules might mask hidden complexities arising from the fact that, by virtue of their very simplicity, they are silent on how they should be applied in many common situations. Donaldson (2003) is sceptical whether simplifying the tax system will necessarily lead to greater certainty and distinguishes between mass and specific complexity. Simple rules contained in a simple system create specific complexity because there is little guidance on how they are to be interpreted in specific situations. Donaldson gives as an example the interpretation of the phrase ‘unforeseen circumstances’. If no guidance is provided there is no impact on a taxpayer unless they believe that their circumstances might possibly be unforeseen. In these cases, however, they must seek advice and very possibly take the matter to the courts. This may be expensive and only those taxpayers with sufficient resources will be able to

challenge the initial ruling of the tax authority, which is the exercise of the second dimension of power through organizing out of many taxpayers.

If an attempt is made to clarify interpretation, mass complexity may result, since the guidance must be read and digested by all professional advisors. If a taxpayer needs to determine whether their circumstances are ‘unforeseen’ they will still probably need to seek professional advice, but the advisor is likely to be able to give this far more quickly and cheaply due to the guidance available. The relationship between simplicity and certainty is therefore likely to be much more ambiguous than simply stating that simpler tax systems are inherently more certain. However, not only may different sorts of complexity arise in simple and complex systems, but because the guidance is extra-legal there are therefore fewer democratic safeguards against powerful actors, such as the interests of capital, influencing it to further their interests, which is the exercise of the third dimension of power.

Broke (2000:21) observes that tax systems have developed organically, consequently making piecemeal reform difficult and that they are like a child playing with Lego: bits get stuck on as needed and, once there, tend to stay there. It is difficult to change the older parts of the structure, the parts at the centre, since a lot of the outside bits will come off as well. Therefore, provided that the system functions

> nobody wants the political pain of making the change...[a]nd, I mean, that’s certainly bedevilled tax reform for a number of

> countries, including, particularly the UK.
>
> (Interviewee cited in Frecknall-Hughes et al. 2014:33-34)

Despite constant change, the basis of the UK taxation system can still be traced to the early part of the nineteenth century. One area of taxation which illustrates the problems caused by organic development well is the remittance basis, whereby non-domiciliaries are only taxed on their overseas income to the extent that it is remitted to the UK in a tax year. The remittance basis may never have been intended by Parliament and might simply have been introduced as part of a 'grand sweeping-up clause', which was re-enacted in every consolidation (Avery Jones 2004:37) until in July 2015 the government announced that from 2017 individuals who had been resident in the UK for 15 of the past 20 tax years would no longer be able to claim non-domiciliary status (Gov.uk 2015b). The HMRC manuals admit that this provision was an anachronism.

> The remittance basis made very good sense in its day. Where a business or possession was wholly abroad we simply had no way of enforcing our tax, at least by recourse to the assets of the business. We could not send our officers out to check the accuracy of returns.
>
> (HMRC 2008)

Avery Jones (2004) points out that the remittance basis had its origins in the days when international payments were made by bills of exchange. The remittance basis was originally far wider in scope than nowadays and applied to

profits from overseas trade, since there was likely to be a considerable delay between the sale of goods and receipt of the money. In general, the issue was not whether the money would eventually be remitted to the UK, but simply of delaying taxation of the profit until the trader had the money with which to pay. The practical justification for the remittance basis in these circumstances has long disappeared, but the fact that it survives at all, even in a more restricted form, is an accident.

In this section I have demonstrated the difficulties of constructing knowledge to mobilize support for tax simplification, but tax simplification can be a discourse through which power may operate in other ways. For example, the remittance basis could simply have gone the same way as the horse many years ago, but it also illustrates the operation of power, because it has, over the years, been reinvented as an important international tax planning tool. There would have been fierce resistance from those in whose interest it operates (and those who represent them) and these actors might make overt or covert threats that wealthy foreigners might be less willing to live in the UK if they had to pay UK tax on their overseas income, thus denying the UK revenue from their spending here (Swinford 2015). However, power is never absolute and eventually public pressure has persuaded the government that restricting the remittance basis in this way was politically preferable to acceding to the threat of the non-domiciliaries (HMRC 2015b). This is an example of a shift in public opinion producing tangible results and I discuss the potential for resistance to the neoliberal paradigm in more detail in chapter 9, but from a tax simplification

point of view it is doubtful from reading the Budget Technical Briefing[1] whether this reform will simplify the tax system.

The remittance basis still survives in a more restricted form and there will be provisions to cover the situations where, for example, an individual who has been resident in the UK for more than 15 of the previous 20 years leaves the UK for a period and later returns. Furthermore, even if the remittance basis were to be abolished entirely, even for temporary residents, this could make the tax system for certain taxpayers. For example, Australians and New Zealanders living in London under the 2-year work/travel visa scheme might be liable to UK income tax on investment and property income arising in Australia or New Zealand, although it would in most case be covered by Double Tax Relief.

It is not just the survival of outdated provisions which cause problems for a tax system whose fundamental design dates from an earlier age, but it must also cope with a tax base which has become increasingly founded on abstract measures of income, rather than products (Snape 2015). One example he cites is transfer pricing where the tax system must determine an appropriate price for goods and services supplied between arms of a transnational corporation and this involves income or liability measurement under ‘a weighty and arcane codification of national and international accounting practice’ (Picciotto 2011:272). This problem is exacerbated by the fact that there are generally no true comparables for these goods and services, since these corporations

[1] This thesis was submitted on 13 July 2015 before the publication of the Finance Act.

usually produce distinctive products or services and can do so at lower prices due to economies of scale and scope (Picciotto 2015).

Not only must the operation of the second dimension of power overcome inertia, but a more intractable reason for the failure of tax simplification to gain support is that, whilst taxpayers might value simplicity in the abstract, it might conflict with other characteristics which they value more, such as equity and certainty. Proposals to simplify the tax system are based on the assumption that the system tries too hard to be fair and that a simpler tax system could be achieved, if taxpayers were to accept some measure of inequity (Gammie 1996). However, whilst qualities such as equity and certainty may be inherently desirable, simplicity is not, since if a simple rule causes a decrease in equity it may not be desirable (Donaldson 2003).

In order to mobilize support for simplification through the operation of the second dimension of power it may therefore be necessary to persuade taxpayers to accept a loss of equity and certainty as a trade-off for greater simplicity. However, if they are not willing to accept this and an attempt is made to impose a tax reform which is seen as inequitable, they resist. The clearest example of this in modern times was the introduction of the Community Charge or Poll Tax in 1990. This was an extremely simple tax, but was widely seen as unfair, with the result that there was significant resistance through evasion and often violent protests which were contributory factors in the resignation of Margaret Thatcher as Prime Minister later that year (Budak et al. 2014).

Advocates such as Avery Jones (1996) tend to compare the simplicity, equity and certainty of the tax system as a whole, whereas even if taxpayers were to agree that a simplified tax system would be collectively beneficial, Olson (1971) argues persuasively that it does not necessarily follow that they will collectively demand it. He argues that in the case of a public good there is a contradiction between the collective interest of a group and the interests of its individual members. Individuals may not lobby for a particular measure or course of action, even though they acknowledge that it is in the collective interest and this will therefore lead to a sub-optimal result.

This is illustrated by Olson as follows: it is assumed that there are a large number of firms in a particular market, so that no single firm can influence the market through its unilateral actions. If a market is temporarily not in equilibrium and marginal revenue exceeds marginal cost, it will therefore be in the interest of an individual firm to increase their output, since if it acts alone this will not cause the price to fall and they will therefore be able to sell all of their increased output at the higher price and thus increase their revenue. However, the prospect of one firm exploiting this situation will tend to make all firms increase their output, which will cause the price of all output, not just the additional output, to fall and thus decrease the total revenue and profit of the industry. Each individual firm has therefore optimized its own position, but the outcome is sub-optimal from the point of view of the group. This paradox is the foundation of game theory, in which individuals attempt to maximize their own personal return, but where the costs and benefits of the various options depend on the actions of others.

The only way to prevent the price from falling is either through government price support or a cartel agreement (Olson 1971). This is, however, difficult to bring about because the same conflicting forces which caused the original situation will again operate. In order to obtain government price support it will be necessary to organize a pressure group, which will incur costs which must be met by the members. Again, assuming that the action of any single member has no effect on the group, as the price support or agreement is a public good it is therefore possible for an individual member to be a 'free rider' by opting out of the pressure group, thereby gaining the benefits without incurring the costs. Similarly, a cartel member may break ranks and still enjoy the benefits of the cartel agreement without being subject to any restrictions which it may impose.

Olson's theory can therefore also explain why it is difficult to use the second dimension of power to mobilize support for tax simplification. Tax simplification is a public good because no taxpayer can be excluded from enjoying its benefits and enjoyment of its benefits by one taxpayer does not reduce the benefits available to other taxpayers. It is therefore in the collective interest to lobby legislators to simplify the tax system. Each taxpayer will, however, only receive a fraction of the benefit of simplification, the exact amount depending on their individual circumstances. For example, a taxpayer whose sole income consists of employment income from which tax has been deducted at source will receive no direct benefit and the indirect benefits will be of less importance since they are invisible to them (McCaffery & Baron 2004). Taxpayers with more complicated tax affairs will receive a much greater direct benefit.

The potential cost to a taxpayer is that a particular reform will impact them adversely. In this case the cost of the reform to such taxpayers may outweigh the fractional benefit from the public good and they may therefore resist the reform. The effect of introducing a rule to help such taxpayers will not on its own make the tax system significantly more complex, but complexity will arise from the accumulation of such measures. However the economic benefits to a discrete constituency of taxpayers of a measure taken in isolation and the political benefits to be gained from satisfying this constituency will generally exceed the cost of greater complexity.

Finally, even if a taxpayer concludes that tax simplification is in their personal interest, they might not take part in lobbying for change, since doing so incurs both financial and time costs. Being a public good, the taxpayer will benefit from tax simplification regardless of whether they have helped campaign to bring it about and they may well be tempted to leave the costs of campaigning for change to others, whilst still reaping the benefits.

Brown (1996) makes the same argument as Olson from the point of view of the tax practitioner.

> I have been part of a number of delegations of taxpayers who have gone to Ottawa to pound the table about the horrific complexity of our Income Tax Act, and immediately thereafter to pound the table some more to ask for dozens of exceptions, special rules and concessions, which complicate the statute

> still further. Taxpayers collectively seek simplicity, understanding and clarity in the tax regime. But individually, they veer towards special rules, exceptions and incentives.
> (Brown 1996: 5.11)

Brown's admission is particularly interesting because it reveals that many tax practitioners are conflicted. Whilst part of them wants simplification, another part realizes that it is not realistic to expect it to happen or, even, that it will not benefit them, since unfairness might disadvantage their clients and helping clients to navigate a complex tax system is the source of their business. If many of those advocating simplification are less than whole-hearted, it need not be a surprise if the second dimension of power is inadequate to convince taxpayers that they should value simplicity over equity. Examples of measures introduced either in response to, or to pre-empt, protests are the 10% entrepreneurs' rate of capital gains tax (Sweetman 2008) and the specific reliefs for carers and ministers of religion who might be disadvantaged by the abolition of the £8,500 threshold (Fisher 2014).

Philosophically then, there are areas of conflict between equity and certainty on the one hand and simplicity on the other. Examination of the research in the area allows us to ascertain whether this conflict materializes. Gamage and Shanske (2011:19, 33) attribute tax complexity to taxpayers' lack of tax salience, i.e. their perceptions of what legislation requires differ from what it actually requires, which causes taxpayers to depart from key assumptions of neoclassical economic theory. There have been a number of studies on the

relationship (or, more accurately the perceived relationship) between simplicity and equity. The results have generally been mixed. Milliron's (2001) study amongst a jury pool in Los Angeles presented respondents with a number of pairs of tax scenarios which they were asked to rate according to simplicity and equity. Correlating the results, Milliron concluded, perhaps unsurprisingly, that the scenarios which were perceived as being simpler were also perceived as being more equitable.

In contradistinction, a study carried out by Carnes and Cuccia (1996) concluded that the relationship between equity and simplicity is much more subtle and ambiguous. They asked 122 respondents to agree or disagree with the statements that 'most complexity in the tax law is unnecessary and creates needless difficulties for people trying to file correct tax returns' and 'complexity in the tax law is necessary to ensure that everyone pays their fair share of tax' on a seven-point scale, where 1 = strongly disagree and 7 = strongly agree. Mean responses were 5.31 and 2.78 respectively. This suggests that, in general, respondents did not believe complexity to be justified. When respondents were asked to provide equity and complexity ratings for 15 specific items with which they were familiar, the equity perceptions varied significantly across the various items and complexity was found to be negatively correlated with equity perceptions. But when respondents were presented with the reason for the complexity of the various items, their perceptions of the justification for the complexity moderated their perception of its relationship with equity. White et al (1990, cited in Carnes & Cuccia 1996: 43) also found that many specific

tax items were perceived to be more equitable when taxpayers were given even a basic understanding of the tax system.

White et al's (1990, cited in Carnes & Cuccia 1996) and Carnes and Cuccia's (1996) research therefore makes a link between the understanding of tax provisions and their purpose and the acceptance of complexity. However, in neoliberal states an understanding of tax provisions may not be to the benefit of hegemonic groups. Mumford (2015) argues that a purported consequence of a lack of tax salience is a growth in the size of the state. Since the tax system is an integral part of the coercive, regulatory state it is desirable from the point of hegemonic groups if taxpayers are unaware of the way in which power is exercised through the tax system, since successful tax legislation is not sustained by overt coercion, but by broad conformity with the neoliberal consensus which is characterized by 'economistic' political debate and a restrictive scope of tax policy discussion (Snape 2015:159).

This suggests that where taxpayers understand a particular area of the tax system, not only is the second dimension of power inadequate to persuade taxpayers to prioritize simplicity over equity and certainty, but it is also difficult to exercise the third dimension of power to create a false consciousness through the power to mislead (Lukes 2005). This normally operates through the hegemonic group possessing, or appearing to possess superior knowledge about the consequences which will flow from particular actions. It is therefore easier to gain support for ideas and policies if their details can be kept vague and open to a variety of interpretations (Smith 1987), since this permits the

hegemonic group to construct knowledge surrounding the consequences in a manner which suits them.

Groups of taxpayers often have a good understanding of the particular area of tax *which affects them*. Since tax simplification cannot progress beyond rhetoric unless concrete proposals for the reform of specific areas of the tax code are put forward, taxpayers are therefore able to analyze them in detail to determine whether they will be adversely affected, and the nature of taxation means that any such effect will be felt immediately and acutely through a financial loss. Even if taxpayers are not able or willing to do this themselves, the admission by Brown (1996) that tax advisers are conflicted means that they will analyze the proposals on behalf of their clients. There will also always be at least one alternative with which the proposals can be compared; the status quo.

The reasons discussed in this section for the failure to mobilize support for tax simplification all assume that tax policymakers fundamentally desire a simpler tax system, but are frustrated either by the collateral costs of the reforms or by resistance from taxpayers. However, complexity is a necessary and inevitable feature of tax systems in neoliberal states because that the tax system has become an important component of the regulatory state and therefore has taken on the function of coercing individuals to comply with privatized forms of governance (Snape 2015). This is not only a feature of the UK tax system and Gribnau (2015:229) argues that the Dutch government uses its tax system for non-fiscal purposes as an integral part of government policy. He lists some of the ways in which it seeks to micromanage the behaviour of taxpayers through

tax incentives, such as commuting by bike, employee training, day-care centres and production of Dutch movies and these incentives can also be found in the UK tax system.

The failure to gain sufficient support for the adoption of a version of the flat tax in the UK and other countries in Western Europe, North America and Australasia is a good example of why it has not been possible to exercise the third dimension of power by misleading taxpayers of the consequences of reforms. The ability to mobilize support for the flat tax relies on the credibility of the claim that individuals' tax liabilities can be reduced, whilst the overall tax revenue raised remains constant, or even rises. However, despite their headline claims, even supporters of the flat tax undermine their position in this respect if their detailed figures are examined. For example, Sastry and Nugent's detailed calculations based on US statistics for 1996 estimated that their reforms would result in a shortfall of $58.3 billion ($809 billion under the existing system as compared with $750.7 billion under their proposed system, a fall of 6% in tax revenue) (Sastry & Nugent 1998: 30-31). Similarly the flat tax proposals of Dick Armey suggested a rate of 17%, although, according to Toder (1996: 4.4) a rate of 20.8% would have been necessary for the proposals to be completely tax-neutral. Armey proposed that the shortfall would be paid for by capping government expenditure, including entitlements (National Centre for Policy Analysis 1997).

If taxpayers do not believe that tax revenue can be maintained, whilst reducing individuals' tax liabilities, they must be convinced that a reduction in tax revenue

and the consequent reduction in government spending is justified. As I have previously argued, it is easier to construct knowledge in favour of a particular proposal if the details remain vague, since, whilst taxpayers may be in favour of lower tax liabilities, McCaffery and Baron (2005) suggest that this support weakens when they are asked to choose where cuts in public spending should be made. No comment was made by Sastry and Nugent on the feasibility of cutting government expenditure by the required amount beyond stating that the 6% shortfall would be met by curtailing welfare programmes, but the reality of cutting such sums from government spending may result in decisions being made which prove highly unpopular with many of the same taxpayers who are in favour of the reforms in general and may also provoke protest and civil unrest.

When the flat tax was first proposed evidence concerning its effect on overall tax revenue necessarily relied on forecasting techniques. However, since a number of countries in the formerly Communist Eastern Europe have operated a flat tax (or, at least, something approximating to it), for a number of years, evidence can be obtained from their experiences. For example, Tóth & Virovácz (2010) found that, in Hungary, the adoption of the flat tax resulted in a reduction in tax revenue of Ft444bn (roughly £1.1bn). Similarly, the introduction of the flat tax in Kyrgyzstan in 2009 has reduced tax revenue (Ismailakhunova 2014). Even where the introduction of the flat tax led to an increase in tax revenue as, for example, in Russia in the early 1990s, it was not possible to determine the extent to which this was attributable to the flat tax or to other factors, such as the increase in real wages and the introduction of basic anti-avoidance

measures, such as giving taxpayers numbers (Ivanova et al. 2005).

It is not only the effect of a flat tax on overall tax revenue which might concern taxpayers, but also the redistribution of the tax burden between different groups of taxpayers. Whilst one of the most appealing claims for the flat tax is that all taxpayers would pay less, Toder (1996:4.4) states that if the Armey proposals were adopted in the US, with the exception that the revenue-neutral rate of 20.8% was used, instead of Armey's proposed rate of 17%, the federal effective tax rates for families in the bottom four quintiles of the population would rise by between 10% and 81%, but would fall by 7% for families in the top quintile and by 36% for families in the top 1%. Similarly, Jeffrey Owens and Stuart Hamilton of the OECD have claimed that in, for example, New Zealand, only the richest 10% of households would pay much less tax if a flat tax of 25% were introduced (Owens & Hamilton 2005:70). It is interesting that Owens and Hamilton, who appear to be supporters of the flat tax, try to minimise its impact, but ignore the political reality that a tax system which substantially benefits the already wealthy may be unacceptable to the majority.

The redistributive effects of the flat tax in favour of wealthier taxpayers are borne out by studies carried out in countries which adopted it. For example, Tóth & Virovácz (2010) found that, in Hungary, the adoption of the flat tax not only resulted in a reduction in tax revenue of Ft444bn (roughly £1.1bn), but that the tax burden on the bottom seven deciles of the population increased by Ft134bn, whilst the tax burden on the top decile fell by Ft501bn.

Even if it is not explicitly stated it is easy to calculate that a flat tax would be likely to give very large tax cuts to high earners. For example a flat rate of 35% will translate into a saving of roughly £500,000 for a top footballer earning £5m a year (based on the great majority of the income being taxed at a marginal rate of 45%), whilst it would increase the tax paid by middle earners on £60,000 by roughly £3,000. This means that, disregarding any other factors, it would take roughly 160 middle earners to pay for the tax cut of one footballer. Given the rate suggested by Teather (2004:2) of 22%, the savings for a top footballer and a middle earner would be roughly £1.15m and £3,000 respectively. At this rate all taxpayers would pay less than under the current system. This would leave a very significant shortfall in revenue to be made up from broadening the tax base and reducing evasion and avoidance and also raises the question whether the shift in the distribution of the tax burden would be regarded as equitable.

Slemrod (2003) suggested that many taxpayers might be unaware of the large tax savings which would be made by high-earners under a flat tax. Indeed, according to research in the United States reported by him, 41% of those surveyed thought that high-earners would actually pay *more* under a flat tax and a similar percentage thought that high-earners would pay more under a retail sales tax. However, these misconceptions might have been prevalent when discussions of flat taxes remained confined to think tanks and academic conferences, but if a flat tax were seriously proposed it would doubtless not take long for the media to publicize the potential tax savings of high-profile high-earners and to compare these with the relatively modest savings, let alone with tax increases, of middle-earners. The percentage of the population holding this

misconception would fall rapidly and, Slemrod predicts, support for such regressive taxes would fall.

It is not only the single rate of tax which might bring about a redistribution of resources but certain other characteristics of a flat tax system, of which taxpayers might be initially unaware, are also likely to have a similar effect. For example, whilst the flat taxes proposed by Hall & Rabushka (1995) and Forbes (2005) were intended to replace income tax, corporation tax, capital gains tax inheritance tax, other significant taxes would have remained, such as VAT and excise duties, local authority taxes and national insurance (Murphy 2006). In many countries which adopted the flat tax, social security contributions made up a much more significant portion of the total tax revenue than in the UK. For example, in Slovakia, the employee's contribution rate was 13.4% and the employer's contribution rate was 35.2% and these contributions made up 40.2% of total tax revenue, compared with 18% of the total in the UK (Eurostat 2005). Combined with a high rate of VAT, the social security contributions would have the effect of transferring the burden of taxation from capital to labour and consumption, which is one of the key objectives of neoliberalism. Whilst these aspects of flat tax systems might not currently be widely appreciated, they would be widely publicized if such a system were seriously proposed and, once again, support may well fall.

Peichl (2013) attributes the decision to abolish the flat tax in Slovakia to a combination of the economic crisis and the distributional effects of the social security contributions and indirect taxes adversely impacting the middle classes

and leading to demands that the rich should pay their ‘fair share’. It therefore appears that even those countries which enthusiastically adopted the flat tax are beginning to have second thoughts and that the effects which its critics predicted have been borne out. This evidence therefore makes it much harder to exercise the third dimension of power and construct knowledge to persuade taxpayers to accept such a system.

He also attributed the initial success of flat taxes in transitional Eastern European countries to the use of low marginal rates as a signal of the shift towards more market-oriented policies and that the idea had less appeal in Western European countries in which these reforms and signals were not necessary. Matlack (2013) observed that flat taxes ‘seem to work pretty well’ when the economy is growing, but not when it is stagnant or shrinking. This echoes Campbell’s (2009) observation about the very different and highly progressive tax system in post-war America (an observation which would have applied equally well to the UK) that the public tolerated the tax system because post-war prosperity meant that real post-tax incomes were increasing, despite the high tax rates. It would therefore appear that when an economy is buoyant, taxpayers are relatively unconcerned about equity and the distribution, or re-distribution, of wealth. These concerns tend to surface in harsher economic climates and if it was not possible to exercise the second dimension of power to mobilize bias and build a consensus in favour of flat taxes during times of economic growth, it is hardly likely to be possible in times of recession.

The claim that the flat tax will eliminate, or, at least significantly reduce, tax avoidance opportunities and tax evasion may also be incorrect. This assumption may derive from a belief that the wealthy will always arrange their affairs to pay minimal amounts of tax, or from press stories concerning tax avoidance by certain high-profile personalities and the negligible amount of UK corporation tax paid, for example, by Google, Amazon and Starbucks (e.g. Kiss 2012), despite the fact that corporation tax has always been charged at a single flat rate on profits, since for large companies the small profits' rate is almost always irrelevant. Adopting the flat tax may not eliminate these opportunities, since it is always necessary to have rules concerning the territorial limit of the charge to tax and whether taxpayers have divested themselves of money or assets. Indeed, the flat tax could do the very opposite and legitimate the activities and transactions which are now considered to be controversial, e.g. by exempting capital gains, and this would be the operation of Lukes's (2005) third dimension of power.

Taxpayers' perceptions about the increase in voluntary compliance which would ensue from lower taxes may also be misplaced. Christian (1994, cited in Slemrod 2003) reported that voluntary compliance (i.e. reported income as a percentage of true income) was over 95% for those earning over $100,000, but less than 90% for those earning less than $25,000 (figures from 1988 Taxpayer Compliance Measurement programme data). Slemrod (2003) attributes this misconception to publicity surrounding a few high-profile tax evaders and books detailing tax avoidance and evasion strategies widely used by the wealthy, since tax evasion involving offshore trusts and companies makes for much

more interesting copy than, for example, phantom businesses dealing only in cash. Furthermore the wealthy may not *need* to evade tax under a flat tax regime if it provides sufficient tax avoidance opportunities. For example, if, as many models propose, only wages and business income are subject to tax, there might be attempts to convert income into capital gains. Again, if a flat tax is proposed the media will surely highlight these opportunities, support for such a tax is likely to fall and, if such a tax were implemented, there would be pressure to introduce complex anti-avoidance measures.

In this section I have argued that the second dimension of power is inadequate to mobilize support for tax simplification because it is unlikely to be possible to persuade taxpayers to sacrifice equity for simplicity, since they will only gain a fraction of the benefit of greater simplicity but may bear all the costs of increased inequity if a reform adversely impacts them. Furthermore it is unlikely to be possible to mislead taxpayers that the consequences of the reforms will benefit them when that is not the case through a vague lack of details because proposals for reforms need to be specific. It is a straightforward task to calculate how much more or less specific taxpayers or groups of taxpayers might pay and even where aspects of the reforms are more hidden, the press or the tax profession are likely to publicize them.

7.4. Summary

Tax simplification is intuitively attractive, however (as ever) the devil is in the detail. There have been many calls for simplification from practitioners in both

the UK and the United States and also from academics. However, despite this only a modest degree of simplification has been achieved and many simplifying proposals provoke criticism and resistance. The second dimension of power through the mobilization of bias has therefore failed to gain support for more radical simplification in practice. This is because it is not possible to make progress towards simplification without making specific proposals, the consequences of which are open and transparent.

Resistance may be due to inertia, since the current system is familiar to taxpayers and its complexities do not impact many taxpayers. However, more critically and intractably, although taxpayers desire simplification, they place more importance on other characteristics such as equity and certainty and it has not been possible to persuade them to change this preference. If taxpayers are not prepared to sacrifice equity for simplicity, they must be persuaded, or misled, that they can have both and the flat tax attempts to overcome this problem by claiming to offer all taxpayers lower tax rates, and therefore lower tax liabilities, as a trade-off for any loss in equity, whilst maintaining total tax revenue raised through a broadening of the tax base and a decrease in avoidance and evasion.

However, attempts to mobilize support for such a tax system have so far failed, since its consequences are too open. For example, by far the largest beneficiaries of such a system will be the highest paid and the inevitable publicity surrounding this fact may well lead to a decrease in support. Furthermore, despite their headline claims, an analysis of the detailed figures of

the proposals by, for example, Armey (Toder 1996) and Sastry & Nugent (1998) demonstrates that the adoption of the flat tax would generally cause a fall in tax revenue and this may encounter the problem that taxpayers tend to be much less enthusiastic about making specific tax cuts than tax cuts in general. If a version of the flat tax were to reach the stage of being seriously considered these contradictions and characteristics would be publicized and support for a flat tax would be likely to fall.

Given that the forces which have caused complexity and the barriers to simplification cannot be eradicated, it is therefore unlikely to be possible to mobilize support in favour of a significant degree of simplification and this discourse cannot therefore be used to legitimize a transfer of resources to capital and the wealthy. Actors who wish to transfer resources in this way therefore need to find an alternative legitimizing discourse and the following chapter explores whether the debates concerning basing tax law on detailed rules or on general principles might have more potential to provide such a legitimation.

CHAPTER 8: RULES AND PRINCIPLES

8.1. Introduction

In the preceding chapters I argued that the UK in the 21st century strongly characterizes a neoliberal state, serving the needs and facilitating the operation of capital. As a result of this, the tax burden has been shifted from capital, and in particular large multi-national corporations, to labour and from wealthier to poorer taxpayers by, for example, the reduction of direct tax rates on capital and the increase in the rates of indirect taxes (Dietsch & Rixen 2010). This shift has been justified by the need to incentivize individuals to work and undertake entrepreneurial activity and to attract capital to invest in the UK by offering an attractive or 'competitive' tax system.

In chapter 7 I discussed how attempts have been made to use tax simplification, in particular in the form of the flat tax, to further entrench these shifts. However, it has not been possible to mobilize support by convincing taxpayers that their interests are aligned with those of the hegemonic group, since the consequences of suggested simplifying reforms and flat tax models are transparent. It is therefore only possible to employ Lukes's (2005) second dimension of power by convincing taxpayers to accept, grudgingly or otherwise, greater inequity as a price for greater simplicity. The fact that attempts to simplify the tax system have been largely unsuccessful and have incited resistance from those disadvantaged by them suggests that the second dimension of power is inadequate to mobilize support and it is necessary to employ the third dimension of power to do so. In order to convince taxpayers

that their interests are aligned with those of the hegemonic group the consequences of proposed reforms should therefore not be transparent and their details should therefore remain unspecified, whilst having a superficial appeal (Smith 1987). In this chapter I explore the debate on whether tax law should be drafted using detailed rules or broader, more general principles which would be interpreted by the courts in specific cases as a discourse through which the third dimension of power might be employed to mobilize support for a tax system which privileges the interests of capital and the wealthy.

I examine the rules versus principles debate in the context of its potential to counteract tax avoidance. Tax avoidance is a contest between large corporations and wealthy taxpayers on one side and the tax authority on the other side. Whilst the tax authority is ostensibly acting on behalf of taxpayers and citizens, in a neoliberal state it is conflicted since it is part of the same assemblage of power as large corporations and wealthy taxpayers (see chapter 5.2.). Discretion is inherent in both rules-based and principles-based legislation and can be used to favour the interests of either powerful taxpayers or the state and taxpayers as a whole. One of the key characteristics of a neoliberal state is that it favours the interests of capital, but the conflicted position of the tax authority means that if discretion is to be used to favour powerful taxpayers it must be done covertly in order not to incite resistance.

This chapter has the following sections. In chapter 8.2. I compare and contrast the nature of rules and principles, arguing that there is subjectivity and discretion in both, but that these characteristics are more covert in rules and

that legal certainty is a construct developed from the *post hoc* rationalization of judicial decisions. Chapter 8.3. explores six cases which provide empirical evidence of the subjective power of judges in deciding contentious issues, even in a rules-based system. In chapter 8.4 I discuss how power operates through a rules-based system in the tax avoidance debate. Chapter 8.5. interrogates whether principles-based legislation, and in particular a General Anti-avoidance Rule (GAAR) might enable the state to exercise the third dimension of power and covertly facilitate tax avoidance. This is followed by a summary in chapter 8.6.

8.2. The Nature of Rules and Principles

In order to compare the operation of power in rules-based and principles-based systems it is first necessary to understand the nature of rules and principles and to differentiate between them. Dworkin (1977) argues that rules are prescriptive: if a rule covers the facts of a particular case, the rule prescribes the outcome. Rules should not conflict with each other: if two or more rules apply to a particular case, but each specifies a different outcome, there is an irreconcilable conflict because it is impossible to conform to one rule without simultaneously breaking one or more others. In contrast, Dworkin argues, principles provide reasonings which indicate a particular direction, but do not determine a given outcome. Unlike rules, there is no problem where principles conflict as they merely provide guidance rather than prescribe outcomes. Where more than one principle is relevant it may be necessary to assign each a weighting in order to reach a decision, which need not be the same in all circumstances. Different

decisions therefore may be reached in similar situations because the relevant principles have been assigned a different weighting in each case.

Such an approach implies that, since principles embody the exercise of subjective discretion, they will provide less certainty than rules. John Braithwaite (2002) argues, perhaps counter-intuitively, that principles-based regulatory regimes may provide greater certainty than rules-based approaches in complex and dynamic situations. Rules can only provide a basis for a decision if the facts of the particular case fit the criteria for applying a particular rule. In complex situations this is likely to generate a plethora of rules designed to cover particular circumstances. These rules may conflict, necessitating a choice between rules and, hence, uncertainty of outcomes. In contrast, he concludes that principles lead to greater certainty because they only provide guidance, allowing assessors to use their discretion in deciding which factors indicate compliance or non-compliance in any given situation. He supports this by a comparison of the assessment of nursing homes for the elderly. In Australia, they are assessed through broad standards based on principles such as ‘respecting the dignity of the residents’, whereas in the US detailed rules are used, such as counting the number of residents attending various activities or the number of pictures on the walls of residents’ rooms. Although evaluation according to principles also involves the exercise of judgement and may therefore lead to subjective outcomes, Braithwaite found that the use of broad standards led to greater consistency, and therefore greater certainty, than detailed rules in the assessment of nursing homes.

Where two or more rules or principles conflict uncertainty arises which must be resolved through adjudication. As Braithwaite acknowledges, whilst conflicts between rules should not arise in theory, in practice they do, and this situation is more likely to arise in complex systems, such as taxation. Resolving such a conflict requires a judgement on which rule should have precedence and it is possible that different rules will favour different interests. Adjudicating the conflict will therefore mean favouring the interests of one party over the interests of other parties.

Problematically, these arguments may not be well-demonstrated by Braithwaite's arguments because the regulation of residential homes is a very limited application of the distinction between rules and principles, since conflict between the rights of involved parties will not generally arise when evaluating standards. In contrast, tax cases generally concern a conflict between the rights of two parties which result in (financial) winners and losers. Hence, the exercise of judicial discretion will operate to the benefit of one party and the detriment of the other. Whilst at the formal, first-dimensional level it is only the judges who wield power and the parties to the case each present their case in the best possible light, the parties may exercise the second or third dimensions of power by influencing the legal parameters within which the judges operate.

Tax cases generally reach court only where the rules provide contested outcomes due to ambiguity, making judicial interpretation of legislation inevitable. In criminal cases the prosecutor is the Crown as representative of the state, but in tax cases the plaintiff will originally be a taxpayer and the

defendant will be HMRC (although these roles might be reversed in subsequent appeals). Judges will therefore only rule on cases, and therefore favour one party over the other, where a taxpayer is seeking to challenge the prevailing view of the law and both they and HMRC put forward competing arguments concerning its plain, literal meaning. The scope for judicial discretion in the interpretation even of detailed and apparently precise rules confers considerable power on judges and Lukes's (2005) multi-dimensional model of power can be used to analyze the operation of judicial power in tax systems.

The first dimension of judicial power is where judges simply interpret the techno-rational rules of statute and case law in an objective manner. This accords with John Braithwaite's (2002) notions of interpretation. In the second dimension rules require interpretation in their application to the specific facts of a case and judges exercise considerable discretion through the organization of the decision-making system. For instance, the rules, as detailed by Zander (2004), relating to when judges may depart from case law precedent, which may itself be subjectively determined, allow a large degree of subjective judgement. Judges have the power to depart from the precedent of a higher court or court of the same level where the facts of the case under consideration can be distinguished from the precedent, since this means that the case cited ceases to be a precedent. Judges in the Supreme Court (formerly the House of Lords) may also depart from a precedent of that court where it considers that it is no longer compatible with contemporary society and attitudes and might 'unduly restrict the proper development of the law' (Practice Statement 1966).

The fact that laws need to be interpreted to determine their application to specific situations allows the second dimension of power to operate by actors organizing certain options onto or off the agenda. However, if the principles underlying judicial interpretation appear to be objective and techno-rational, when they are in fact inherently subjective, discretion becomes covert and power operates through the third dimension. For example, Zander (2004:275) argues that the relevant precedents are usually a mixed bag of decisions with different degrees of relevance to the case under consideration. Judges therefore have considerable discretion in deciding which precedents to give weight to, and, furthermore, that a court sometimes 'distinguishes the indistinguishable' in order to escape from an unwelcome precedent. The ability to choose between a number of conflicting precedents and to depart from a precedent due to its incompatibility with contemporary values give judges scope for subjective reasoning. This makes rules a more powerful tool for the exercise of power than proposals for tax simplification discussed in chapter 6 since, whilst the consequences of the rules are transparent, there does not appear to be an alternative.

I demonstrate in chapter 8.3. that judges have found considerable scope to interpret even the 'normal' or 'plain English' meaning of words in a subjective manner in order to reach their desired conclusion (James 2010). Robertson (1998) suggests that, in rules-based systems, judges may reach their decisions by reasoning backwards: instead of the application of rules leading inexorably to a decision, judges will reach a decision based on their own instincts and prejudices and then seek a legal rule which supports it. In many cases, and the

Law Lords admit this readily enough, they work ‘bottom-up’, from a basic instinct that the plaintiff or the defendant ought to win, to an argument that makes them a winner (Robertson 1998:17). He demonstrates that, in cases heard by the House of Lords[1], over 90% of tax and criminal and over 80% of public, constitutional and civil cases could be correctly predicted by simply knowing which judges would hear the case. That the identity of judges hearing cases, which are likely to be among the most complex, provides such a strong prediction of the outcome indicates that even what appears to be strictly technical interpretative reasoning is not objective, but is rather subjective and guided by judges’ personal positions. Countering Robertson's (1998) arguments, John Braithwaite (2002) contends that judges’ instincts or intuitions are grounded in professional training, rather than personal values and that this yields some consistency. However, this in turn begs the question of the extent to which professional training is itself subjectively grounded.

The scope for subjective judgement within detailed rules arises from the inherent indeterminacy of language. Hart (1994) argues that language has a ‘core’ meaning, which is certain, and a ‘penumbra' where the meaning is indeterminate. Words do not have intrinsic meaning, because their meaning is determined by their linguistic context and because language is social, the meaning is constructed through social interaction (Picciotto 2015:169), which suggests that even the core meaning might not be as certain as Hart argues.

[1] The House of Lords was until 2009 also effectively the supreme court of the UK. However, the UK now has a Supreme Court and the House of Lords no longer fulfils this function.

The superficially objective nature of rules-based systems of law also obscures the fact that they are overlaid by normative principles and that rules should be the result of weighing and balancing conflicting principles (Gribnau 2015). The principles are therefore unstated and implicit, whereas in a principles-based system these principles become explicit and the more detailed gloss provided by the rules is absent. However, rules can never be comprehensive operational guides to the operation of legal principles and there always remains a residual normative element and law cannot therefore be divorced from ethical considerations (Gribnau 2015:242). Applying rules to specific cases necessarily involves value judgements, since laws are normative. Even the core meaning might therefore depend on a shared view of its underlying values, which can be fostered by judges' training. Consequently, it is easy for judges to lose sight of the normative element and disagree on the interpretation of laws from an objectivist perspective, attributing disagreements to bad drafting which creates the loopholes in the law (Picciotto 2015:171).

Whilst judicial discretion might operate truly randomly and on personal whim, it might also constitute the mobilization of bias, with certain interests being systemically favoured and others being 'organized out'. Where the exercise of discretion is more covert it is easier to systemically favour particular interests since citizens may be less likely to hold judges accountable for their decisions if they are unaware of the potential of these being based on personal, rather than legal, judgements. In the following section I demonstrate the covert operation of judicial power under rules-based systems by drawing upon six legal cases in

which judges reached conclusions which appear at odds with established precedents and the interpretation of statute.

8.3. Rules and the Operation of Power

In chapter 8.2. I argue that the meaning even of detailed rules is inherently uncertain due to the inherent indeterminacy of language. Consequently, even though applying them to specific circumstances might superficially appear to be an objective, techno-rational exercise, there is scope for subjective reasoning by judges. This becomes most apparent where the judges' decisions seem to be surprising and contrary to the apparent meaning of the legislation or to decisions in previous, similar cases. In this section I therefore illustrate the scope for subjective reasoning through six cases in which the judges' reasoning has produced an apparently surprising decision.

In *Bourne v Norwich Crematorium (1967)* Justice Stamp held that a commercially operated crematorium could not claim industrial buildings tax allowances. The allowance, which was abolished in 2011, could be claimed in respect of a building in which goods were subjected to a process *(CAA 2001 s.274(1))*, but Lord Justice Stamp ruled that a corpse was not 'goods' and cremation was not a 'process'. The legislation does not define the words 'goods' or 'process', but case law has elaborated on this. The leading precedents are those cases in which allowances were denied because one or both of these tests were not deemed to have been satisfied. The term 'process' implies a substantial degree of uniformity and in *Vibroplant v Holland (1982)* the cleaning and repair of items was not deemed to be a process because each item was

assessed individually and the work done therefore varied considerably. In *Crusabridge Investments Ltd v Casings International Ltd (1966)* the act of simply making chalk marks on tyres to indicate defects was not a process, but in *Kilmarnock Equitable Co-operative Society v IRC (1966)* the repacking of coals was deemed to be a process. Using these definitions, the uniformity of the act of cremation would therefore appear to be a process. Two leading cases concerning the definition of goods are *Buckingham v Securitas Properties (1980)*, in which it was held that coins which were broken down into wage packets were not goods, and *Girobank plc v Clarke (1998)*, in which it was held that banking documents were not goods. Coins and banking documents appear to belong to a different category from corpses, which are raw materials converted into a different form in the manner of manufacturing in order to generate income and would therefore appear to be similar to industrial waste.

Given that the crematorium appeared to satisfy both tests it is interesting to examine why they did not win and possibly the most revealing part of the judgement is the preamble to Lord Justice Stamp's reasoning.

> I would say at once that my mind recoils as much from the description of the bodies of the dead as 'goods or materials' as it does from the idea that what is done in that crematorium can be described as 'the subjection of' the human corpse to 'a process'. (Bourne v Norwich Crematorium 1967:167)

Having made his instinctive revulsion clear, he dismissed the arguments that a corpse was 'goods' and that cremation was a 'process' by arguing that legislation cannot be interpreted by simply assigning individual words their normal English meaning. He did not, and did not need to, provide a robust argument why the words should not be so construed in order to reach his decision because the authority vested in him as a judge did not require him to do so. This is an example of the third dimension of power because a subjective interpretation, possibly because he instinctively could not stomach the inevitable conclusion of giving the words 'goods' and 'process' their normal meanings, is given the appearance of an objective, techno-rational interpretation of the law. This case may therefore illustrate Zander's (2004) argument that judges' decisions are often influenced by their subjective attitudes, rather than objective legal reasoning. Whilst this case illustrates the inherent subjectivity of legal interpretation, it would merely be a curiosity if it were simply an isolated instance, motivated purely by Lord Justice Stamp's personal sensibilities rather than any desire to favour a particular party. However, this subjectivity is illustrated by a number of other cases.

Taking Leave (of His Senses)

In *HM Revenue & Customs v Grace (2008),* Justice Lewison, for the first time in over a hundred years, overturned the decision of a Special Commissioner[2] on a question of residence for tax purposes. A decision on residence status is a

[2] Until they were replaced by First Tier and Upper Tribunals in 2009, the General Commissioners and Special Commissioners were the lowest court to which taxpayers could appeal tax cases. Most cases were heard by the General Commissioners, which consisted of laypersons assisted by a qualified clerk, but cases of a particularly technical nature, such as these, were heard by the Special Commissioners, who were tax experts.

finding of fact, rather than law, and Commissioners' decisions could only be overturned on a finding of fact if the findings are considered so bizarre that no reasonable person could have reached them from the evidence available. It follows that Justice Lewison could not overturn the decision simply because he disagreed with it.

The case involved a South African airline pilot who piloted long-haul flights between the UK, South Africa and elsewhere. He had owned a house near Gatwick airport since 1987, but in 1997 had acquired a second home in Cape Town. Since that time he had only spent brief periods in his UK house immediately before and after flights, and was not resident in the UK on the basis of a day count in accordance with HMRC guidance.

The judgement contains the following statement on the interpretation of the relevant section of the Income and Corporation Taxes Act 1988 (ICTA 1988) s.334 which states that a taxpayer will still be resident in the UK 'if he has left the UK for the purpose only of occasional residence abroad'. Justice Lewison considered that this section contained two tests: whether a taxpayer had 'left' the UK, and, if so, whether it was for the purpose of 'occasional residence'.

Of the first test he said 'it follows that if a person has not "left" the UK at all, s.334 will not apply to him' *(HM Revenue & Customs v Grace 2008)*. Truman (2008) observed that this point had not arisen in any previous cases that he was

aware of, but that the only reference could be found in an appendix to IR20[3] (HM Revenue & Customs 1999) which read 'where an individual has lived in the UK the question of whether he has left has to be decided first'. He believed that in this statement (which is contained in an explanatory document with no legal force), 'left' was a shorthand for 'left for more than occasional residence' (Truman 2008:542). Since the word is not in inverted commas, and the relevant section does not give the word a special meaning, he is of the view that the word is not 'a term of the art' and should be given its normal English meaning. He observed that the only debate surrounding when the taxpayer leaves the UK is whether this occurs when the plane takes off or when it leaves British airspace. By placing the word 'left' in quotation marks Justice Lewison therefore created a legal test out of a word which is clearly intended to carry its normal English meaning and Truman argues that the only legal test intended by legislators concerned the phrase 'occasional residence'. It was common ground that s.334 did not apply in this case and the remarks were *obiter dicta* (i.e. the remarks, although included in the opinion, did not form a necessary part of his decision), therefore Justice Lewison did not elaborate on what that test should be. However, the remarks once again illustrate the operation of the third dimension of power through the subjective interpretation of and reading of meaning into an English word whose meaning would appear to be uncontroversial.

[3] A leaflet published by HM Revenue & Customs which explained the law and practice concerning residence for the benefit of taxpayers. It was therefore written as far as possible in non-technical language.

Wartime Profit(eering)

If these cases could be dismissed as isolated ones, motivated by the foibles of a particular judge rather than any wider political motives, they would be curiosities of no great importance. However, other cases have had wider significance. Examples of these can be found in cases involving Excess Profits Duty (EPD). EPD was a tax imposed during World War I, initially at 50% and later at 80%, on any trading profits in excess of a pre-war profit standard, calculated as the average of any two of the three accounting periods immediately preceding the start of the war. The rationale for the tax was summed up by Lord Hanworth in *Birt, Potter & Hughes v CIR (1927)* thus:

> …[EPD] was designed, as we all know, to try to secure to the Revenue a portion of the profits being made in the course of the War which were said to be enhanced by the circumstances of the War and, being so enhanced, to be beyond the sum which the subject was entitled to keep free of taxation, inasmuch as he ought not to be entitled to make a larger profit due to the misfortune of the nation at large in being at war.

This statement indicates that it was generally felt that the taxpayer had not only a legal duty, but also a moral, patriotic duty to pay tax in order to help the war effort rather than profit from the ‘misfortune’ of the nation. It is interesting to consider whether decisions on EPD cases might have been influenced by this motive.

In *Hinshelwood (Thos.) & Co. Ltd v I.R. Commissioners (1920)* an agreement signed in 1913 provided that the managing directors, Mr Beattie and Mr Malone, should receive fixed salaries of approximately the same amount as they had previously received plus commission based on the company's profits. No commission was paid in the year ended 31 December 1913 due to low profits, but in the year ended 31 December 1916 Messrs Beattie and Malone each received commission of around £4,500 and in the year ended 31 December 1917 they each received around £5,000. The excess profits duty legislation gave the tax authorities wide discretion to disallow payments of salary in excess of the pre-war level, otherwise this would have been an obvious means of reducing the liability. The issue was whether these payments should be deductible for the purpose of EPD, given that they were payable under the terms of a pre-war agreement and that the only reason why similar amounts had not been paid in the year ended 31 December 1913 was because of the poor performance in that year and it is impossible to know now whether profitability would have improved to allow the salaries to be paid if it had not been for the war. If the salaries were not deductible the income tax paid by the directors would be refunded, but the rate of EPD payable on the additional profits would be greater, thereby enabling the Inland Revenue to maximize tax revenue.

Lord Justice Clerk's decision was marked by the use of less legalistic language than might be expected, stating that:

> The Inland Revenue Commissioners now say that they are entitled to issue an additional assessment in order to recover the amount of Excess Profits Duty which they failed to collect in respect of that omission to notice that there had been an increased payment to the managing directors in the two years under charge. In equity there would be no answer at all to that because the only result, except for a point I shall mention in a moment, would be that these payers of Excess Profits Duty would be allowed to *get off with* Excess Profits Duty on something like £10,000 or £11,000, which at 60%, would be a very large sum. (*emphasis added*).
> (Hinshelwood (Thos.) & Co. Ltd v I.R. Commissioners (1920):425)

That is, the judge said simply that the taxpayers should pay the tax because it would be simply inequitable (in his view) for them not to do so. This is despite the fact that the agreement cannot be considered as tax avoidance, since at the time it was drawn up the directors could not have known that World War I was about to start and that EPD would be imposed. Lord Justice Clerk did not elaborate further on the reasons why it would be inequitable for the directors to obtain the deduction. This case is therefore reminiscent of *Bourne v Norwich Crematorium (1967)* in that the judge was exercising the third dimension of power by presenting reasoning which can be summed up as ‘because I say so’ as an objective, techno-rational interpretation of legislation. However, in contrast to the crematorium case, there appears to have been a motive of

maximizing tax revenue and this is not the only case from this era in which this motivation is apparent, as the case of *Glenboig Union Fireclay v IRC (1921)* demonstrates.

This case is frequently quoted in technical books and manuals as being a leading case in establishing that compensation received in respect of the loss or sterilization of profit-making apparatus is a capital receipt and therefore not taxable as trading income. From this description it might be assumed that the case was won by the taxpayer, but this is not so.

The appellant company owned and mined beds of fireclay, over part of which ran a railway line owned by the Caledonian Railway. The railway company paid the appellant company compensation of £15,316 in the year ended 31 August 1913 in return for it agreeing not to work the beds of fireclay close to the railway. Glenboig treated the compensation as a trading receipt in their accounts and accounted for income tax on it. Later, under the EPD regime, the tax authorities successfully contended that it should have been treated as a capital receipt and the income tax paid was refunded. This curious situation can only be presumed to have arisen because, due to the high rates of EPD and the fact that the pre-war profits standard was used to determine the level of EPD payable over a number of years, it was in the interests of the tax authorities to reduce the profits of the pre-war accounting periods in order to maximize EPD assessments.

In order to reach their conclusion, the judges distinguished the facts from cases such as *Bwllfa & Merthyr Dare Steam Collieries (1891) Ltd v Pontypridd Waterworks Co. (1903)* and *Eden v North Eastern Railway Co. (1907)*, the material facts of both of which were identical to Glenboig Union Fireclay. These cases (which were admittedly not tax cases) held that compensation paid where a mining business is unable to exploit part of a mine or quarry should be calculated by reference to profits forgone. On that basis, the compensation should be treated as a trading receipt. Having cited these cases, the Lord Justice Clerk then stated that he did not accept that the compensation should be so treated in this case, but that the restriction on working certain areas of the beds of fireclay reduced the capital value of the beds and the compensation was received in respect of that diminution in value and the Lord President (Clyde) agreed with his colleague's arguments.

This case appears to support Zander's (2004) arguments concerning the alacrity with which judges will distinguish the indistinguishable. Not only did the judges distinguish the facts from the two precedent cases cited, but there have been a number of subsequent cases in which the facts have been distinguished from those of *Glenboig Union Fireclay*. For example, in *Waterloo Main Colliery Co. Ltd v IRC (1947)*, which was a case involving Excess Profits Tax (EPT), which was the World War II equivalent of EPD, compensation paid when part of the colliery's area was requisitioned by the Ministry of Works for opencast working was held to be a revenue receipt. The case was distinguished from *Glenboig* on the grounds that the portion of the asset had not been sterilized, but had been worked by the Ministry of Works, although the result for the

taxpayer was identical in both cases; they were unable to exploit that part of the asset and its value to them was thereby reduced. Furthermore, for the same reason as in *Hinshelwood (Thos.) & Co. Ltd v I.R. Commissioners*, the taxpayer in *Glenboig Union Fireclay* could not be accused of attempting to avoid EPD in 1913.

If it is difficult to reconcile the judges' reasoning in either *Glenboig* or *Hinshelwood* their context must be borne in mind. Both cases enabled the tax authorities to levy additional EPD. Given Lord Hanworth's statement of the rationale for the introduction of EPD it may well be that the cases were decided in a particular way because it was considered the taxpayers' patriotic duty to pay the tax and that it would be iniquitous to permit them to profit from war. Having decided on the desired outcome, it may be that legal reasoning tweaked the rules in order to achieve this, discarding inconvenient precedents and creating new distinguishing precedents. This is therefore again the exercise of the third dimension of power where a techno-rational, objective façade obscures the fact that those in power can make rules mean what they want them to mean.

Watered Down Law?

Whilst the previous two cases related to the years following World War I, the case of *North of Scotland Hydro-Electric Board v IRC (1961)* related to the years after World War II and concerned EPT. Once again, a decision which seems to go against the apparent meaning of the law might possibly be

explained by ulterior political motives. The *Finance Act 1946 s.37* permitted businesses a 'deferred repairs allowance' in relation to expenditure on the repair or renewal of fixed assets which, but for wartime conditions, would have been incurred in 1946 or earlier years. This allowance could reduce the profits liable to EPT in the year to which the cost of the repairs, in the opinion of the Commissioners, was attributable *ex post*. It was, however, a condition that the business was being run by the same persons in the year in which the expenditure was eventually incurred and the year to which it was attributable. This condition is logical because if the business had been sold in the intervening period the sale price would have been reduced due to the poor state of repair, thus reducing the profit on sale and tax payable. The North of Scotland Hydro-Electric Board was a statutory board set up on 1 April 1948 under the *Electricity Act 1947*, which nationalized the electricity companies. The tax authorities therefore contended that the Board did not qualify for this allowance, since it was the not the same person that was running the business in 1946 and earlier years.

Crump (1961) argued that the tax authority's contention was irrefutable, but that the judges constructed a statutory hypothesis to allow the taxpayer to win the case by construing the *Electricity Act 1947 s.14* (which nationalized the private electricity companies) as overriding the *Finance Act 1946 s.37*, even though there was no evidence that the legislation intended this. Crump notes that there were political reasons for finding in favour of the appellant company; if the tax authority's argument had been upheld, the result would have been that a nationalized industry would have had to pay a higher amount of EPT than

otherwise, which may have been an obstacle to further nationalization – a key aspect of post-war government policy. Members of the Conservative Party, the official Opposition in the 1940s, had suggested that nationalization could be frustrated by companies liable to be nationalized including a clause in any contract that any rights or liabilities under the contract should be cancelled on nationalization.

A Refreshing View of Tax Avoidance?

Similar cases can be found much more recently, albeit where the motive for the decisions has been very different. In the 85 or so years which had elapsed between *Hinshelwood v I.R. Commissioners (1920)* and these cases the nature of the state and its relationship with citizens had also fundamentally changed. This case was heard as the level of taxation was rising to fund increasing social provision, whereas by the time the recent cases were heard the UK had become a neoliberal state, one of whose functions is the transfer of resources to capital. These cases are *Five Oaks Ltd v HM Revenue & Customs (2006)*, heard in September 2006, *Limitgood Ltd v HM Revenue & Customs (2007)* and *Prizedome v HM Revenue & Customs (2007)*, heard in March 2007. The companies in the last two cases were part of the same group and the cases were heard together. Since the reasoning was similar in all three cases, only these latter two cases are discussed here.

Limitgood Ltd and *Prizedome Ltd* both concerned the use of capital loss ‘refresher’ schemes, which sought to circumvent the provisions of the Taxation of Chargeable Gains Act 1992 (TCGA 1992) Sch. 7A (as inserted by Finance

Act 1993 Sch. 8) restricting the use by companies of pre-entry losses[4]. Both cases were initially heard by the Special Commissioners. *Limitgood* was heard by John Avery Jones sitting alone and he found for the tax authority by interpreting the provision in a purposive[5] manner and the case was not appealed to the High Court. The latter case was again heard by Avery Jones, but on this occasion he was sitting with Theodore Wallace, who was the chair, and where two Special Commissioners disagreed the chair had the casting vote. Avery Jones again found for the tax authority, using a similar line of reasoning. However Wallace found for the taxpayer and, since as chair he had a casting vote, his view prevailed. The case was appealed to the High Court *(HM Revenue & Customs v Limitgood Ltd and Prizedome Ltd (2008))*, where it was heard by Justice Blackburne, who overturned the Special Commissioners' decision, again taking a purposive view of the provisions, albeit using a different line of reasoning from Avery Jones.

The company's scheme contravened the intention of TCGA 1992 Sch. 7A, but, perhaps surprisingly, the legislation could be read to allow it to succeed. The facts of the case were as follows:

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[4] TCGA 1992 Sch. 7A (inserted by FA 1993 s.88 and Sch. 8) sets out to prevent companies acquiring other companies in order to exploit either their realized or unrealized capital losses to shelter gains arising elsewhere in the group. If company A (a member of group X) acquires company B and B has at the date of acquisition an unrelieved capital loss of £1m, Sch 7A prevents a company in group X from transferring an asset pregnant with gain, acquired before the date that company B joined the group, into company B shortly before sale (which under TCGA 1992 s. 171 can be done without any tax consequences arising) and offsetting company B's loss of £1m against the gain arising on the sale of the asset. Where, at the date of acquisition, company B has an unrealized loss, i.e. holds an asset pregnant with loss, and that asset is subsequently sold at a loss, the loss must be time-apportioned between the pre-entry and post-entry portions and only the post-entry portion may be used to shelter gains arising elsewhere in the group.

[5] A purposive reading of statute interprets legislation in a manner which is consistent with its (presumed) intention. This contrasts with a strict legalistic interpretation which seeks to interpret legislation according to the meaning of the words used, even if it appears to contradict its intention.

1. On 26 September 2000 Limitgood Ltd and Prizedome Ltd each acquired half the share capital of Coalite Group Ltd, which was worthless, from their parent company, Anglo Ltd, for a consideration of £1. The shares had been transferred under TCGA 1992 s.171(1) and the deemed acquisition cost for each of the two companies was £243m.
2. On 27 September 2000 the shares in Limitgood Ltd and Prizegood Ltd were transferred from Anglo Ltd to Grantchester Ltd, a subsidiary of Grantchester Holdings, upon which transfer the losses on the shares in Coalite Ltd crystallized under TCGA 1992 s.179(3), the losses being restricted to £114m due to depreciatory dividends. The losses were pre-entry losses of Limitgood Ltd and Prizedome Ltd.
3. On 12 October 2000 other companies in the Grantchester Holdings group realized gains totalling £29m, which were deemed to arise to Limitgood Ltd under TCGA 1992 s.171A (under which an asset may be deemed to have been transferred to a company with available capital losses shortly before sale, even if no legal transfer is actually made).
4. On 19 December 2000 the share capital of Grantchester Holdings was acquired by Grantchester plc under a scheme of arrangement under the Companies Act 1985 s.425.
5. In the returns for the year ended 30 September 2001 Limitgood Ltd claimed to set off £29m of its loss of £113m against the gains of the other group companies and Prizedome Ltd claimed to set off £8m of its loss against gains of other companies which had been acquired by Grantchester plc on 19 December 2000 and which had been elected to Prizedome Ltd under TCGA 1992 s.171A. Similarly, in the returns for the

year ended 30 September 2002, the companies claimed to set off losses of £33m and £56m respectively against gains of other companies which had been acquired by Grantchester plc on 19 December 2000.

The case hinged on the interpretation of TCGA 1992 s.170(10) and, in particular, of TCGA 1992 Sch. 7A para. 1(6). S.170(10) reads:

> For the purposes of this section and sections 171 to 181, a group remains the same group so long as the same company remains the principal company of the group, and if at any time the principal company of a group becomes a member of another group, the first group and the other group shall be regarded as the same, and the question whether or not a company has ceased to be a member of a group shall be determined accordingly.

Sch. 7A para. 1(6) reads:

> Subject to so much of sub-paragraph (6) of paragraph 9 below as requires groups of companies to be treated as separate groups for the purpose of that paragraph, if:
>
> a) the principal company of a group of companies ('the first group') has at any time become a member of another group ('the second group'), *so that the two groups are treated as the same by virtue of subsection (10) or (10A) of section 170* (emphasis added) and;

b) the second group, together in pursuance of that subsection with the first group, is the relevant group [the group by reference to which the question of pre-entry losses is to be determined];

then, except where sub-paragraph (7) below applies, the members of the first group shall be treated for the purposes of this Schedule as having become members of the relevant group at that time, and not by virtue of that subsection at the times when they became members of the first group.

It was agreed by both sides that neither para. 1(7), nor para. 9(6) applied.

The case hinged on the interpretation of the italicized words in Sch. 7A para. 1(6)(a). Theodore Wallace, who ruled in favour of the taxpayer, interpreted them as referring to the combined group as a result of s.170(10) on the grounds that the reference to the combined group in para. 1(6)(b) would not otherwise make sense. The result of this is that when the Grantchester Holdings group joined the Grantchester plc group on 19 December, all the companies in the former group (including Limitgood Ltd and Prizedome Ltd) were to be treated as having become members of the Grantchester plc group on that date and the losses of £114m accordingly ceased to be pre-entry losses and were available for offset against the gains of other group companies.

This may seem to be an odd result and Avery Jones construed this paragraph to reach the opposite conclusion, an argument which was criticized by Murray (2007:138) as flying in the face of the statute. She accused him of setting up a

tension between a real world and the deemed world of TCGA 1992 s.170(10), where two groups are treated as being one and the same (*Limitgood Ltd v HM Revenue & Customs 2007:* para. 63). He stated that TCGA 1992 Sch. 7A para. 1(6)(a) starts in the real world by referring to the 'first group' and the 'second group', but that the paragraph then refers to the deemed world by stating that these two groups are treated the same. He reasoned from this that the second part of para. 1(6)(a), which deems companies to have joined the first group on the date of the merger with the second group, creates a contradiction, since, in the deemed world, the merger is a non-event (para. 64). Since the two groups are treated as the same, by stating in para. 1(6)(b) that 'if…the second group, together in pursuance of that subsection [s.170(10)] with the first group is the relevant group', the two groups must be considered together, the companies must be treated as having become members of the relevant group when they joined the first group. The losses of Limitgood Ltd and Prizedome Ltd therefore remained pre-entry losses after the merger with Grantchester plc.

Regardless of which judge was 'right', this disagreement clearly demonstrates both the capacity for detailed rules to be read in diametrically opposite ways and the difference between literal and purposive readings of statute. It was therefore no surprise that taxpayer appealed the case to the High Court, where Justice Blackburne's approach was different, but similarly purposive. He stated his position clearly at the outset of his conclusion (*HM Revenue & Customs v Limitgood Ltd and Prizedome Ltd 2008*:53) by citing Lord Nicholls in *Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes) (2004)*, that

> [t]he correct approach to statutory construction in the field of taxing statutes is...'first to decide, on a purposive construction, exactly what transaction will answer to the statutory description and, secondly, to decide whether the transaction in question does so'.
>
> (Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes) 2004:36)

Consequently, he stated that the purpose of the Schedule is clearly to restrict the use of pre-entry losses and to define the relationship of a company with such losses to the relevant group (para. 55). Since s.170(10) would allow losses realized by companies in the first group to be offset against gains realized by companies in the second group (para. 57), he construed para. 1(6) to mean that only losses incurred by Limitgood Ltd and Prizedome Ltd whilst they were members of the Grantchester Holdings group (there were none) would fall within para. 1(6). He reached this conclusion because, if para. 1(6) were to also apply to losses which were pre-entry losses to the Grantchester Holding group, he considered that the paragraph would add nothing to the Schedule; the paragraph was necessary because s.170(10) must be disapplied in order for losses incurred whilst the companies were members of the Grantchester Holdings group to be pre-entry losses of the Grantchester plc group. Since it would not be necessary to disapply s.170(10) in order to treat losses incurred by Limitgood Ltd and Prizedome Ltd as pre-entry losses, he considered that para. 1(6) does not apply to these losses (para .63). He concluded by saying that the above reasoning enables the purpose of the provision to be achieved.

This decision has been criticized by Murray (2008), who characterized the approach of Avery Jones and Justice Blackburne as

> step[ping] back from the statute, decid[ing] independently from the words of the statute what was Parliament's purpose, then ignor[ing] certain inconvenient words or add[ing] in others, to give effect to that presumed purpose.
> (Murray 2008:123)

Murray cites Lord Justice Peter Gibson in *Frankland v CIR (1997)*, who said that it was the function of the court to interpret the legislation and not to legislate in the guise of interpretation. Murray observed that no tax avoidance scheme will, by definition, accord with the purpose of the statute and, if statutes are interpreted purposively, the taxpayer would never win a case. Nevertheless, Justice Blackburne's decision has been upheld by Lord Mummery in the Court of Appeal in *Prizedome Ltd & Limitgood Ltd v The Commissioners of HM Revenue & Customs (2009)* and no appeal has been made to the Supreme Court, therefore this decision is now final. Lord Mummery upheld the decision on the grounds that the construction of the legislation argued by the taxpayers could not have been intended by Parliament and he could therefore only uphold such a construction if 'compelled to do so by the language of the statute' (Prizedome Ltd & Limitgood Ltd v The Commissioners of HM Revenue & Customs (2009):10), which he felt unable to do.

All of the cases analyzed in this section demonstrate that, even where law is drafted in the form of precise rules, judicial discretion exists due to the need to adjudicate the precise meaning of legislation in specific situations. This may be overt, but may also be covert due to the uncertainty inherent in language. This means that certainty in law, whilst intuitively appealing, is unattainable and the *post hoc* rationalization of judges' decisions merely produces an illusion of certainty which is the exercise of the third dimension of power through the construction of knowledge. One of the most important consequences of this illusion is that it enables the construction of a rationalizing discourse for tax avoidance which is based on the twin pillars of libertarianism and legal formalism and the following section discusses and critiques this discourse.

8.4. Tax Avoidance and the Construction of Certainty

In the previous two sections I have discussed the hidden discretion in rules-based legislation and the more overt discretion of principles-based legislation and in this and the following section I turn to one of the most important consequences of this discretion, which is its capacity to either facilitate or frustrate tax avoidance. Tax avoidance has been defined by many writers, but the definitions are nearly always very similar. For example, Prebble & Prebble (2010:696) define tax avoidance as '[c]ontriving transactions and structures that reduce tax in ways that are contrary to the policy or spirit of the legislation'. The definition contains two parts; first, a taxpayer must undertake transactions or create structures which have the result of reducing their tax liabilities and, second, these must comply with the strict letter of the law, but contravene its intention or spirit (James S. 2012). This contrasts with tax planning, where a

taxpayer takes advantage of a relief in a manner which the legislation intended, and tax evasion, where a taxpayer either makes false returns to the tax authorities, e.g. understating income by not recording ‘cash jobs’ which are not recorded in the accounts, or fails to disclose information which they are obliged to disclose, e.g. that they have started trading (James S. 2012).

Since there is no question of illegality, if a tax avoidance scheme fails but there has been full disclosure of the material facts, there are no civil or criminal sanctions and the only penalty suffered by the taxpayer is that they do not obtain a reduction in their tax liability. However, since this liability would have been payable if the scheme had not been attempted, this does not really represent a real loss to the taxpayer beyond the abortive professional fees expended. This therefore gives an advantage to taxpayers, whose potential gain might be significantly larger than their potential loss.

That a scheme has resulted in a lower tax liability due to its operation is an objective fact. Furthermore, a scheme will succeed either if a judge has concluded that it complies with the letter of the law or if HMRC decides not to challenge it, but it is more problematic whether it complies with the spirit of the legislation and it is contested whether compliance with the spirit of the legislation ought to be a consideration in determining whether a scheme succeeds or not. Taxation imposes a direct cost on a defined type of activity and there is therefore an incentive to devise a legal form of the activity which complies with the letter of the law, but achieves an economic purpose which did not occur to the legislator or which the legislator wished to prohibit (Picciotto

2015:170). Where taxpayers engage in tax avoidance they are therefore engaging in ‘creative compliance’ in order to escape legal control without violating legal rules (McBarnett 1991) or to create the appearance of being regulated, whilst avoiding its impact (McBarnett 1992). This is not simply a tax issue, but an ethical one based on a strict separation of law and morals, where law is treated as a set of formal, self-contained norms (Gribnau 2015:235).

The moral justification for tax avoidance derives from libertarianism and the legal doctrine of formalism. However, the normative argument that it is only necessary to comply with the letter of the law is a contested one and uncertainty and ambiguity are inherent in language. Consequently the objective, techno-rational nature of legal rules is an illusion and their literal meaning is in fact constructed through a discursive process which involves the exercise of the third dimension of power. Using these as a rationalizing discourse for tax avoidance is therefore not transparent and this is likely to be a more effective means of transferring resources to wealthier taxpayers and large corporation than tax simplification discussed in chapter 7.

Tax avoidance arises from the conflict between the power of a state to levy taxation according to democratically agreed principles and the libertarian view that taxpayers have an inalienable right to their pre-tax income, a position which derives from the principles of liberty, the right to be free from an overreaching state, the freedom of property and the freedom to contract (Barker 2009). According to this view, the state has no right to force individuals to surrender part of their income in the form of taxation even if it is imposed according to the

democratic will (Murphy & Nagel 2002), which is characterized as the 'tyranny of the majority' (Adams 2015 [1787]:291). Tax avoidance is therefore justified as an act of resistance against an overweening state (Barker 2009).

In practice libertarians accept that a minimal level of taxation must be levied to provide functions which cannot realistically be organized privately, such as the police and armed forces (Murphy & Nagel 2002) and therefore accept a narrower interpretation of the Lockean social contract in which members of a state freely contract to contribute to the cost of a minimal state which ensures their physical protection, but reject any attempt by the state to use taxation for the redistribution of wealth (Frecknall-Hughes 2007). However, they will only accept taxation as legitimate if its scope is certain (Barker 2009).

A legal justification for the doctrine of legal certainty is provided by Lord Oliver of Aylmerton (1996:174):

> Law is all about the rules which society imposes upon its members for the regulation of their conduct. Elementary fairness dictates that if rules are to be imposed in an area in which there is *no universal moral imperative to aid understanding*, they shall be clear and unequivocal, so that the subject may know with certainty what he or she may or may not do and what are the legal consequences of any projected course of action.
> (Emphasis added)

By stressing the need for certainty Lord Oliver is echoing one of Smith's (1776) four canons of taxation. However, when Smith wrote:

> [w]here it [the tax system] is otherwise, every person subject to the tax is put more or less in the power of the tax-gatherer, who can either aggravate the tax upon any obnoxious contributor, or extort, by the terror of such aggravation, some present or perquisite to himself.
> (Smith 2015 [1776] Book V 2:26)

he meant that a taxpayer's liability should be determined by a codified system of law rather than subject to the arbitrary whim of individual tax officials (Tribe 1981). Over the two centuries between Smith's and Lord Oliver's remarks tax law had developed substantially and the concept of certainty is now often asserted to mean that the application of codified law should be certain in any given situation (Weinrib 1988). Whilst it is perfectly natural for such doctrines to develop as law itself develops, the co-option of Smith to give authority to this can be seen as the operation of Lukes's (2005) third dimension of power.

The notion that the meaning of law can be certain is a doctrine known as legal formalism, which is defined as '[l]egal analysis involving the presentation of argument as though conclusions followed inexorably from indisputable premises' (Curzon 2002:247) and can be contrasted with legal realism. Realism regards the prospect of an objective, apolitical law as a chimera and recognizes that the law is inextricably bound up with morality and politics, since judging is

inherently discretionary and the exercise of discretion is inevitably influenced by political considerations and the biases of the judges (Chemerinsky 2001).

Formalism approaches law either as a science, in which a handful of permanent, unchanging and indispensable principles are imperfectly embodied in the legal code and judges must tease out the application of these to specific cases through legal reasoning, or as an exercise in inductive reasoning in which general legal principles are formulated *post hoc* from the decisions in specific cases (Posner 1993:15). Formalism holds that law contains an 'immanent rationality', so that its intelligibility does not therefore depend on anything extrinsic to it and its form is integral to this understanding (Weinrib 1988). The immutable principles upon which the law is based are sometimes assumed to derive from natural law where just solutions to social problems can be found in the facts of nature (Curzon 2002:244), such as may be found in primitive societies.

Libertarianism therefore asserts that the law *should* be certain whilst legal formalism argues that the law *can* be certain. These are intuitively attractive notions, since they give the impression that we are governed by laws rather than people (Chemerinsky 2001) and it is how the legal profession would like to see the law because it casts lawyers and judges in the role of seekers after an absolute truth in the manner of scientists (Weinrib 1988). However, both libertarianism and formalism are open to a number of criticisms. For example, in order to earn their pre-tax income, individuals must rely on the institutions and structures of a market economy which have been created by the state, such as

the legal and banking systems, and they should therefore contribute to the cost of these (Murphy & Nagel 2002).

Similarly, there is an assumption that the pre-tax distribution of income is presumptively just, whereas, in reality, if a taxpayer earns a high pre-tax income, this is not wholly attributable to their innate ability and industry, but may also rely on educational advantages which they have enjoyed courtesy of the state or sheer good fortune. For example, they may have had the benefit of state education or, even if they were wholly privately educated, most of their employees will almost certainly have had that benefit and the existence of a well-resourced private education system might undermine a state system by, for example, attracting the best teachers. The redistributive function of taxation is therefore based on the premise that those who have enjoyed such advantages and fortune should therefore assist those who have been less fortunate (Murphy & Nagel 2002). Libertarianism's prioritization of individual rights over the collective will is therefore profoundly undemocratic and tax avoidance is not a victimless activity. Even if no specific victim can be identified, since the harm is diffused, it results in other taxpayers having to pay more tax in order to make up the shortfall or governments being unable to fund services in accordance with their democratic mandate (Prebble & Prebble 2010).

Whilst the acceptance or rejection of libertarianism can be argued to depend on an individual's philosophical outlook, the problems with formalism are more fundamental. The assumption that the fundamental principles underlying the law are natural and immutable in the sense that they derive from natural law

(Posner 1993) is open to two criticisms. Firstly and more fundamentally, the existence of a natural law is problematic, because, even in a pre-legal society in which all members will nearly always be in no doubt about their social roles and how to act in given situations, the norms will be determined by fairly rigid customary or conventional practices which are clearly understood (Prebble & Prebble 2010:734). Even in these societies, law is therefore largely a product of social relations and conventions rather than deriving from fundamental and immutable principles.

Secondly, the application of fundamental rights and freedoms to specific situations is contestable in any branch of law, but is even more so in the area of tax. Tax cases often involve the interpretation of statute, which is enacted through an inherently political legislative process. Prebble (1997) describes income tax as ‘ectopic’ because income exists neither as a physical fact nor as an abstract thought, but must be defined by statute and is therefore even further removed from immutable principles. However, as I demonstrated in chapters 8.2. and 8.3, law is a product of societal relations and conventions, which is due to imprecision and ambiguities inherent in language. Certainty in the law is therefore unattainable because the meaning of language always has a social element and the meaning of law is therefore discursively framed through the interpretation of language (Picciotto 2015).

The formalist view that law has an immanent rationality therefore becomes problematic because this relies on the acceptance of underlying principles which are discursively framed. Law therefore becomes a discourse conducted

according to codified rules, which can be divorced from reality and resemble the fantasy wargaming world of *Dungeons and Dragons*, in which the rules are similarly logical and internally consistent, provided that the underlying premises of the game have been accepted. This comparison is brought to mind by Weinrib's (1988) argument that law constitutes its own ideal and that its immanent rationality allows it to be understood in and through itself. In this respect parallels can be drawn with neoclassical economics, in which the operation of the real world economy has been reduced to a set of abstract, self-referential models.

The pursuit of certainty demanded by formalism requires that taxation is drafted as a set of complex, specific rules and successful tax avoidance involves finding and exploiting ambiguities in these and large taxpayers are exercising the third dimension of power by lobbying through their barristers for certainty to be constructed in a manner which favours them. In attempting to combat such schemes, legislators reactively enact specific anti-avoidance legislation, spawning new complexity and ambiguity. This in turn is exploited by new avoidance schemes and such cycles could, in theory, continue indefinitely (James 2010). This game of cat and mouse disguises the fact that in a neoliberal state the position of the state is conflicted. The tax authority notionally defends the interests of the state and society in general, but as I discuss in chapter 5.2. a central aim of a neoliberal state is the transfer of resources to capital and tax avoidance is a means of achieving this.

Tax avoidance by large corporations such as Google, Starbucks and Amazon has become an extremely sensitive political issue (e.g. Neville & Treanor 2012; Barford & Holt 2013), as has the suspicion that the tax authority is favouring the interests of large corporations (e.g. Armitstead 2010; 2011) and these are discussed in more detail in chapter 9. There is a widely held view, in the UK and elsewhere, that tax avoidance has increased in recent year, which has created greater pressure on HMRC to police the boundaries effectively (Oats & Gracia 2012). This means that if the tax authority is to be complicit in tax avoidance by large corporations without arousing public ire it must be done covertly.

Furthermore it might appear to be contradictory to argue that the uncertainty inherent in detailed rules gives scope for tax avoidance when five of the six cases I analyzed in chapter 8.3. were won by the tax authority and therefore resulted in a transfer of resources from taxpayers to the state and the taxpayer in the remaining case was a nationalized industry. It is a fundamental principle of a democratic state that the judiciary is independent of the legislative and executive arms of the government. Judges such as Lord Blackburne and Lord Mummery cannot be prevented from interpreting legislation in a purposive manner in order to frustrate tax avoidance if they wish to do so and Robertson's (1998) observation that the outcome of cases can be predicted with a high degree of certainty simply by knowing which judges will hear the case suggests that it can be a matter of chance whether a tax avoidance scheme succeeds or fails.

In this section I have demonstrated that the illusory certainty of rules-based legislation has been exploited to justify tax avoidance by constructing a rationalizing discourse based on the legal doctrine of formalism and the libertarian view of taxation, which both contain major flaws. This discourse is therefore an exercise of Lukes's (2005) third dimension of power to justify transferring resources from the state to wealthy individuals and large corporations. However, as I have demonstrated in chapter 8.3., the interpretation of rules to favour these taxpayers is not inevitable. These taxpayers can again exercise of power through their ability to lobby judges and there have been many reported cases of alleged tax avoidance, but they are by no means guaranteed to succeed. This presents a neoliberal state with a dilemma, since it is simultaneously answerable to taxpayers and voters as a whole and a co-actor in the assemblage which includes large corporations and cannot therefore be seen to be complicit in the transfer of resources through allowing tax avoidance to succeed. Chapter 8.5. therefore addresses the question of whether and how principles-based legislation might allow them to resolve this dilemma.

8.5. Principles and Power

In chapter 8.3. I demonstrated that judges can, and do, interpret rules-based legislation subjectively and that this subjective discretion has been used in recent years in cases such as *Prizedome Ltd* and *Limitgood Ltd* to frustrate attempts at tax avoidance. However, concern about the scope for tax avoidance in a rules-based system remains and since 2010 public interest in this issue has

become much greater. It has been suggested by, for example John Braithwaite (2002), that an alternative approach to anti-avoidance legislation is needed to cut through the vicious circle created by tax avoidance schemes and specific anti-avoidance legislation and enable the state to resist tax avoidance. He advocates a shift away from specific rules to a more principles-based approach in which the legislation would be interpreted purposively. Such legislation would contain less detail and judges would be given a greater degree of discretion to interpret it in accordance with clearly stated principles. Braithwaite's call has been echoed in the UK by amongst others Avery Jones (1996) and Freedman (2004), who argue that this would create greater certainty for both citizens and the state and could be used for this purpose. However, I argue that principles-based legislation would not provide any greater degree of certainty and that the subjectivity, and therefore exercise of power, involved in the interpretation of principles would be more overt than that involved in the interpretation of rules. The UK evidence on this is limited, as nearly all statute law is rules-based and the UK currently has little principles-based tax legislation. However, it is important to consider, *a priori*, whether it is likely to achieve this purpose and whether it might be used in ways which its supporters would not welcome.

An example in the UK of both the uncertainty inherent in principles-based legislation and the fact that judicial discretion can result in unpopular decisions is the *Human Rights Act 1998*, which enshrines the *European Convention on Human Rights* of 1950 into UK law. While the principles as stated in the Act, such as the right to family life, may be uncontroversial, they lack guidance on how they might be implemented in various situations. It is therefore left to the

judge to establish the specific line of reasoning for the decision in each particular case and it is these interpretations which cause controversy. There is no requirement that subsequent cases follow the same line of reasoning, particularly since it will usually be possible to differentiate the facts of each case which could be used to justify reaching a different decision, if that is considered desirable or expedient.

Whilst the discretion in interpreting rules can be disguised as techno-rational decisions, the discretion inherent in the interpretation of principles is more overt and is an example of Lukes's (2005) first dimension of power. This discretion will be of particular importance where two or more principles conflict and a judge must decide which principle should be prioritized. Such a conflict arose in *Mosley v News Group Newspapers Ltd (2008)* (e.g. The Lawyer 2008 and Gibb 2008), in which the judge, Justice Eady, awarded substantial libel damages to Max Mosley for stories concerning his private life printed in the *News of the World* newspaper. Justice Eady was widely criticized for using the Human Rights Act 1998 to create a privacy law through judicial ruling. Whilst in this case the conflict was between the interests of Max Mosley and the press, in other cases, such as taxation it may be between the interests of individual citizens and the state, which is acting on behalf of society as a whole.

The judgement turned on a conflict between *article 8* of the *European Convention on Human Rights* (as incorporated into the *Human Rights Act 1998 Sch. 2*) which guarantees the right to private and family life and *article 10*, which guarantees the right to free expression. Conflict therefore arose since, in

exercising its right to freedom of expression, Max Mosley felt that the *News of the World* had infringed his right to privacy. Similarly, by successfully asserting his right to privacy, the *News of the World* may feel that their right to free expression has been infringed. The fact that the way in which this, and other, conflicts may be resolved is subjective is demonstrated by *The Lawyer (2008)*, which summarized the views of various eminent judges on this case. It considered that the decision in this indicated that Mr Justice Eady and Mr Justice Blackburne were strongly inclined to prioritize the individual's right of privacy, whereas Mr Justice Tugendhat was strongly inclined to favour the right of the press to free expression, as illustrated by his decision to allow the press to report details of the personal life of the Chelsea footballer and then England captain John Terry (Jones 2010), while Mr Justice Lindsay sat in the middle of this spectrum. It is, therefore, quite possible that the case Max Mosley's case would have been decided differently if it had been heard by, for example, Mr Justice Tugendhat. This recalls Robertson's (1998) argument that, even with rules-based legislation, it was possible to predict the outcome of cases with a high degree of certainty simply by knowing which judges were hearing the case. There are therefore likely to be cases where the judges' interpretation of the Act proves to be unpopular and this has led to the Conservative government elected in May 2015 to make a commitment to repeal the Act and break the link with the European Convention on Human Rights.

If a principles-based approach were adopted in tax legislation, and in particular in the area of anti-avoidance legislation the UK tax authorities and courts would be asked to consider whether a scheme was 'artificial' or 'abusive' using

principles. Previously, tax avoidance was simply distinguished from tax evasion, the former being legal and the latter involving deception and dishonesty and, therefore, being illegal (James S. 2012). The distinction has become blurred in recent years and the tax authorities have taken a more aggressive stance against tax avoidance. For example, Simon James (2012) defines the term 'avoision' as behaviour designed to reduce tax payments in areas where the law is unclear, which indicates that the distinction between avoidance and evasion need not always be clear. Relating this definition to the above terms, an 'artificial' scheme might involve transactions which generate a tax loss, but where no commercial loss has been suffered, and an 'abusive' scheme would comply with the letter of the law, but not with its spirit. The origins of this more aggressive approach can be seen in *W.T. Ramsey Ltd v IRC (1981)*, in which a scheme to shelter a capital gain was held to be ineffective, even though none of the individual steps could be considered a sham, because the taxpayer's financial position was essentially unchanged at the end of the scheme and the only purpose of the scheme was tax avoidance. This test was developed further in *Furniss v Dawson (1984)* in which the judge applied a 'blue-pencil' test, i.e. if pre-ordained steps were inserted into a scheme purely for tax reasons they could be ignored. The scope of this doctrine was limited by later cases such as *Craven v White (1988)*, but the readiness of the judiciary to go beyond strict black-letter law in striking down tax avoidance schemes remains.

One of the most powerful tools which tax authorities can be given to counteract tax avoidance is a General Anti-avoidance Rule (GAAR), which gives HMRC wide discretion to disallow tax avoidance schemes based on a number of broad

principles without giving specific technical reasons. A GAAR was introduced in the UK in 2013 (Finance Act 2013 ss.206-215) and it is too early to assess its impact here, but a similar rule has existed for a number of years in Australia and their experience can provide evidence of how practice might develop in the UK.

In Australia a GAAR was introduced in 1981 to 'toughen' Income Tax Act 1936 Part IVA and this approach has been supported by the judiciary. However, Evans (2008) argued that, whilst the Australian government was satisfied with the way that the GAAR has operated, there had been a cost. Despite the large number of adjudicated cases, a large number of issues remain unresolved and there was no greater certainty about whether the GAAR would apply in a particular case. Cashmere (2006) (cited in Evans 2008:40) echoed Murray (2008) when he argued that Part IVA:

> is drafted so widely as to be capable of enabling the Commissioner of Taxation to annihilate any transaction which provides a tax advantage…..[w]hile certainty relating to the application of legal principles (including tax principles) cannot be assumed, it is important that there be certainty relating to the principles which are to be applied. The High Court has yet to provide that certainty in relation to the interpretation of Part IVA

Pickup (2008) argues that this lack of certainty means that there is serious concern that legitimate business and personal transactions are being 'wrongly' caught by the rule and speculates that the courts may, in time, start to favour

the taxpayer to a greater extent. Furthermore taxpayers might not consider it worthwhile devising avoidance schemes, given the ease with which they could be struck down. In this respect, the power of principles-based legislation may be greatest if it is not invoked, but simply left as a bogeyman to scare taxpayers. Taxpayers would thereby be using the Foucauldian concept of 'techniques of the self', whereby they exercise self-discipline and regulate their own behaviour, without the need for overt state coercion and a shift to principles-based legislation would therefore be one of the techniques and structures of governmentality whereby taxpayers regulate their conduct in accordance with the wishes of the government (Tuck 2013).

The fact that the GAAR has not delivered greater certainty and may be used in ways which taxpayers find unwelcome is demonstrated by a comparison of two Australian cases, *Federal Commissioner of Taxation v Spotless Services Ltd (1996)* and *Commissioner of Taxation v Futuris Corporation Ltd (2012)*, both of which hinged on the interpretation of the 'dominant purpose' rule. In *Spotless Services* the taxpayer, a corporation tax-resident in Australia, invested A$40m as a short-term investment in the Cook Islands, the interest from which was tax-free in Australia. The rate of interest offered in the Cook Islands was lower than that which the taxpayer could have obtained if the funds had been invested in Australia and the only factor which made the arrangement commercially attractive was the fact that the receipt would be tax-free. The Federal Court found that, if the opportunity to invest the funds offshore had not been available, Spotless would have invested the funds in Australia and received income which was assessable there. This was a quite straightforward transaction and the

taxpayer relied on the Income Tax Act 1936 s.23(q) for the tax exemption. Nevertheless, this was sufficient for the court to conclude that the 'dominant purpose' of the arrangement was obtaining a tax benefit, which was sufficient for it to rule that it could be assessed under Part IVA (D'Ascenzo 1998).

In contrast, in *Futuris* the taxpayer devised a scheme which permitted the tax-free disposal of a subsidiary. This scheme was considerably more complex than the arrangement in Spotless and it might therefore superficially appear more likely that court would rule that it, too, could be assessed under Part IVA. However, this case was decided in favour of the taxpayer on the grounds that they would not have made the disposal at all if the gain were taxable and that obtaining a tax benefit was not therefore the 'dominant purpose' of the scheme *(Commissioner of Taxation v Futuris Corporation Ltd (2012))*. In response to this decision the Australian Tax Office proposed to change the law retrospectively from 1 March 2012, which Thompson (2012) has criticized. He argues that Part IVA is now being applied to arrangement which might be seen as normal commercial dealings, rather than just those which normal understanding might characterize as 'artificial or contrived' arrangements, 'paper' tax schemes or marketed arrangements (Thompson 2012:4). This shift might provide the certainty which Cashmere (2006) and Evans (2008) were seeking, but his fears concerning the consequences of this shift are explicitly stated in his title, which is *Part IVA: Shifting the Goal Posts – Will You Have to Take the Highest Taxed Alternative?*

This highlights the problem that the interpretation of a GAAR involves the exercise of discretion, which is the exercise of the first dimension of power. This is an overt exercise of power and its transparent nature might lead to the same problem as the tax simplification proposals discussed in chapter 6 encountered. Acceptance of this discretion depends either on it assuming a hegemonic status, so that its existence seems totally natural and inevitable, or a belief that it will only be used to target schemes of which an individual disapproves. However, the case of *Jones v Garnett (2007) UKHL35* (generally known as the Arctic Systems case after the name of the company used by the taxpayer, Mr Jones) might possibly be seen as a warning of how a GAAR could be used in ways taxpayers find unwelcome.

In this case the tax authorities sought to re-allocate dividends paid to Mrs Jones by the company to Mr Jones on the grounds that Mrs Jones's contribution to the company would only have justified a small salary and that this was a means of enabling her to utilize her personal allowance and basic rate band. The tax authorities won all the way up to the Court of Appeal, but the decision was overturned in favour of the taxpayer in the House of Lords. The tax authorities' stance had attracted much adverse comment in the professional press (for example Truman 2007b) and was criticized by Gracia and Oats (2012) on the grounds that these arrangements were not tax avoidance, but merely sensible tax-planning by ordinary taxpayers. The taxpayers eventually prevailed because the Law Lords held that the tax authorities had misinterpreted the law. Often taxpayers are unable to resist due to the cost of fighting the case, but in this instance their costs were paid by the Professional Contractors' Association, who

were concerned about the possible effect of this case on their members, if the tax authorities had won. The ability to fund a lengthy court battle with HMRC is an important factor which determines the relative power of HMRC and the taxpayer, with large taxpayers having significantly more power than smaller taxpayers. They might therefore view this extension of the powers of HMRC as a welcome attempt to 'level the playing field', but might also change their mind if HMRC attempted to strike down a scheme which they regard as 'plain vanilla' tax planning.

Concern about uncertainty in the application of the GAAR in Australia contrasts with the 'judicial castration' (Pickup 2008:27) of the Australian GAAR's predecessor, Income Tax Act (1936) s.260, whereby this section was contested in a succession of judicial cases and reduced to a set of rules which taxpayers and their advisers could navigate. The Australian experience therefore indicates that a GAAR will be largely ineffective if it is interpreted narrowly and its scope and application are certain, but create disquiet if it is interpreted broadly and its scope and application are uncertain. The response of the Australian government to the *Futuris* case suggests that it has opted for the latter alternative, which enables the government to prevent resources from being transferred to capital.

In Australia the power to interpret the GAAR has largely been wielded by the judiciary (and large taxpayers through lobbying the courts through their lawyers) and the government has been therefore been unable to directly influence their decisions. The UK GAAR (termed in FA 2013 the General Anti-Abuse Rule)

was introduced too recently for its scope and application to have been tested through the courts, but already there is evidence of an even more insidious exercise of the third dimension of power through extra-legal guidance. This might provide certainty and allay concerns that it might be used in unwelcome way, but it is not subject to the same scrutiny as parliamentary legislation and judicial decisions and may therefore be more vulnerable to lobbying by large corporations and their advisers.

The legislation defines terms such as ‘tax arrangements’ and ‘abusive’ (FA 2013 s.207), but does so by referring to phrases such as ‘accord with established practice’ (FA 2013 s.207(5)) which themselves require clarification. In order to provide greater certainty and protection for taxpayers HMRC have issued guidance on the application of the GAAR. These terms are to be interpreted according to a ‘double reasonableness test’, which requires HMRC to demonstrate that the arrangements ‘cannot reasonably be regarded as a reasonable course of action’ (HMRC 2015:B12.1). In determining whether this test has been met a court is empowered to

> take into account any relevant material as to the purpose of the legislation that it is suggested the taxpayer has abused, or as to the sort of transactions which had become established practice at the time when the arrangements were entered into
> (HMRC 2015:B12.1)

and

> requir[e] HMRC to obtain the opinion of an independent advisory panel as to whether an arrangement constituted a reasonable course of action, before proceeding to apply the GAAR. (HMRC 2015:B12.1)

Terms such as ‘relevant material’ and ‘established practice’ are highly subjective and large corporations and their advisers might be expected to lobby assiduously to ensure that material which supports their particular favoured schemes is ‘relevant’ and that they are ‘established practice’. Any judge who personally disagrees with their position might therefore find themselves hamstrung. This is therefore the exercise of the third dimension of power by mobilizing support by presenting the rule as a solution to an issue of public concern and the advice as for the protection of taxpayers, whilst attempting to ensure that the reality falls far short of what the public might wish for.

In this section I have argued that a move to a principles-based system might not give taxpayers any greater certainty than under a rules-based system and that it might come as an unwelcome surprise to taxpayers to find that the overt discretion inherent in a principles-based system will not always be exercised for their benefit. In the realm of tax, such principles-based legislation might be construed as only attacking tax abusers and therefore be of popular appeal. However, judicial discretion might either construe these principles narrowly, thus largely negating their effect, or broadly, giving rise to concerns that its application is uncertain. In order to forestall the latter concern governments might issue extra-legal advice, but this is susceptible to lobbying by large

taxpayers and might be the exercise of the third dimension of power to covertly favour their interests whilst mobilizing support by having the appearance of protecting taxpayers.

8.6. Summary

In this chapter I have argued that uncertainty is inherent in both rules-based and principles-based methods of drafting tax legislation due to the uncertainty inherent in language and that both can be used as a vehicle for the exercise of power. The ostensibly techno-rational nature of rules therefore obscures the power conferred on judges through judicial discretion, because it erroneously assumes that the judicial decisions arising from the adjudication of uncertainty represents the pronouncement of an objective truth. An analysis of cases demonstrates that judicial discretion has at times been used to reach a decision which appears to be contrary to the meaning of the legislation. There has been much debate surrounding how the exploitation of uncertainty for the purposes of tax avoidance can be reduced or eliminated and the characterization of tax avoidance as arising from bad drafting of rules-based legislation is the exercise of the third dimension of power because it mis-states the problem by insisting that tax can only be charged by reference to law which is certain, whereas certainty is unattainable. The inherent uncertainty can thereby be exploited by large corporations and wealthy individuals lobbying for discretion to be applied in a manner which benefits them, whilst denying the existence of this discretion.

Uncertainty is more apparent in principles-based legislation since principles only provide guidance which must be applied to specific situations. Whilst discussions of uncertainty have emphasized that uncertainty in the meaning of rules is exploited by taxpayers to avoid tax, the belief that this could be eliminated or reduced by adopting a principles-based approach to the drafting of tax legislation may well be misplaced. Since principles may conflict with each other, the subjectivity and discretion inherent in principles-based legislation is more overt. In order to mobilize support for a change, power must be exercised by convincing taxpayers that discretion will always be exercised in ways that they approve of. For example, if this shift is portrayed as being necessary to combat tax avoidance, it might appear to be superficially attractive to the majority of taxpayers and garner their support.

However, there is no guarantee that these powers will not be used in a manner which adversely affects them. Principles-based legislation may therefore be effective in counteracting tax avoidance, but this might come at a price which taxpayers are not prepared to pay if they were aware of this at the time the change was made. Alternatively, judicial decisions might allow the principles to effectively evolve into a set of rules, with the result that they are no more effective in countering avoidance than rules-based legislation or official extra-legal guidance might ensure that the legislation is interpreted narrowly, thus presenting the illusion to the public of tough action being taken. However, this might suit the government and represent the exercise of the third dimension of power by providing a means of resolving the tension between it being both part

of the assemblage of power in a neoliberal state and answerable to the public and this is one of the themes to which I return in chapter 9.

CHAPTER 9: THE SHOOTS OF RESISTANCE

9.1. Introduction

In chapter 7 I demonstrated using the debate on tax simplification as an example that the second dimension of power is inadequate to enable an ideology to assume a hegemonic position because its consequences are transparent and those who feel disadvantaged by proposed reforms are able to resist. In chapter 8 I demonstrated through the debate on whether tax law should be based on detailed rules or more general principles how the third dimension of power might be deployed for this purpose by constructing a discourse around the need for certainty, when this is unattainable due to the uncertainty inherent in language. The subjectivity inherent in interpretation can therefore be used to favour hegemonic groups, whilst the operation of power is obscured behind a techno-rational façade.

In this chapter I argue that the neoliberal paradigm of taxation has assumed a hegemonic position and that the power which has enabled it to do so has been exercised through a combination of economics and ideology. Its dominance might appear to be complete, but Lukes (2005) recognizes that power can never be absolute. In this chapter I explore whether it is possible, or feasible, to overturn a hegemonic paradigm through grass-roots resistance and how this might be achieved.

In this chapter I use the application by the pressure group UK Uncut for a judicial review of an agreement between HMRC and the American investment

bank Goldman Sachs under which HMRC forgave £10m interest due on the late payment of tax as a case study to demonstrate how the normally hidden workings of power may be exposed and how this might form the basis of concerted resistance to overturn the neoliberal paradigm of taxation.

In chapter 9.2. I discuss the three ways in which power is exercised to ensure the hegemony of the neoliberal paradigm and how it might be possible to resist despite its power being ostensibly complete. In chapter 9.3. I illustrate these arguments by analyzing the judicial review which Mr Justice Nicol conducted in May 2013 into the agreement between HMRC and Goldman Sachs, drawing on an earlier attempt by the Federation of Small Businesses and the Self-employed (FSB) to petition for a judicial review into an agreement between the Inland Revenue (the tax authority responsible for direct taxation prior to the formation of HMRC in 2005) and the Fleet Street print unions in the early 1980s as a comparison. This is followed by a summary in chapter 9.4.

9.2. Discretion, Accountability and Power

In this thesis I argue that powerful actors in a neoliberal state have a ‘triple lock’ on power in the area of tax policy. In chapter 6 I demonstrated that tax policy favouring the interests of capital was justified on economic grounds, so that low rates of taxes (or a ‘competitive’ tax regime) are necessary in order to encourage corporations to invest in the UK and thus bring economic benefits through the creation of jobs. Corporations are therefore considered to contribute to tax revenue through the payment of PAYE and national insurance on wages and salaries and VAT on sales. However, the validity of this argument depends

on the economic incidence of the various taxes and whilst PAYE, national insurance and VAT are borne by labour and consumers, the incidence of corporation tax is more controversial and empirical evidence suggests that it is borne mainly by corporations (Kleinbard 2014). This attempt to shift the burden of taxation onto labour and consumers is the exercise of power. This can be regarded as the first dimension of power where this line of argument is pursued through threats by corporations to leave the UK if their demands are not acceded to (e.g. Ahmed & Quinn 2011), but as the third dimension of power if individuals can be persuaded to 'buy into' this ideology and internalize it so that simply becomes received wisdom.

The second source of power is ideological. In chapter 3.4. I demonstrated that contemporary, hegemonic understanding of taxation is a set of ideological constructs deriving from neoclassical economics. Furthermore, in chapter 8 I demonstrated that interpreting tax law is not simply a techno-rational exercise in uncovering an objective truth enshrined in legislation, but that this simply obscures subjective interpretation underpinned by normative principles. This is the exercise of the third dimension of power since if tax law is interpreted in a manner which benefits corporations and other powerful taxpayers this can be presented as inevitable due to the ostensibly techno-rational nature of tax law. This ideological power can be used to restrict debate on tax policy, since if tax is assumed to be merely a techno-rational exercise, discussion should be restricted to professionals who understand the subject and exclude the 'ill-informed' majority (Bradley 2015:218). Since the meaning of tax law is inherently indeterminate because the meaning of language is determined by its

social context (Picciotto 2015) this means that decisions and discussions on its meaning may reflect the shared training and largely shared social and educational background of a relatively small circle of individuals. However, if it is recognized that taxation necessarily embodies normative principles, the debate on what these should be might involve a wider cross-section of the population (Bradley 2015).

The third source of power is administrative and is founded on the twin pillars of the discretionary powers of HMRC and the right of a taxpayer to confidentiality in their tax affairs. Because it is not always practicable or expedient to make highly scripted decisions, the civil servants who administer taxes must be able to exercise a significant measure of administrative discretion. Thus HMRC has general discretionary powers to do anything 'necessary and expedient in connection with the exercise of their functions or incidental and conducive to exercise of their functions' *(Commissioners of Revenue & Customs Act (CRCA) 2005 s.9(1))*. HMRC's exercise of discretion is generally circumscribed by the supremacy of Parliament and the rule of law and, more specifically, Article 4 of the Bill of Rights Act (1689), the treaties of the European Union, the Human Rights Act (1998), the HMRC Taxpayers' Charter and case law.

Freedman and Vella (2011) identify several categories of limitations on the discretion which HMRC may exercise. The first category is the non-application of the law when its interpretation is generally agreed. The second category is in the interpretation of the law where this is not agreed. The third category is discretion in the management of legislation and litigation and the fourth category

covers hybrids of the previous three. The first category may be subdivided into cases where HMRC interprets the law in a manner which goes beyond what Parliament clearly intended, and cases where HMRC simply disregards a certain provision. An example of the former is *R v Commissioner (ex parte Wilkinson) (2005)* where on judicial review the courts ruled that HMRC did not have the discretion to grant Mr Wilkinson's claim for a widow's bereavement allowance because the word 'widow' clearly excluded widowers; the choice of gender-specific nomenclature made clear parliament's intention and HMRC had no authority to extend this. It should be noted that the various safeguards against misuse are principles-based and therefore open to judicial interpretation (James 2010).

This pragmatic approach to the administration of taxes is clearly commonsensical, but it creates a tension with the expectation of fairness and equity between taxpayers, which suggests that tax rules should be absolute and applied ubiquitously, so that taxpayers are neither treated more harshly than the law stipulates nor are able to preferentially obtain more generous treatment than the law and associated rules (such as the UK's Extra-statutory Concessions) require. Whilst the detailed rules and procedures which underpin taxation are the operation of Lukes's (2005) second dimension of power, flexibility is still required to cater for situations not adequately covered by these. However, this flexibility becomes the exercise of the third dimension of power, if it conceals systemic bias towards particular groups of taxpayers whilst maintaining the impression of operating in a generally even-handed manner, with any favourable or unfavourable decisions being random.

Administrative discretion therefore becomes problematic in a neoliberal state where the relationship between HMRC and powerful taxpayers is fundamentally different from the relationship in earlier state forms. Whilst the financial resources of these taxpayers have always given them a degree of power through their ability to pursue a case through the courts, in a neoliberal state they have become co-actors in the assemblage of power and the relationship has therefore become more one of equals than of a governing body and the governed. This has also gone hand-in-hand with reforms to make public services user-led, rather than led by the producer or bureaucracy (Tuck 2013).

The concept of the taxpayer as customer raises concerns in the field of tax administration, since they do not have a choice as to the amount of tax paid or to whom they pay it (Tuck et al. 2011). Administrative discretion is predicated on the fact that there is an objectively correct amount of tax payable in any situation and it is simply a matter of how that amount can be collected most conveniently. However, it should not be a process of negotiation in which the taxpayer can influence the amount payable (de Cogan 2015:252). As I have demonstrated in chapter 8 this view of tax law is based on a false premise since there exists inherent subjective interpretation in the determination of a tax liability (Tuck 2010) and this creates the opportunity for powerful actors in an assemblage to exercise power and influence over HMRC.

This equalization of power between certain taxpayers and HMRC has led to the development of responsive regulation, where tax officials can switch between a traditional ‘tough’ method of ensuring compliance and punishing recalcitrant

taxpayers and a more cooperative approach or even delegation of responsibility to the private sector with the approach chosen depending on factors such as industry structure and behaviour. However, the tough enforcement approach should always be held in reserve if the more cooperative approach fails (de Cogan 2015:253). In practice there are concerns that powerful taxpayers might exploit the fact that what constitutes compliance is often subjective in order to 'game' responsive regulation by adopting a stance which, whilst very favourable to them, is very difficult to definitively argue is incorrect and making the judgement that HMRC are unlikely to adopt the tough approach in practice (de Cogan 2015:253).

Problems might therefore arise where the exercise of discretion is, or is perceived to, unfairly advantage one taxpayer over others due to the shift in power relationships. This might result in a breakdown in trust in the equity of the tax system; such distrust might be particularly serious because the tax system constitutes a critical nexus between citizens and the state (Boden et al. 2010; Freedman and Vella 2011). Diminished trust can lead to significant problems of non-compliance, public disorder, civil disobedience or even revolution. Examples of the consequences of mistrust include the grievances of the barons which led to the signing of Magna Carta (Frecknall-Hughes & Oats 2007), the American and French Revolutions and the Poll Tax riots of 1990 which led to the resignation of Margaret Thatcher as Prime Minister (Seldon & Collings 2000).

Freedman and Vella (2011) admit that the balance between efficient administration of the tax system and respect for taxpayers' rights is a difficult one and there might be occasions where the fuzzy line between acceptable administrative discretion and unfairly lenient treatment is crossed. Officials might exercise their discretion inappropriately if they are, exceptionally, corrupt or incompetent. But a more pernicious and systemic problem arises if the tax system falls prey to regulatory capture. This occurs where certain interest groups come to dominate the policy-making apparatus and culture, constructing legal and administrative systems and practices to serve their own interests (Levine & Forrence 1990). Preferential treatment arising from the exercise of administrative discretion might therefore be contentious if it appears to be systemic and the result of the exercise of undue influence or power (de Cogan 2011), which might arise in a neoliberal state where the taxpayer is part of the same assemblage as HMRC.

However, concern over the use (or perceived misuse) of administrative discretion can be exacerbated by the fact that it can be very rare indeed for specific instances of the exercise of administrative discretion (outside of the use of Extra-statutory Concessions) to enter the public domain. This is because the CRCA 2005 s.18(1) imposes a statutory duty of taxpayer confidentiality on HMRC, which effectively prevents decisions involving administrative discretion from being made public. Thus the third-dimensional aspects of power – for instance where a corporation uses its influence to shape the nature of the tax regime to its interests – remain hidden by virtue of the law.

This ‘triple lock’ on power might therefore appear to be complete because influential actors in the assemblage of power control both the economic and ideological discourse, are potentially able to enjoy more favourable discretionary treatment from HMRC and the principle of taxpayer confidentiality should ensure that this does not become public knowledge. This therefore makes resistance to the use or abuse of power problematic, but Lukes (2005) counsels us that power can never be absolute. The Achilles heel of this ostensibly hermetically sealed system of power is that, as I have argued in chapter 8, governments and their agencies such as HMRC are conflicted. Whilst in a neoliberal state both they and large corporations form part of the assemblage of power, one of whose principal aims is to facilitate the operation of capital, MPs must stand for re-election at least every five years. Governments are therefore answerable to the electorate as a whole and must heed, or least appear to heed, its wishes. For example, I argued in chapter 8 that the enactment of a GAAR in 2013 is a result of this conflict, but the interests of capital might still be favoured by ensuring that it is interpreted in a manner which only disallows a few of the most egregious schemes.

Furthermore, however sealed the operation of power might appear to be Lukes (2005) also counsels us that there will always be critical incidents, such as the controversy surrounding the abolition of the 10p tax rate in 2008 discussed in chapter 6.5., which lay bare the normally hidden operation of power and the resistance of MPs and the public forced concessions from the government. This critical incident arose from a miscalculation by the government about its ability to enact legislation which increased the tax burden on poorer taxpayers as a

class, but the principle of taxpayer confidentiality makes it more problematic to identify examples of the misuse of administrative discretion, which remains hidden by virtue of the law. It might therefore be necessary to rely on accidental releases of information, whistleblowers or investigative journalists such as Brooks (2010), although press reports in general should be treated with caution since they are rarely nuanced and cannot always be assumed to be even accurate.

Where the use of administrative discretion does become public, it affords the opportunity for others to challenge the power exercised. Challenges can take two routes – the democratic and the legal. Democratic challenges have become an important feature of UK public debate since 2010. The Parliamentary Accounts Committee (PAC) has taken advantage of a series of whistleblowers to publicly call a number of corporations and the HMRC to account for the nature of the discretionary relations between them (House of Commons 2011). Whilst this has raised the level of public interest and debate, it should be noted that Parliament has no ability to intervene directly in the administration of taxes and its power lies purely in fuelling public debate – effectively naming and shaming – although the announcement by Starbucks that it would ‘volunteer’ to pay £20m of corporation tax (Neville & Treanor 2012) demonstrates that this can have an effect.

UK taxpayers may challenge the use of administrative discretion, thereby holding them to account for the way in which flexibility is used, through HMRC’s internal procedures, complaints to either the Adjudicator or the Parliamentary

and Health Service Ombudsman and, finally, through a judicial review (Freedman and Vella 2011).

One reason for using the legal process is that a successful challenge might force a government to change the law or the practices of government, but its significance can be far wider, since it can expose the operation of power. Lukes (2005) provides an appropriate lens with which to analyze how power might operate in such circumstances. Using the concept of the first dimension of power, in normal circumstances there would be no cause for concern: the exercise of discretion remains invisible because of taxpayer confidentiality and there is a widespread acceptance of the neutral and objective nature of taxation. Using the second dimension of power, we can examine how certain forms of accountability are currently organized off the agenda. In particular, the difficulties that might beset concerned citizens from seeking judicial review point to a particular mobilization of bias. A third-dimensional analysis of the way discretionary power is exercised might suggest that the interests of powerful taxpayers are woven into the fabric of HMRC's policy and decision-making apparatus or that individual tax officials have absorbed and internalized the ethos of an organization which has been subject to regulatory capture, and thus exercise their discretion in a partial way. Once the operation of power is exposed, this can become part of the democratic discourse and there is potential for power relations to change.

The Adjudicator may look into cases concerning HMRC's use of discretion (Adjudicator's Office 2015) but it is unclear whether this covers the use of

discretion in dealings with other taxpayers. Furthermore the opportunity for redress is limited because the Adjudicator can only require HMRC to apologize, meet additional costs incurred or make a small payment in recognition of the worry and distress caused by the error (Freedman & Vella 2011). The Ombudsman may investigate complaints that HMRC has acted unfairly, although it is again not clear whether a complaint may be made concerning their treatment of another taxpayer, or has provided a poor service (Freedman & Vella 2011).

In the UK, judicial review allows plaintiffs to ask the courts to rule, quite simply, whether or not a public body was acting within its powers. It can therefore allow taxpayers to challenge decisions on the grounds that HMRC exceeded its powers of discretion or applied its powers improperly. Judicial review is not a panacea for accountability for the use of administrative discretion and there exist several barriers to using this method. Firstly, it is costly to undertake for the plaintiff. Secondly, the legal rules and procedures which a court might be asked to rule on are social and legal constructs or Foucauldian truth regimes (Foucault 1980) and are likely to have been constructed to serve the interests of the dominant actors. Legal terms and procedures might therefore be defined in a manner which restricts the terms of reference of a challenge or review to aspects which the dominant actors are prepared to expose to public scrutiny. These procedural barriers are the operation of Lukes' (2005) second dimension of power, since they are a means of 'organizing out' resistance. Plaintiffs therefore need to establish to the courts' satisfaction that there are appropriate grounds for review. Reviews are limited in scope to narrow, technical

considerations which do not threaten the dominance of the hegemonic group rather than broader notions of justice and equity which might do so (de Cogan 2011). Judicial review cannot of itself overturn decisions and the threshold of unreasonableness is very high – being such that no reasonable person would have taken that decision (Freedman & Vella 2011). Plaintiffs must demonstrate that they are entitled to seek a review – that is, they must have legal standing (*locus standi)* (Ho and Ross 2010).

Taxpayers will almost certainly have standing in judicial review if they are directly affected by the HMRC's use of its discretion, such as Mr Wilkinson in *R v Commissioner (ex parte Wilkinson) (2005)*. More contentious is the use of judicial review by third parties who are not directly affected. Taxpayers do not have a direct interest in the affairs of other taxpayers. However, if some taxpayers are permitted to pay less than they might otherwise because of the exercise of administrative discretion, then others must pay more or public expenditure must be reduced. The social contract implicit in taxation (Boden 2012), which underpins notions of fairness and equity, suggests that taxpayers do have at a legitimate indirect interest in what others pay.

The question of precisely how direct an interest must be in order for it to be deemed sufficient to give a taxpayer standing therefore determines, *inter alia*, the extent to which it is possible to exercise oversight over the exercise of discretion by tax authorities using judicial review. Ho and Ross (2010) admit that standing is one of the most controversial areas of US federal law. Jensen et al. (1986) describe the concept as 'amorphous' and examine the consequences

of adopting either a restrictive or a liberal doctrine, suggesting that this is not an objective concept, but one which is subjective and socially constructed. Winter (1988) proposes an 'insulation thesis', which holds that progressive Supreme Court justices invented the concept of legal standing to insulate government agencies from judicial review in order to ensure that these agencies were free to 'experiment' with progressive legislation, a thesis that has gained some support (see for example Sunstein 1988). Whilst Ho and Ross (2010) dispute this thesis, it does point to an admission amongst some legal commentators that standing might be deliberately used to permit or restrict access to judicial review.

The range of the types of applicants and interests who may petition for judicial review will depend on whether the rules of standing are interpreted in a narrow or a broader, more relaxed manner, with more relaxed rules permitting a wider range of litigants to petition the courts. Some of the arguments for or against a particular interpretation are practical. For example, advocates of narrow rules of standing argue that a broad interpretation will lead to a larger number of reviews, with a resulting increase in costs, much of which would have to be met from the public purse. Judges might also spend more time trying to 'fireproof' decisions against subsequent reviews. Furthermore, restricting the right to those with a personal interest might give plaintiffs greater motivation and sharpen legal arguments. However, Hilson and Cram reject these criticisms, arguing that objections on grounds of cost prioritize the flow of government over legality, or functionalism over normativism, that taking care to fireproof decisions can equally be viewed as ensuring higher quality decision-making and

that there is no evidence that ideological interest groups demonstrate any less motivation than those with a personal interest (Hilson & Cram 1996:4-6).

At a more principled level, the interpretation of standing might depend on whether a moral, strategic litigation or a politically instrumental perspective is adopted (Vanhala 2012). Liberal individualism places much emphasis on individual property rights and a narrow interpretation restricts standing to those whose property rights have been infringed. A broad interpretation might mean that, where a decision is reached after democratic debate by elected representatives, allowing parties other than those directly affected to litigate that decision might lead to the earlier debate being re-run, thus usurping the role of the elected representatives, and public law might focus on policy evaluation, rather than legal principle (Hilson & Cram 1996). Hilson and Cram reject these criticisms, arguing that judicial reviews do not have free rein and must adhere to the principles of administrative law. If any of these principles appear to give the judges free rein, the solution should be to develop tighter principles, rather than restrict the right of standing.

Furthermore, permitting a broad interpretation of standing means that judicial review can be used as a means of promoting good administrative practices, which might prevent threats to individual liberty arising in the first place (Hilson & Cram 1996), and, if courts are viewed as an important part of the democratic policy process and as a pluralistic and participative venue for debate, groups who may have been excluded from the original debate may be included (Vanhala 2012). From a strategic litigation perspective, broadening the

interpretation of standing increases opportunities for ‘winning’, although Vanhala (2012) cautions that being granted standing does not equate to a good chance of winning and cites statistics which indicate that the record of non-governmental organizations (NGOs) in winning legal challenges is poor. However, NGOs must make a strategic choice on whether to pursue their objectives through political lobbying or litigation. If the political environment is not receptive to their cause, lobbying is unlikely to be effective and they are more likely to prefer litigation (Hilson 2002), but from a politically instrumental perspective, the mere threat of legal action might give an NGO bargaining or lobbying power (Vanhala 2012).

The question of standing in English law has evolved in a rather haphazard and *ad hoc* manner, but a review of cases in the 1980s and 1990s such as *Reg. v Inland Revenue Commissioners ex parte National Federation of Small Businesses and Self-Employed (1980), Greepeace Ltd v HM Inspectorate of Pollution No. 2 (1993)* and *Reg. (Friends of the Earth) v Secretary of the State for the Environment (1994)* show a tendency to prefer a broader interpretation of standing (Hilson & Cram 1996; Vanhala 2012). Hilson and Cram argue that applications from groups should be preferred to those from individuals on the grounds that groups are likely to possess greater expertise and in the case of *Reg. v Inspectorate of Pollution and another ex parte Greenpeace Ltd (No. 2) (1994)*, Otton J described Greenpeace as an entirely responsible and respected body with a genuine concern for the environment and that an important reason for granting them standing was that their experience and access to expertise

meant that they were able to mount focused, relevant and well-argued challenges (cited in Hilson & Cram 1996:24).

In chapter 9.3. I use the judicial review in May 2013, which the pressure group UK Uncut successfully petitioned for, into the decision by HM Revenue & Customs to forgive give of interest payable by the investment bank Goldman Sachs as a case study. This case study illustrates how UK Uncut successfully surmounted the barrier of establishing legal standing, but failed to surmount the barrier of demonstrating that HMRC had acted beyond its power, although the long term effect of the decision on public opinion might still lead to a shift in the underlying power relations. This challenge is contrasted with an earlier challenge by the FSB, which failed to even gain access to the legal process to mount a challenge in order to illustrate the shift in legal reasoning, and therefore in the underlying power relations within the law, which had already taken place in the intervening 30 years.

9.3. Troubling Cases

The FSB is, as its name suggests, an organization which represents and lobbies on behalf of small businesses and the self-employed and in the early 1980s it petitioned for a judicial review into what it saw as inequitable treatment of its members by the Inland Revenue compared to the Inland Revenue's treatment of the Fleet Street print unions and this has become a leading case on administrative discretion. In the days when the newspaper industry was based along Fleet Street in London, the 'Fleet Street casuals' were around 6,000 casual print workers nominated by their trade unions to work for

newspapers on specified occasions. These workers were given call slips and collected pay dockets from the unions in order to claim pay from their employers. A number of them gave false names (sometimes, allegedly, as blatant as ‘M. Mouse’ or ‘D. Duck’), making it impossible for the Inland Revenue to collect payroll taxes. The tax lost was estimated at around £1m a year. The unions to which the casuals belonged had a full list of the workers’ details and the payments made to each, but were not allowed to disclose these to third parties. A deal was made between employers, the unions and the Inland Revenue under which, in return for the Inland Revenue not pursuing tax already lost through these frauds, it was agreed that tax would be properly assessed and accounted for henceforth.

The FSB challenged this agreement on the grounds that it compared unfavourably with what it saw as the aggressive stance taken by the Inland Revenue towards its members suspected of tax evasion. It wanted the Fleet Street tax amnesty to be ruled illegal and for the Inland Revenue to be required to collect the tax due from the workers for previous years. The FSB’s application for a judicial review was refused by the Court of Appeal and on appeal to the House of Lords (at that time the highest court in the UK).

Whilst the majority of judges took a narrow perspective and rejected the FSB’s application, in the Court of Appeal Lord Denning alone dissented. His judgement was based on much broader notions of equity and the public interest and, whilst legal rules and procedures might dismiss this dissenting opinion as mere ‘noise’ (Edgley 2010), it can give valuable insights. The central issue of

the case was whether the FSB had a sufficient interest in the affairs of other taxpayers by virtue of their perception that other taxpayers were receiving more favourable treatment than their members. Further issues were whether this interest might override the general principle of taxpayer confidentiality and whether the agreement reached exceeded the limits of the Inland Revenue's administrative discretion.

Denning was the only judge in the FSB case who considered the issue of the accountability of public bodies in detail *(Reg. v IR Commissioners ex parte Federation of Self-employed and Small Businesses Ltd 1980).* Denning argued that the public interest dictated that it was of paramount importance that there be oversight of public bodies in the way that they carried out their functions; if the FSB were unable to complain, there was nobody else who would be able to do so, excluding the possibility of oversight.

Denning stated that preventing oversight of public bodies might lead to 'deplorable decisions'; such as that in *Reg. v Lewisham Union Guardians (1897) (*cited in *Reg. v IR Commissioners ex parte Federation of Self-employed and Small Businesses Ltd 1980)*, where the guardians of the poor in Lewisham were obligated by statute to ensure that everyone was vaccinated against smallpox, but they failed in that duty, thus putting everyone at risk (Lord Denning implying that this included even those who had been vaccinated). In the Lewisham case the court decided that nobody had *locus standi* to complain. The consequence was that there was no way in which the public authority could be obliged to perform its duty. Lukes (2005) might argue that this was the

mobilization of bias characteristic of the operation of the second dimension of power.

Denning argued that accountability in the FSB case was necessary because it was undesirable that certain groups in society should be able to exert undue influence. Quoting Mr Hoadley (the Principal Inspector of Taxes involved in negotiating the Fleet Street agreement) at some length, he made it quite clear that, in his opinion, Mr Hoadley believed that the attitude of the newspaper owners and of the print unions would frustrate a successful investigation and that more tax could be raised through the arrangement made. The Inland Revenue was prepared to admit defeat in the face of these obstacles. It is worth noting that under UK law Mr Hoadley could have simply raised reasonable assessments against the workers and placed the onus on them to produce the evidence to displace them. The argument that it would have been difficult or impossible to raise large amounts of tax through an investigation therefore appears contentious. The decision of the Inland Revenue not to pursue the investigation might therefore be viewed as the operation of the third dimension of power, since he was using his authority to disguise the exercise of discretion as a techno-rational decision.

Perhaps because of his commitment to the notion of public accountability, Denning was prepared to interpret the doctrine of standing broadly, arguing that the FSB did indeed have a sufficient interest. He reasoned that the Fleet Street casuals had been afforded special treatment because of their industrial muscle, which the FSB members lacked and that, if the FSB were unable to complain,

there was nobody else who would be able to do so and there would therefore be no possibility of a remedy. He cited the words of Walton J. In the Court of Appeal in *Vestey v IRC (1979) (cited in Reg. v IR Commissioners ex parte Federation of Self-employed and Small Businesses Ltd 1980:24)*, noting that they were quoted and stressed by Wilberforce when this case was heard in the House of Lords

> I conceive it to be in the national interest not only of all individuals…but also in the interests of the revenue authorities themselves that the tax system should be fair…One should be taxed by law and not untaxed by concession…A tax system which enshrines obvious injustices is brought into disrepute with all taxpayers accordingly, whereas one in which injustices, when discovered, are put right (and with retrospective effect if necessary) will command respect and support.

Denning argued that if the tax system is not fair and no remedies are available for injustices, then it will fall into disrepute.

Denning exercised his prerogative to depart from the Lewisham precedent and establish a less restrictive interpretation of 'sufficient interest' as argued in *Attorney General of the Gambia v N'Jie (1961)* (cited in *Reg. v IR Commissioners ex parte Federation of Self-employed and Small Businesses Ltd 1980:421).* In this judgement, he precluded a 'mere busybody' from having

standing, but included anyone with a ‘genuine’ grievance. In doing so he illustrated the power held by judges, to reverse decisions by ruling that a precedent is no longer compatible with contemporary values and society.

If judges exercise power in overturning precedents and extending the concept of standing, it follows that they are equally exercising power by refusing to do so. In his judgement on the FSB case in the House of Lords, Lord Wilberforce argued that

> As a matter of general principle I would hold that one taxpayer has no sufficient interest in asking the court to investigate the tax affairs of another taxpayer or to complain that the latter has been under-assessed or over-assessed; indeed there is a strong public interest that he should not. (Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd 1982:633)

Wilberforce did not (and was not obliged to) elaborate on why it was not it the public interest to allow taxpayers to complain in such circumstances. However, the fact that what appears to be an objective exercise might actually be a somewhat arbitrary exercise of power may be discerned by contrasting his argument here with the argument that he made in *Vestey v IRC (1979)* quoted above. Denning also cited similar statements by Wilberforce in *Gouriet v Union of Post Office Workers (1978)* and *Arsenal Football Club v Ende (1979) (*both cited in *Inland Revenue Commissioners v National Federation of Self-Employed*

and Small Businesses Ltd 1982:633), in which Wilberforce emphasized the need for fairness in taxation and advocated a much more liberal concept of standing than he was prepared to allow in the FSB case. Wilberforce distinguished the latter case from the FSB one by the narrowly legalistic argument that the General Rates Act 1967 gave an 'aggrieved person' the right to mount a challenge, whereas no corresponding right was intended by the income tax legislation *(Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd 1982:633-634)*.

The FSB therefore failed in its attempt to obtain a judicial review on the grounds that it had no standing, that the Inland Revenue's action fell within the administrative discretion permitted by statue and that there was therefore no public interest in overriding the statutory duty of taxpayer confidentiality. Thirty years later these principles were once again tested in broadly similar circumstances.

An interesting case

In October 2011 *The Guardian,* a UK broadsheet newspaper, reported that HMRC had agreed to forgive the American investment bank Goldman Sachs £10m of interest arising as a result of failed tax avoidance schemes. This deal was described by officials as 'cock-up' (Leigh 2010), but they refused to disclose who was responsible. Disclosure of this agreement was not an isolated incident: in July 2010 the *Daily Telegraph,* another broadsheet, reported that HMRC had settled a long-running tax dispute with Vodafone (Armitstead 2010),

under the terms of which the company agreed to pay £1.25bn over a five-year period. The precise amount of tax which might have actually been due is speculative, and was variously estimated between £6bn (Sikka 2011) and £8bn (Mason 2011).

The agreements with Goldman Sachs and Vodafone had entered the public domain due to Osita Mba, an HMRC solicitor who had turned whistleblower. These disclosures therefore breached the barrier of taxpayer confidentiality which prevents the use, or abuse, of administrative discretion becoming public knowledge and allowed the normally hidden operation of power to become visible. They were often termed ‘sweetheart deals’ and were widely criticized in the media. For example, Norman (2011) criticized the facts that HMRC’s lawyers had little information about the deal because Hartnett had not consulted with them and were ‘evidently deeply uncomfortable about the settlement’. He also criticized the lack of disclosure by HMRC, citing their counsel James Eadie who stated that, whilst HMRC had a general duty of confidentiality, it could make disclosures to a parliamentary body with an oversight role and the decision not to do so was Hartnett’s. Similar criticisms were made elsewhere, for example by Armitstead (2011). Outrage was not restricted to media coverage; a report by the PAC (House of Commons 2011) accused HMRC of giving large firms favourable treatment and singled out Dave Hartnett, the then head of HMRC, for particular criticism, accusing him of failing to conduct negotiations properly and adhere to internal procedures.

These were clear accusations of regulatory capture – the operation of the third dimension of power (Lukes 2005) HMRC, Goldman Sachs and Vodafone are all part of the same neoliberal assemblage and HMRC were accused of having relinquished its role of being an independent administrator treating all taxpayers equally and having adopted the values of large corporations. In the wake of this Sikka (2011) repeated the accusation in the PAC report that HMRC had a 'cosy relationship with the tax avoidance industry' and argued that the deals had let multinational corporations off the hook, but that there was little public accountability. He cited as evidence that: HMRC officials attended numerous lunches, dinners and receptions organized by the Big Four accounting practices who work for such firms (which had been established by researchers at Bureau of Investigative Journalism 2010); that this hospitality by the accounting profession was intended to further their own interests; and, that former ministers, such as Lord Mandelson and Lord [Digby] Jones, acted as consultants to these firms.

Sikka was not alone and similar criticisms were made by, for example, BBC (2010). The National Audit Office (NAO) (National Audit Office 2012) then conducted an investigation headed by Sir Andrew Park, a former judge, into five large corporate deals in order to ascertain whether they were 'reasonable' and in accordance with legal advice and internal HMRC guidelines. It concluded that all the settlements relating to tax and national insurance were reasonable, that the failure to charge Goldman Sachs interest appeared to be a deliberate decision which made sense in the context of reaching a deal on the various issues, and that officials may 'genuinely have believed that there was a barrier

[to demanding the interest]'. The NAO also made similar criticisms of HMRC's governance procedures as the report by the PAC (National Audit Office 2012:84).

Against this background, the grass-roots pressure group UK Uncut, which was founded in 2010 to campaign against the public spending cuts imposed by the Conservative - Liberal Democrat coalition government, announced on 20 December 2011 that it intended to seek a judicial review of the deal between HMRC and Goldman Sachs and a ruling that it was *ultra vires*.

UK Uncut's decision to pursue the Goldman Sachs case and not the Vodafone one merits explanation, especially as the latter case involved far greater sums. The Vodafone case involved disputed tax on the application of the Controlled Foreign Companies (CFC) legislation[1] to profits arising on the acquisition of the German company Mannesmann through Vodafone's Luxembourg subsidiary dating back to 2000. Although HMRC had prevailed in the Court of Appeal *(Vodafone 2 v HM Revenue & Customs 2009)* and Vodafone had been refused leave to appeal to the Supreme Court, there remained the possibility that the decision might be challenged in the European Court of Justice on the grounds that applying the UK CFC legislation to transactions within the EU contravened European law. Vodafone had indicated its willingness to pursue a lengthy and costly dispute to the bitter end. HMRC was willing to negotiate a settlement in order to avert an expensive case that it had no guarantee of winning, even though the case had been finally settled as far as the UK judicial system was

[1] Legislation which prevents companies from avoiding tax by artificially diverting profits into overseas companies resident in tax havens.

concerned. Armitstead (2010) claimed that this approach was evidence of a policy shift by the government, dubbed the ‘dash for cash’ – that is, a desire to relieve ailing public finances now rather than hang out for possibly greater amounts in the future. Vodafone were clearly exercising the power that comes from having a significant war chest for such battles and knowing that its payments could have a significant effect on public finances and this shift in the balance of power from nation states to large corporations is a characteristic of a neoliberal state. Problematically from UK Uncut’s perspective, any European case was highly contestable and would have been the subject to much abstruse legal argument. This would have made HMRC’s exercise of discretion appear more justifiable on the grounds of expediency.

In contrast, the sum in the Goldman Sachs case related to interest payable on tax which had initially been underpaid due to the failure of tax avoidance schemes relating to staff bonuses. Goldman Sachs had admitted that the tax itself was due and that it had been paid late. The addition of interest to the bill in such circumstances would normally be automatic and non-discretionary in law – yet HMRC had forgiven it *(SI 2001/1004 reg.67)*. This case therefore avoids the difficulty that the assumption of the existence of an objectively correct amount of tax payable is fallacious. The action by HMRC was contrary to the principle that, whilst administrative cooperation might provide a convenient means of securing the correct payment, it should not be a process of negotiating what that amount should be (de Cogan 2015). Pursuing the more clear-cut case allowed UK Uncut to focus on the important issue of the extent to which it is possible to

subject the system of tax administration to public scrutiny and hold it to account for the way in which it exercises discretion.

UK Uncut decided to petition for a judicial review in December 2011 after what it described as a 'dismissive' response to its letters (UK Uncut Legal Action 2015) and following the publication earlier in the month of a report by the PAC (House of Commons 2011), which seriously criticized HMRC's handling of large tax disputes. Like the FSB, UK Uncut also had to prove that it had legal standing and that there was a case to answer in order to pursue its challenge and an initial hearing was held in June 2012 to adjudicate this issue *(R v Revenue and Customs Commissioners 2012)*. HMRC advanced three arguments as to why the review should not proceed. First, the proceedings had been commenced more than three months after the claim became public knowledge in *Private Eye*[2] in April 2011. Second, UK Uncut did not have standing. Third, there was an alternative remedy as the PAC was already investigating the matter.

The judge rejected all three arguments. First, whilst the claim may have been public knowledge in April 2011, it was arguable that UK Uncut was entitled to await the outcome of the PAC report, which was published on 14 December 2011 (House of Commons 2011), since this report carried much more weight and authority than the piece in *Private Eye*. Assembling and marshalling the evidence necessary to conduct a judicial review entails considerable cost, and UK Uncut were entitled to wait until they had authoritative evidence before proceeding. Indeed, if UK Uncut had petitioned the courts on the basis of

[2] A UK magazine which combines satire and investigative reporting and which is well known for being willing to risk being sued.

evidence contained in *Private Eye*, this might well have been deemed to be insufficient grounds. This detail points to the reliance on leaks and whistleblowing to bring such matters into the public eye. HMRC's attempt to divert examination of the issue to Parliament would have effectively ensured that fewer details of the actual deal would have come out as its powers of examination are considerably weaker and it has no right to declare decisions *ultra vires*.

Second, the judge held that UK Uncut had a legitimate argument that they were a category of persons as set out in the FSB case who could take advantage of a more relaxed view of the categories of persons who had standing, i.e. parties who had an indirect interest in the matter. The judge said that the issue of standing would not by itself prevent the application being granted *(R. v Revenue and Customs Commissioners 2012)*. As well as adjudicating the issue of standing, the initial hearing also determined whether the plaintiff had a *prima facie* case and UK Uncut therefore had to present their evidence. Although it is not known what evidence was presented, this might have included the e-mail of 7 December 2010 from Dave Hartnett in which he stated that going back on the agreement would cause HMRC and him personally great embarrassment and reputational harm because of the mistakes they had made and the judge may therefore have concluded that the public interest was sufficient to allow this review.

Third, the judge noted that whilst the PAC might express an opinion on a number of issues connected with this case, it could not rule on the legality of the

arrangement *(R. v Revenue and Customs Commissioners 2012)*. The judge did not elaborate on this statement, but may well have meant that a finding by a judicial review that the arrangement was unlawful would be more severe criticism than the findings of the PAC. UK Uncut therefore achieved more than the FSB by obtaining a judicial review and thereby calling HMRC to account for the way in which it used its administrative discretion.

Calling to account

The FSB case was never heard fully as the plaintiff had no standing. However, the judges did adumbrate on the extent to which the Inland Revenue might have exceeded its powers as part of their consideration of the public interest of the case (and therefore of standing). The UK Uncut case did go to review, so full consideration was given to the question of whether the HMRC had exercised its discretion legitimately.

UK Uncut put forward three arguments why the settlement should be ruled unlawful. First, it breached the guidelines in HMRC's *Litigation and Settlement Strategy* (HMRC 2007) in the following ways;

1. the settlement with Goldman Sachs resolved a number of issues for the payment of an agreed sum and was therefore a package deal', i.e. an agreement where a number of issues are settled for a single payment that is not subdivided between individual disputes. Officials are instructed not to enter into such deals;
2. the dispute with Goldman Sachs involved a single point of law and should therefore have been settled on an all-or-nothing basis. However, in the

settlement HMRC conceded some issues and Goldman Sachs conceded others and the parties therefore effectively 'split the difference', in contravention of the guidelines;

3. officials should not undercharge tax, interest or penalties in the interest of quick settlement, even if doing so would constitute a good return on time spent on the case and officials should always consider whether the settlement terms do enough to promote positive taxpayer behaviour and discourage non-compliance. Furthermore, the guidelines instruct officials not to accept settlements for less than 100% of the tax and interest due, if HMRC's advice is strong.

(Litigation and Settlement Strategy 2007 cited in *UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:9*)

Second, Dave Hartnett had taken account of immaterial considerations in reaching the agreement and in support of this argument they presented the email sent by Hartnett on 7 December 2010. Furthermore, when a colleague broached the matter of the interest with Goldman Sachs they 'went off the deep end' and threatened to withdraw from the code of conduct on taxation which the Chancellor of the Exchequer had persuaded the major banks to sign up to, thereby causing great political embarrassment *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:15 & 33)*. Third, there was a breach of equality, since the case was settled on different terms from those of other companies who had adopted the same arrangement as Goldman Sachs, but had settled in 2005 *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:33)*.

Mr Justice Nicol rejected all of UK Uncut's arguments, ruling that the agreement to waive interest was lawful and that HMRC was acting within its powers of administrative discretion. However, he also noted, with lawerly understatement, that '[t]he settlement with Goldman Sachs was not a glorious episode in the history of the Revenue' *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:66).* He rejected the argument that the settlement contravened HMRC's *Litigation and Settlement Strategy* (HMRC 2007), stating that interest and principal were treated as separate issues and that an all-or-nothing approach was taken on each of these, with HMRC getting all of the principal and nothing of the interest. He did not comment on whether this treatment was correct, given that interest arises due to the late payment of the principal, simply noting that the treatment was consistent with the settlements reached with the other companies in 2005 *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:36).* He also accepted (as had Sir Andrew Park, National Audit Office 2012:85) that HMRC had genuinely believed that there was a technical barrier to recovering the interest, although he states that this was a mistaken assumption and also criticized Hartnett for not consulting with their lawyers on the matter and not obtaining approval from the Programme Board *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:37)*.

Despite these criticisms he ruled that the settlement was not unlawful because the Commissioners were dealing with an exceptional situation *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:38)* and they believed that it represented a 'good deal for the Revenue' *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:41)*. The fact that the correctness of HMRC's

position was less important than what they believed can be seen as the operation of the third dimension of power where subjectivity is hidden behind a techno-rational, legal justification (James 2010).

Mr Justice Nicol also rejected UK Uncut's second argument that Hartnett had taken irrelevant considerations into account in reaching the settlement. Whilst these factors included personal embarrassment and reputational harm due to the admission of errors, it also included the accusation that he had given in to threats by Goldman Sachs and this makes for an interesting comparison with the FSB case. It was common ground between Denning and his colleagues that the Inland Revenue had wide administrative discretion and the disagreement between them concerned not whether this discretion extended to giving in to outside pressure and threats, but whether they actually did so. Denning agreed that the Inland Revenue should have the power to negotiate with taxpayers, but stressed that the threat of industrial action had been a significant factor in the decision to settle. He cited an affidavit by Mr Hoadley, the Inspector of Taxes, which said

> ...I considered that if any solution was to have a real prospect of being effective the agreement of the employers and the co-operation of the casual printing worker and their union representatives was essential. I feared that if this co-operation could not be achieved, *the employers* would be unlikely to agree to any solution *because of the real*

> *possibility of industrial action being taken*. (Emphasis in original)
>
> (Reg. v IR Commissioners ex parte Federation of Self-employed and Small Businesses Ltd 1980 418-419)

Whilst Wilberforce made much of the difficulty of obtaining large sums of money from uncooperative workers and employers, he dismissed the idea that HMRC bowed to pressure from the unions and employers due to the threat of industrial action, describing Mr Hoadley's reasoning as 'all part of the process of obtaining the agreement' *(Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd 1982:635)*. He therefore considered that, in coming to the arrangement 'the Inland Revenue… were acting genuinely in the care and management of the taxes under the powers entrusted to them', that they ''acted in the *bona fide* exercise of the wide judicial managerial discretion conferred on them by statute' and that this discretion should be used so as to generate the 'highest net return that is practicable having regard to the staff available to them and the cost of collection' *(Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd 1982:635-7)*.

The disagreement between these two judges was therefore one of interpretation of the facts, rather than a point of law. It is not clear whether the employers and/or unions actually made any explicit threats or representations to HMRC. However, even if they did not, the mere possibility of this might have been

enough to cause Mr Hoadley to hesitate and, arguably, he was responding to the potentiality of overt power, which is an illustration of Foucauldian self-regulation (Foucault 1979 [1975]). Wilberforce's denial that Mr Hoadley was influenced by the power of the employers and unions suggests a similarly partial and subjective process. If Wilberforce had viewed Mr Hoadley's behaviour as the product of trepidation based on the previously militant behaviour of the print unions, this might have taken him in a direction he did not wish to go. That is, it is possible that Wilberforce, consciously or unconsciously, was exercising his power to construct the behaviour of the Inland Revenue.

In the UK Uncut case, the e-mail from Dave Hartnett meant that, unlike Wilberforce, Mr Justice Nicol could not simply pretend that Dave Hartnett was not influenced by threats. He acknowledged that Dave Hartnett was worried that going back on the agreement would damage a relationship with Goldman Sachs which had been very difficult and that it might lead to more aggressive future behaviour *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:20)*. However, he ruled that this, like the embarrassment, both personal and to HMRC, was irrelevant, because Dave Hartnett would have reached the same conclusion even in the absence of these factors *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:45-65)*.

Furthermore, it was for the decision-maker (i.e. the HMRC official) to decide which factors were relevant or irrelevant, subject to any statutory limitation. Therefore, even though Mr Justice Nicol considered these factors to be irrelevant, it was not irrational for Dave Hartnett to have considered them and it

was therefore not unlawful for him to have done so *(UK Uncut Legal Action Ltd v Commissioners of HMRC 2013:62)*. Dave Hartnett was therefore able to exercise the third dimension of power by being able to subjectively select which factors he wished to consider, which recalls Boll's (2011) argument that tax compliance is constructed by the factors which the tax authority wishes to view and those it chooses to ignore.

Since Mr Justice Nicol dismissed UK Uncut's appeal the question therefore arises whether the challenge has actually achieved anything and the conclusion therefore discusses whether it might have any significance, despite the defeat.

9.4. Summary

In this chapter I have discussed the extent to which and how it might be possible to resist the hegemonic, neoliberal paradigm of taxation. This paradigm is held in place by three types of power. The first is economic, whereby large corporations are able to use the international mobility of capital to coerce governments into enacting a tax regime which favours their interests as a price for enticing inward investment by these companies. This argument still exerts considerable power even though this often merely leads to tax arbitrage, where corporations use legal and accounting techniques to shift profits to low-tax jurisdictions without relocating the underlying economic activity. The second type of power is ideological, whereby a tax regime favouring the interests of capital is justified through constructs of incentivization and economic efficiency derived from neoclassical economics and tax law is presented as objective and techno-rational so that the exercise of power through judicial discretion remains

hidden. The third type of power is administrative. Whilst administrative discretion is necessary in order to operate a tax system on a day to day basis and HMRC have always had wide powers of discretion, the acceptability of this relies on it being exercised in an even-handed manner with no systemic bias towards particular groups of taxpayers. However, in a neoliberal state this becomes problematic since the tax authorities and large corporations now both form part of the same assemblage of power, raising the possibility or the suspicion of corporate capture of the tax authority. This is made more acute by the principle of taxpayer confidentiality so that it is not usually possible to observe how administrative discretion has been exercised.

Instances where it is alleged that administrative discretion has been exercised in a partial manner are occasionally made public due to the accidental release of information or the actions of whistleblowers or investigative journalists. These releases of information may often have an effect on public opinion and whilst governments form part of an assemblage of power they also remain answerable to the public and cannot afford to ignore public opinion. However, even where the public becomes aware of uses of administrative discretion which it considers unacceptable, hegemonic groups can exercise power by placing restrictions on the remedies available and thus frustrating democratic oversight of the way in which public bodies exercise their powers. These might take the form of imposing high costs on those wishing to pursue a remedy, confining the scope of a remedy to narrow technical issues rather than wider issues of social justice or restricting the availability of a remedy to those who have been directly harmed.

It is therefore in the context of seeking to resist the neoliberal paradigm of taxation that I discussed UK Uncut's legal challenge to the agreement between HMRC and Goldman Sachs to waive approximately £10m of interest relating to the late payment of national insurance contributions, which I have compared with the FSB case which raised similar issues in the 1980s. Whilst UK Uncut achieved more than the FSB by successfully arguing that they had legal standing in order to obtain a judicial review, their challenge was defeated, the review did not raise any fundamental issues which had not been raised by the reports of the PAC and the NAO and the reasons given for dismissing their case were very similar to those in the earlier case. The question therefore arises whether UK Uncut's challenge can be dismissed as merely a magnificent, but ultimately futile, gesture of defiance or whether it might be the starting point for more concerted resistance to the neoliberal paradigm of taxation, or indeed to neoliberalism in general.

The judicial review forced Dave Hartnett to give evidence, thus making HMRC more accountable for the way in which it carries out its duties and his evidence, particularly the widely-reported e-mail of 7 December 2010, provided additional richness of detail concerning HMRC's relationship with large taxpayers and exposed clearly the operation of power. Furthermore, in contrast with the FSB case, it has gained wide press coverage and in the age of the internet the full judgement, Dave Hartnett's evidence and e-mail were all posted on UK Uncut's website (UK Uncut Legal Action 2015) within hours of the decision being released. The details of the behaviour of HMRC and Goldman Sachs and the extent of HMRC out its duties and his evidence, particularly the widely-reported

e-mail of 7 December 2010, provided additional richness) than would otherwise have been the case, although much of this has admittedly been unnuanced and/or ill-informed.

There is, however, only a limited benefit from exposing the operation of power, if this does not then lead to change. Campaigning organizations, such as UK Uncut, usually use litigation as one part of their campaigning strategy and have an attitude of 'losing the battle, but winning the war' in relation to a specific campaigning goal (Vanhala 2012:544). Although law and legal procedures may appear to have the characteristics of Foucauldian truth regimes, i.e. historically specific mechanisms which produce discourses which function as true in particular circumstances (Michel-foucault.com 2015), they are not static and immutable, but dynamic. Epp (2009 cited in Vanhala 2012:526) has found that law emerges both out of the interests and power of elites and out of social relationships, rather than being imposed from above. The drive for legal change can therefore be 'bottom-up' as well as 'top-down' and Hilson (2002) reminds us that elites can ensure that their interests are heard through effective lobbying, whereas litigation is more likely to be a tool used in 'bottom-up' pressure for change. The emergence of movements such as UK Uncut can be seen as a shift away from the law and courts as drivers of law and social change towards multiple locations of social movements (Paris 2010 cited in Vanhala 2012:526).

Furthermore, it might conceivably lead to fundamental changes to the basis of company taxation, such as replacing the territorial basis of taxation where countries tax companies on profits arising in their territory with the unitary basis

of taxation[3]. Such a shift in public opinion is usually gradual and cannot occur unless people become aware of the hidden operation of power which holds the status quo in place. By holding HMRC accountable for its relationship with Goldman Sachs and the manner in which it exercised its discretion, UK Uncut has achieved a significant success by illustrating Lukes' (2005) argument that power, however complete and hidden, can never be absolute and that there are always critical windows of opportunity through which its hidden operation becomes apparent. There is, indeed, a long way between a matter being on the political agenda and effective action being taken, but if public opinion and the political process does lead to a shift in power relations. Indeed, the announcement in the July 2015 Budget of the curtailment of the use of the remittance basis (HMRC 2015b) can be seen as an example of governments being forced to bow to public pressure and, although the threshold of being resident for 15 of the past 20 years might be seen as excessively generous by some, once the principle has been conceded it is easier to adjust this subsequently. If this is simply the first in a number of such changes which radically reform the tax system history may well conclude that, whilst UK Uncut may have lost this particular battle, it helped to win the war.

[3] A basis of taxation under which the worldwide profits of a group are calculated and apportioned between the countries in which they operate according to an agreed formula based on, for example, sales generated in and/or assets located in each country.

CHAPTER 10: CONCLUSION

10.1. Introduction

In this concluding chapter I summarize and evaluate the arguments I have advanced in the previous eight chapters. In chapter 10.2. I set out the questions I have addressed in this thesis and in chapter 10.3. I summarize the detailed arguments which I have advanced. This is followed in chapter 10.4. by an evaluation of the thesis and suggestions for further work.

10.2. Questions Addressed

Taxation is generally studied as either a branch of law or economics. A legalistic study of taxation analyzes extant law or proposed changes in terms of how they should be interpreted and an economic study analyzes taxation in terms of theoretical models relating to how taxpayers respond to tax regimes. However, both of these paradigms ignore the fact that tax policy is subjectively framed through a discursive process, which can be influenced by the exercise of power.

Accordingly, my principal research question was: *how, in a neoliberal state, are power relationships between citizens and the state mediated through taxation and what are the consequences for tax policy?*

With regards to taxation, formal relationships between citizens and the state are strictly bilateral and confidential. For example, individuals must make a return of their income and the state will assess them accordingly. However, the formulation of tax policy involves multilateral relationships and public debate

and discussion as actors combine into social groupings of various sorts in order to express their preferences. The state is not necessarily a neutral institution in such multilateral relationships and certain social groupings might assume a hegemonic position, thus exerting power through the state by ensuring that it serves their interests at the expense of the interests of other social groupings.

In order to answer this question I therefore addressed the following subsidiary questions:

The first subsidiary question was: *what strategies might be deployed in the formulation of tax policy in order to achieve the exercise of power?*

The exercise of power in the formal bilateral relationships between citizens and the state is structural and largely hierarchical, but this can be frustrated by violent or civil disobedience or deceit. However, the formulation of tax policy in the first place involves capillary flows of power through numerous social actors. Tax policy is therefore the product of these networked social relationships and the strategizing of various social groups.

My second subsidiary question was: *what are the factors which might inhibit the exercise of power in the formulation of tax policy?*

In multilateral networks power is capillary and, as such, its exercise is subject to restraint and inhibition. This question will therefore allow the exploration of the factors which limit the exercise of power.

My third subsidiary question was: *given that tax policy is discursively framed, how might counter-hegemonic discourses challenge and supplant dominant paradigms?*

This question addresses how resistance to the operation of power in the formulation of tax policy might arise and how it can be effective in creating new tax regimes.

10.3. Arguments Advanced

In chapter 3 I set out the theoretical concepts which underlie my arguments in subsequent chapters. The need for taxation arises because governing regimes (which have generally historically been in the form of states) need to raise money to finance their activities, and the only realistic way of doing this is by making a compulsory levy on its citizens, i.e. taxation, in order to avoid the 'free rider' problem. However, the notion that taxation is merely a set of objective, immutable and techno-rational rules is a serious misconception which ignores the fact that it is underpinned by many subjective choices (chapter 3.2.).

Underlying the detailed rules are policy decisions about the amount of tax revenue which must be raised and this will depend on how wide-ranging the functions of the state are to be. This is an inherently subjective decision and must be agreed through a discursive process. Similarly, the question of how much revenue is to be contributed by different groups in society and how the revenue should be spent must similarly be agreed discursively. This discursive

process is imbricated in societal power relationships, but power is not necessarily exercised in an overt manner and Lukes (2005) offers a three-dimensional model of power in which the first dimension is the overt operation of power and the second and third the more covert operation (chapter 3.3.). This model therefore provides a framework for the discussion and analysis of the more covert operation of power. Furthermore, this is not necessarily exercised hierarchically, but may operate in a capillary fashion through an assemblage of actors.

In this thesis I argue that the UK in the early 21st century characterizes a neoliberal state in which power operates covertly through the third dimension and one of the ways in which it does so is through the construction of knowledge based on neoclassical economics. However, this is not a set of immutable laws, but constructs which evolved from the late 18th century onwards which derive from a reworking of economic principles formulated by economists such as Smith (1776), Ricardo (1815), the marginal analysts, such as Jevons, Menger and Marshall, to Hayek, in the course of which economics evolved from being a branch of moral philosophy to a mathematical science based on abstract models (Landreth & Colander 2002). These models assume *inter alia* that the interests of capital should be prioritized over those of labour and that low-paid workers can be incentivized to work by paying them less, whilst high-paid workers need to be incentivized by paying them more and these assumptions underlie tax policy in the neoliberal state (chapter 3.4.).

In chapters 5 and 6 I set out the characteristic features and values of a neoliberal state and argue that these can be found in the UK, and the UK tax system in particular, in the early 21st century. However, the neoliberal state has evolved from earlier state forms and in chapter 4 I argue that tax systems have throughout history reflected the dominant power relations in society. From roughly the 12th to the 17th century the dominant state form was feudalism, which was characterised by a set of mutual social obligations between classes (Gill 2003) (chapter 4.2.). Taxation took the form of feudal dues payable by serfs to their feudal overlords and from the feudal overlords to the king and were payable simply by virtue of their relative social positions (Gill 2003). This is an early illustration of Lukes's (2005) first dimension of power, where taxation is payable simply by virtue of the authority of one party over another, for which no teleological justification was made, beyond the fact that it was ordained by God and which was backed by the potential threat of, or even actual, violence.

The Industrial Revolution of the late 18th and early 19th centuries swept away the last vestiges of feudal society, from which the liberal state evolved (chapter 4.3.). One of its central characteristics was the antagonism between the aristocracy and the bourgeoisie which was theorized by Ricardo in his rent theory (1815). The liberal state was therefore a state form which allowed this conflict to be managed and contained by allowing each group distinct spheres of influence and control. Government was dominated by the landed gentry, but the liberal state was a limited state and the government did not involve itself in areas such as the economy and the professions, in which it ceded control to the bourgeoisie. The tax system of the 19th century reflected the economic power of

the bourgeoisie and power operated through the second dimension because issues which were antithetical to their interests were ‘organized off’ the agenda and could not be seriously discussed (Daunton 2002a). The level of taxation was kept low and governments were therefore forced to rely on taxing income because after the repeal of the Corn Laws in 1846 it became politically impossible to raise significant tax revenue through the taxation of goods, a situation which lasted around 100 years (Howe 1997).

This compromise lasted until roughly the 1870s, from which time the rise of the power of organized labour saw the liberal state start to evolve into the welfarist state in which the extent of the state’s involvement in people’s day to day lives increased greatly, with the state providing education, healthcare and relief from poverty (chapter 4.4.). The tax system became highly progressive, with high marginal rates of tax which, combined with high levels of social provision, meant that there was a significant degree of wealth redistribution, particularly in the years after the establishment of the Welfare State in 1948 (Daunton 2002b) (chapter 4.5.). The rationalizing discourse for welfarism did not rely on economics, but on the need to improve the lives of workers. Initially this was for practical reasons and to forestall the threat of revolution, but later in the Welfare State there was a more ideological, socialist rationale. The welfarist state was therefore a compromise between the interests of the bourgeoisie and the working class in which the bourgeoisie financed a high level of social provision through taxation which largely benefitted the working class, in return for their position not being challenged.

The economic slow-down of the 1970s led to the post-war consensus being seriously questioned (Campbell 2009). This gave the opportunity for neoliberalism to supersede welfarism as the hegemonic ideology and in chapter 5 I demonstrated that the UK in the 21st century strongly characterizes a neoliberal state. Neoliberalism is a deliberate attempt by capital to wrest back power from labour (Harvey 2007) and the neoliberal state is an economic state in which neoclassical economics has become a hegemonic knowledge. This provides a rationalizing discourse for divorcing the economic domain from the social domain, giving priority to the former, and replacing the principle of egalitarianism with that of economic rationality (Miller & Rose 2008) (chapter 5.2.).

The twin concerns of the neoliberal state are to protect the interests of capital and to maximize the incentive of individuals to work and engage in entrepreneurial activity. Power operates through the third dimension and individuals are persuaded to ‘buy into’ the ideology through the economization of all areas of life and the fragmentation of power relationships, resulting in power being wielded by assemblages in which the state is merely one actor, but which also consists of actors such as quangos and private companies (Miller & Rose 2009).

This ideology is based on neoclassical economics and holds that the economic sphere operates according to objective, immutable and quasi-scientific laws, meaning that governments cannot govern the economy by determining policy, but that economic policy is governed by the laws of economics (Rose 1999).

The rise of neoliberalism was therefore not simply a response to the economic difficulties of the 1970s, but its antipathy to welfarism was apparent from the outset and it always had the aim of enabling capital to wrest back power from labour (Roehner 2007) (chapter 4.5.).

Since the tax systems in the feudal, liberal and welfarist states reflected the dominant values and power relationships in those societies it might be expected that the tax system in the neoliberal state in the UK in the early 21st century will similarly reflect neoliberal values. In chapter 6 I therefore demonstrated that the UK tax system has been extensively reformed since 1979 to do so (chapter 6.2.). Rates of income tax, and especially the higher rates, have been sharply reduced, which favours wealthier taxpayers. Consumption taxes, such as VAT, the burden of which falls most heavily on poorer taxpayers, have been increased and these changes have been justified through the rhetoric of incentives (Hansard 1979 & 1988) (chapter 6.3.). The rate of corporation tax has been substantially reduced in this period, and large corporations have benefitted from other tax changes, such as the exemption of foreign profits, which was justified both on the grounds of economics and compliance with EU law (Gammie 2009), both of which I argue are questionable (chapter 6.4.). Although these reforms have utilized the third dimension of power through the construction of knowledge there remains the possibility of critical incidents which expose the normally hidden operation of power and in chapter 6.5. I illustrated this by an analysis of the controversy which arose in 2008 over the abolition of the 10p tax rate.

In chapter 7 I discussed how the discourse surrounding tax simplification, and in particular the flat tax, might be a vehicle through which power may be exercised to further entrench neoliberal values in the tax system. However, despite the calls over the years for simplification (e.g. Kempster 2006) and a number of initiatives both in the UK and overseas (e.g. the Tax Law Rewrite Project) it has not proved possible to achieve significant simplification of the tax system. Similarly, proposals to introduce a flat tax (e.g. Teather 2004; Heath 2006) have not attracted significant support in the UK and other more developed countries (chapter 7.2.).

This suggests that it is not possible to use tax simplification as a rationalizing discourse for further redistributing resources from poorer to wealthier taxpayers and that this failure demonstrates that the second dimension of power, the mobilization of bias, is inadequate as the basis of a rationalizing discourse. This is because simplifying reforms must be set out in some detail, meaning that their consequences are open and transparent. Any loss in equity will therefore be apparent and where taxpayers are asked to choose between simplicity and equity, where any loss in equity impacts them directly, they will prefer an equitable system over a simple one (chapter 7.3.).

If the second dimension of power is inadequate as a rationalizing discourse to further redistribute resources in favour of wealthier taxpayers, chapter 8 discussed whether the debate over whether tax law should be based on detailed rules as at present or on more general principles, whose application to specific situations would require judicial interpretation, might be a more

successful vehicle for the exercise of power. Legal scholars (e.g. John Braithwaite 2002) have argued that principles-based legislation would produce greater certainty and that a principles-based GAAR would decrease tax avoidance. However, I argued that this debate involves the operation of the third dimension of power since uncertainty, and therefore the need for judicial discretion, is inherent in both rules and principles, but that this discretion is covert in rules whereas in principles it is overt (chapter 8.2.). The judicial discretion even in rules-based system is apparent from a number of cases in which the decision might seem surprising and contrary to the meaning of the law (chapter 8.3.).

The arguments in favour of tax avoidance rely on the principles of libertarianism and legal formalism. The former holds that the property rights of individuals are paramount and that taxation is a form of legalised confiscation. Tax avoidance therefore becomes an act of legitimate resistance against the overweening power of the state (Barker 2009). The principle of legal formalism flows from the libertarian principle and states that, if the state is to levy taxation, it must be levied according to tax law, the meaning of which is certain (Curzon 2002). This dictates that law must be interpreted in a literal manner and that, if a tax scheme is held to succeed on a literal interpretation of the legislation, it must either comply with the intentions of the legislators or, if it contravenes these intentions and the legislation is uncertain, this must be due to defective drafting (Lord Aylmerton cited in Barker 2009:233) (chapter 8.4.).

However, legal formalism ignores the fact that uncertainty in law arises not from defective drafting, but is inherent in the contested nature of language and that certainty is therefore illusory. Judges therefore have considerable discretion in interpreting legislation (James 2010) and plaintiffs and respondents similarly have discretion to advance arguments which favour them. Legal formalism can therefore become a rationalizing discourse to obscure the operation of power in using the inherent uncertainty in law to construct a desired interpretation of the law.

Whilst discretion in principles-based legislation is explicit, rather than hidden, there have been many cases where rules have been interpreted by judges so as to produce a surprising result. Sometimes the decision might be seen as merely eccentric (e.g. *Bourne v Norwich Crematorium 1967*), but, in other cases, the meaning of legislation appears to have been interpreted in a manner which enabled the judges to achieve an overriding political imperative, for example to enforce the payment of EPD or EPT as a patriotic duty to support the war effort.

In the case of rules-based legislation, the third dimension of power operates through the knowledge/power nexus to obscure the fact that discretion exists in the interpretation of law, so that decisions are viewed as the only possible ones which could ensue from the facts of the case. However, the explicit nature of discretion in principles-based legislation requires a different narrative. Unlike tax simplification proposals, which must be specific, the third dimension of power can operate through proposals for principles-based legislation because of its

lack of specificity and people may be more easily convinced that it will only be exercised in a manner which they support, i.e. to counteract tax avoidance which they view as unacceptable, and therefore consent to this. However, the *Arctic Systems Case (Jones v Garnett 2007)* is a reminder that, once judges are given the power to exercise explicit discretion, there may be no control over how it is used and therefore no recourse if a taxpayer feels aggrieved by a decision. Principles-based legislation may therefore turn out to be a double-edged sword, but, once taxpayers' eyes are opened to the potential disadvantages, it may be too late.

Furthermore, the third dimension of power may operate by creating an illusion that principles-based legislation will create greater certainty. However, general principles owe their potency to their lack of specificity and, if a number of cases are litigated or tax authorities yield to pressure to give taxpayers more certainty by issuing guidance, the decisions and guidance might transform these principles into something akin to the detailed rules they have replaced, which might well defeat the purpose of the new approach and the extra-legal nature of the guidance will also allow the third dimension of power of power to operate since there are fewer democratic safeguards and it is therefore more susceptible to lobbying (chapter 8.5.).

If chapters 3 to 8 might seem pessimistic, chapter 9 addressed the prospects of resistance to, and the overturning of, a hegemonic discourse. The economic downturn of 2008 and the revelations from 2010 onwards of agreements between HMRC large and corporate taxpayers to settle disputes on terms which

were considered to be unduly favourable to the taxpayer have made the public much more aware of and much more interested in the issue of corporate tax avoidance.

These settlements reflected the fact that HMRC has wide administrative discretion to take whatever action it sees fit in order to effectively manage the tax system (chapter 9.2.). However, in a neoliberal state the exercise of administrative discretion by HMRC in its relations with large and powerful taxpayers has become problematic because both HMRC and these taxpayers have become co-actors in an assemblage of power. This is compounded by the fact that the principle of taxpayer confidentiality should prevent details of the relationships between these taxpayers and HMRC becoming public knowledge.

Although the use of administrative discretion should not in theory become public knowledge, in practice it might do so due to accidental disclosures or whistleblowers. When it does so it might cause public disquiet if it is perceived to systemically favour powerful taxpayers who form part of the neoliberal assemblage of power and this disquiet might coalesce into resistance. The revelation that HMRC had forgiven Goldman Sachs £10m of interest was such a case and UK Uncut successfully petitioned for a judicial review. Although UK Uncut lost the review, the review proved highly embarrassing for HMRC, exposing the normally hidden operation of power, and this exposure might prove to be the first step in overturning the hegemonic neoliberal paradigm (chapter 9.3.).

In summary, in this thesis I have illustrated how Lukes's (2005) three-dimensional framework of power can be used to explicate the dominant discourses surrounding taxation in a neoliberal state. Chapters 5 and 6 have demonstrated that the neoliberal state is a new state form in which the state facilitates and serves the needs of capital and in which power does not operate in an overt, hierarchical manner, but in a covert, capillary manner through assemblages. These consist not only of the state, but of a number of actors including quangos and large corporations with the consequence that the state has ceded a substantial degree of its formal power to govern and must therefore govern in an indirect manner. The tax system has become an integral part of these technologies of indirect control and the second and third dimensions of power therefore operate through it by constructing knowledge of taxation as a techno-rational system of rules based on economics, rather than embodying any normative values.

I have also illustrated in chapter 7 through the failure to gain support for reforms to radically simplify the tax system, and in particular the flat tax, that the second dimension of power is inadequate to mobilize support for tax reforms which privilege the interests of capital and the wealthy because the consequences of these are open and transparent. I have therefore argued that in order to mobilize support the consequences of reforms must be vague, whilst containing an intuitive appeal, and that a change from a rules-based system of tax law to a principles-based system might have this potential.

10.4. Contribution Made

As I explained in chapter 1, this thesis has slightly unusual origins, since it initially arose from two papers published in 2008 and 2010 which form the basis of chapters 7 and 8. This was followed in 2013 by a paper which forms the basis of chapter 9. This means that, unlike many PhD candidates I have already been obliged to hone my arguments and writing style to a publishable standard and have experienced the rigours of the academic review process, from the satisfaction of a positive review through the exasperation of questioning whether the reviewer actually understood my paper and of struggling to work out how to address the reviewer's valid points to the realization that these have enabled me to strengthen my argument. Furthermore, I have presented drafts of these papers at a number of conferences and the feedback from colleagues has also contributed to them. The experience of publishing these papers has therefore stood me in good stead in finalizing this thesis. It has also made me better known within the epistemic community[1] and as a result I have already been asked to review several papers for journals, which has obliged me to engage with other researchers arguments in more detail.

Whilst none of the themes discussed are original, they have generally been discussed singly in isolation and in a technocratic manner (e.g. Avery Jones 1996 and Kempster 2006 in the case of tax simplification and John Braithwaite 2002 and Freedman 2004 in the case of the efficacy of rules and principles in taxation). In this thesis, through providing a rigorous, over-arching conceptual framework of power drawing on Lukes (2005), Foucault (1978 [1976], 1979

[1] A diverse range of academics and professional experts who share normative and causal beliefs and notions of validity (Haas 1992).

[1975], 1980 & 1981 [1969]) and Gramsci (1971) and a historical context, I have been able to combine these themes into a single narrative. Whilst each of these themes individually can provide a critique of the paradigm that taxation is simply a set of immutable and objective, techno-rational rules which operate according to the principles of economics, by combining them into a single narrative in this way I have shown how the tax system has evolved to further the interests and values of hegemonic groups in society and how power operates to hold the system in place. Whilst the financial crisis of 2008 has arguably exposed the fundamental flaws in the neoliberal paradigm, this knowledge still underpins the tax system and the Budget of July 2015 demonstrated that this paradigm is hegemonic.

By providing new insights into the ways in which power might operate overtly or covertly in the formulation of tax policy I have demonstrated links between the themes and the limits of and the potential of resistance to power. For example, in both chapters 8 and 9 I have shown that HMRC is no longer simply a government agency to administer and collect of tax, but has become part of the same assemblage of power which also comprises the large corporations they are charged with regulating. However, the fact that HMRC is a government agency means that they are still accountable to taxpayers as a whole through the democratic process and that their position is therefore conflicted.

If the government through HMRC wish to favour the interests of hegemonic groups it must be done covertly using Lukes's third dimension of power in order to prevent accusations of regulatory capture. This approach is evident in the

use of principles-based legislation which has the potential to severely curtail tax avoidance, but whose effect can be largely neutralized by extra-statutory guidance concerning its interpretation (chapter 8), and the manner in which administrative discretion is used to favour the interests of large corporations (chapter 9). This can be contrasted with the inability to use the second dimension of power through the tax simplification debate and proposals for a flat tax, since the consequences are too transparent (chapter 7).

However, even the covert, third-dimensional exercise of power cannot be guaranteed to be successful. HMRC and the government remain vulnerable to the power of grass-roots resistance. There are therefore periodically critical incidents which expose the normally hidden operation of power and this thesis has therefore provided a link between two very different examples of popular resistance, the controversy surrounding the abolition of the 10p tax rate in 2008 (chapter 6) and the judicial review obtained by UK Uncut over the waiving of interest payable by Goldman Sachs (chapter 9).

This thesis is largely conceptual and not empirical, but given that taxation is constantly evolving it might providing a starting point and theoretical framework for empirical research by me or other members of the academic community. In particular, there is scope for developing the work on the flaws in the economic paradigm of taxation, particularly if these become even more apparent in the years to come and any case studies of failures might well lend themselves to empirical analysis. My thesis has also been UK-focussed and there may be opportunities to empirically compare the UK experience with other countries,

such as Australia. In particular, it is far too early to know whether the curtailment of the remittance basis might be the start of a process of attrition leading to its eventual abolition, whether the GAAR might be effective in curtailing tax avoidance or whether the success of UK Uncut and others in raising awareness of tax and tax avoidance might lead to more fundamental changes to the UK tax system. These issues will develop and evolve over the coming years which will offer opportunities for further research.

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