The Leap of Faith:
The Historical and Institutional Roots of Tax Compliance

Robert Schumann Centre Workshop
October 8-10, 2015

Most people who study tax compliance begin with the question: Why do some people evade? Implicitly, we have the model in our head that taxes buy services and public goods and that anyone who 'cheats' the system is unwilling to pay their fair share. We tend to look at societies that have low levels of tax compliance as if they have done something wrong.

This workshop begins from a somewhat different perspective. We begin with the observation that high levels of taxation and tax compliance are quite rare – both historically and cross nationally. Indeed, in only a very small number of societies, and only relatively recently, have citizens been willing to pay significant shares of their income or wealth to governments or rulers. One might think that tax compliance in Greece or Italy, for example, is low compared to the rest of Western Europe. But it is obvious that tax compliance, and tax revenues (these are not the same things, but of course they are connected) are actually quite high in these countries when compared to the rest of the world. They are also high compared to *any country* a hundred years ago.[1]

This workshop is motivated by the question: How did modern states build these extensive and comprehensive tax systems and manage to motivate their citizens to actually pay these taxes? If we can gain purchase on this question, we may be able to answer a second question: Why have some countries been much more successful in this regard than others? The idea of this workshop is to examine specific cases with an eye to the comparative analyses. No one scholar can hope to be an expert on the history and structure tax/revenue/compliance systems in many countries. Instead, the hope here is that we learn from the multiple – and quite different – narratives presented in the workshop.

To willingly pay taxes requires a "Leap of Faith." When a citizen gives money to the government, she/he is paying for something that offers indirect benefits at best. At the same time, for governments to provide the public goods necessary to create the kind of trust implied here, they need money. Lots of money. In short, to do the kinds of things that citizens' are willing to pay for, states need revenues that most citizens should be reluctant to pay. It might seem reasonable for a Swede or a Dane to be willing to pay for the excellent public services they receive today, just as it might seem reasonable that Romanians would be less willing to pay for services that they feel they do not receive. In short, if we take a static view, we may be able to explain the current situation. But this static view cannot help us understand how or why Sweden, or Romania, or the United States for that matter, are now on such different places with respect to the relationship between the citizens, their states and the taxes that they pay.

Each paper in this workshop will examine a different aspect of this phenomenon in a specific country. The countries directly examined here are: Sweden, England, Italy, the US and Romania. Ideally, we will have two papers on each country: One paper should examine the deeper historical roots when these modernizing (democratizing?) states

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began to develop the kinds of modern and extensive tax systems that transformed these societies. What was the connection between the early revenue and administrative systems these countries developed and the eventual structure of these states themselves? A second paper will examine the more contemporary periods as each of these states began to develop far more extensive and invasive tax systems and administrations.[2] In most of the countries we examine here, tax revenues went from somewhere around 5 or 10 percent of (a much smaller) GDP in 1910 to between 30 and 50 percent of (a much larger) GDP by the second half of the century. Government revenues skyrocketed not only because new taxes were developed as these economies modernized, but also because citizens' were willing to pay those taxes.

It is common in the economics literature to argue that, as tax burdens increase, the incentives to evade taxes rise proportionally.[3] But one can scarcely avoid noticing that the opposite seems to be true. How do these different, quite expensive, states continue to get their subjects to bear these quite heavy burdens, and why (contrary to the expectations of modern economic theory) does it seem that those countries with the heaviest burdens seem to have citizens who are the most compliant? Why, have some of these states been so much less successful in this regard?

The workshop is funded by the ERC grant, "Willing to Pay? Testing Institutionalist Theories with Experiments," which is an ongoing project in which we are using laboratory and survey experiments to test for national variations in behavior regarding taxes and public goods. The ERC project is founded on the hope that we can bring the insights of historical/comparative analysis to help explain some of the variation we discover in the laboratory setting. At the same time, it is our hope that we will be able to test the ideas and theories generated through historical analysis with our experiments. The October 2015 workshop will thus be followed by larger conference (March 17-19) that will explicitly bring experimentalists and historical institutionalists to the same table. We will then test the hypothesis that we can really talk to one another.

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May 6, 2015

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[1] No one has very good comparable estimates of the size of tax evasion in different countries, but according to the most widely cited work on the size of the 'Shadow Economies' around the world Schneider and Klingmar (2004) the 'shadow economy' in average OECD country is approximately 15% of GDP, whereas in developing countries of Africa it is 41%, Asia 26%, Latin America 41%, and 38% in E. European and Asian 'transition' economies.

[2] I will be in contact with each of you individually to discuss your particular contribution. Ideally, Julia can coordinate a time when we can talk on skype.

[3] Indeed, classical economists' estimates of tax evasion use tax burdens and/or marginal tax rates as a variable to estimate the size of the tax gap. In other words, they assume that high taxes cause increased evasion.

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