The Right Politics of Income Taxation

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# The Right Politics of Income Taxation

PhD Dissertation

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## Table of Contents

Acknowledgements
Chapter 1. Introduction171.1 Developing the puzzle201.2 The main argument251.3 The approach and plan of the dissertation32
Chapter 2. Clarification of main concepts372.1 Studying income taxation372.2 What taxes are: the policy instruments422.3 What taxes do: understanding their functions and trade-offs482.4 Ways to cut income taxes51
Chapter 3. Right parties and income taxation
<ul> <li>3.1 Definition of Right parties</li></ul>
Chapter 4. The income tax strategies of the Right77
<ul> <li>4.1 The politico-economic constraints of the Right</li></ul>
thresholds
Chapter 5. Using aggregated policy effects to study the impact of
tax institutions1075.1 A new class of income tax measures1085.2 Separating the effects of rates and thresholds1155.3 An illustration of the rate and threshold effect1175.4 Descriptive evidence and two approaches to study macro policy trends1215.5 Countries that lower rates lower income taxes the most1285.6 Few tax brackets inhibit long-term rate-based cuts1325.7 The lacking long-term policy impact of progressivity1355.8 Conclusion139
Chapter 6. The Right effect on major income tax reforms
6.1 The frequency of major income tax reforms

6.6 Does Right government predict the incidence of rate-based or	
threshold-based reforms?	169
6.7 Conclusion	171
Chapter 7. Income tax reforms in Denmark, the United Kingd	om
and the United States	
7.1 Choosing specific reforms to study	
7.2 Strategy of analysis	
7.3 Denmark	
7.3.1 Background of reform	181
7.3.2 The political process	182
7.3.3 The content of reform	
7.3.4 Summary	191
7.4 United States	191
7.4.1 Background of reform	191
7.4.2 The political process	
7.4.3 The content of reform	196
7.4.4 Summary	
7.5 United Kingdom	202
7.5.1 A budgetary overview	202
7.5.2 The Conservative-LibDem coalition	205
7.5.3 Conservative rule amidst Brexit turmoil	206
7.5.4 The 2012 Budget – misjudging the unpopularity of top-end r	ate
cuts	
7.5.5 The 2018 Budget – threshold cuts saved by unexpected wind:	fall 213
7.5.6 Summary	
7.6 Conclusion	
Chapter 8. Visibility of rates and threshold limits	217
8.1 The incomplete knowledge of voters' grasp of tax instruments	
8.2 A survey experiment on rates and threshold limits	223
8.3 Exploring the visibility and feasibility of instrument choice	229
8.4 Low visibility discourage partisan conflict	237
8.5 Ideology associated with conflicting causal beliefs – not just confl	licting
goals	
8.6 Can we generalize the Danish reform case?	243
8.7 Conclusion	245
Chapter 9. Concluding remarks	
9.1 The Right dilemma between simplicity and room to maneuver	
9.2 Instrument choice: looking beyond rates and thresholds	
9.3 Future reform paths	
A	
Annexes	
Anney A.H. Exemple of income to a policy data of recorded baths of	
Annex A III. Example of income tax policy data as recorded by the OE Annex A III. Issues related to the construction of novel policy measure	ND202
Annex A.111. Issues related to the construction of novel policy measured	res263

A.III.I. Rate and threshold effects when j > 1 A.III.II. Rate and threshold effects when j changes from one year to the	263
next	265
Annex A.IV. Example of the calculated policy effects	268
Annex A.V. Descriptives of the major reforms events	269
Annex A.VI. Presentation of the variable used in the Chapter 6 models	272
Annex A.VII. Regression results for the predictions income tax reform	
events	275
Annex A.VIII. Revenue impact of the Tax Cuts and Jobs Act	.281
Annex A.IX. Full survey questionnaire	282
Annex A.X. Control variables used in survey	296
Annex A.XI. Balance tables for survey	297
Annex A.XII. Survey results and supplementary analyses	300
Annex A.XIII. Marginal income tax rate across the top brackets	308
English summary	309
Dansk resume	313
References	.317

#### List of tables

<b>Table 1</b> Summary of the Right's policy strategy in different income tax regimes32
<b>Table 2</b> Population of income tax strategies and their impact on tax rates
<b>Table 3</b> Right seat share as share of all cabinet parties' seat shares inparliament, 2000-2018
<b>Table 4</b> Recent macro-quantiative studies on the impact of partisanship onincome tax policies
<b>Table 5</b> Citizens' views on changing the size of government, lowering taxes vis-à-vis spending more
<b>Table 6</b> Theoretical expectations of the Right's strategies in different taxregimes
Table 7 Overview of the article search strategy for the individual case studies 180
<b>Table 8</b> Proposed changes to income taxation rules in connection to the 2009         tax reform
<b>Table 9</b> Tax brackets in the Internal Revenue Code for single filers (2018) 197
<b>Table 10</b> Overview of UK budget decisions with ain impact on the income taxschedule204
<b>Table 11</b> Income tax brackets in the UK expressed as a percentage of average earnings
<b>Table 12</b> Overview of the OECD policy data for the United Kingdom, 2000-20182020
<b>Table 13</b> Policy scenario with three rates and two thresholds         264
<b>Table 14</b> Policy scenario with a reduction in thresholds
<b>Table 15</b> Policy scenario with a rise in thresholds
<b>Table 16</b> Calculated rate and threshold effects for the United Kingdom, 2000-2018
Table 17 Full list of major reform events across the OECD, 2001-2018
<b>Table 18</b> Variable used in the Chapter 6 models
<b>Table 19</b> Summary statistics for the variables included in the Chapter 6         models       273
<b>Table 20</b> Correlation matrix for the variables included in the Chapter 6         models       274
<b>Table 21</b> Logistical models of major income tax reforms (cuts)
<b>Table 22</b> Logistical models of major income tax reforms (hikes)

<b>Table 23</b> Logistical models of major income tax reforms (cuts) – extremereform cases278
<b>Table 24</b> Logistical models of major income tax reforms (cuts) – interactiverelationships
<b>Table 25</b> Logistical models of rate- and threshold-based major income taxreforms (cuts)
<b>Table 26</b> Estimated 10-year revenue impact of the Tax Cuts and Job Acts
Table 27 Control variables used in the survey analyses    296
<b>Table 28</b> Balance check across treatment groups for the threshold experiment. 297
<b>Table 29</b> Balance check across treatment groups for the rate experiment
Table 30    Sample size across treatment groups    299
Table 31 Successful guess rate for each proposal (logit)       300
<b>Table 32</b> Successful guess rate for each proposal by the order of the experiments (logit)
Table 33 Predictors of successful guesses (logit)
Table 34    Estimated support to the proposals (logit)
<b>Table 35</b> Estimated support to the proposals by partisan messenger (logit) 305
Table 36    Estimated likelihood of the proposals (logit)    306
Table 37 Estimated opposition to the proposals (logit)    307
<b>Table 38</b> Marginal income tax rates for the highest and next-highest taxbrackets across the OECD

### List of figures

<b>Figure 1</b> Marginal tax rates on the highest incomes in the five major OECD economies, 1900-201920
Figure 2 Development of income tax schedules across OECD countries, 2000-2018
<b>Figure 3</b> Conceptual overview of the personal income tax and its constitutive elements
<b>Figure 4</b> Placement of the top income tax bracket expressed as ratio of average wages, 2018
Figure 5 Stylized example of the income tax schedule with three tax bracket53
<b>Figure 6</b> Sketched summary of instrument qualities with respect to visibility and political feasibility95
<b>Figure 7</b> Bivariate relationship between the number of income tax bracket in 2000 and 2018
<b>Figure 8</b> Income tax institutions – progressivity and the number of tax brackets – across the OECD100
<b>Figure 9</b> Number of new tax policy measures (personal income tax) as counted by IMF
Figure 10 The United Kingdom income tax schedule in 2000 and 2018114
Figure 11 Stylized example of the rates and threshold effects 118
<b>Figure 12</b> Histograms of the yearly change in tax liabilities stemming from rates and thresholds
<b>Figure 13</b> Counts of policy changes in tax rates and thresholds across the OECD
<b>Figure 14</b> Aggregated scores on rates and thresholds changes in tax liabilities from 2001 to 2018
Figure 15 Aggregated joint effect plotted against rates and thresholds scores131
<b>Figure 16</b> The number of tax brackets plotted against the aggregated effects rates across countries
<b>Figure 17</b> Comparison of joint aggregated effects of low- and high-income taxpayers
Figure 18 A flow chart of income tax reform events across the OECD 143
<b>Figure 19</b> The distribution of major income tax reforms (total reforms, cuts and hikes)146
<b>Figure 20</b> Effect size of the Right dummy for predictions of major tax reforms (cuts and hikes)160

<b>Figure 21</b> Effect size of the Right dummy at levels of tax brackets and tax progressivity (proxy)
<b>Figure 22</b> Effect size of the Right dummy for predictions of rate- and threshold-based reforms
<b>Figure 23</b> Overview of periods with Right head of government in Denmark, the UK, and the US176
Figure 24 Article count on 'tax reforms' – 2009 DK reform. Week 23 2008 through weak 26 2009
Figure 25 Article count on 'tax reform' – 2017 US reform. Week 52 2016 through week 4 2018194
Figure 26 The United States income tax schedule in 2017 and 2018
Figure 27 Brief overview of the survey structure
Figure 28       Successful identification of the true causal interpretation for each         proposal       231
Figure 29 Estimated support for each treatment
<b>Figure 30</b> Estimated opposition for each treatment moderated by voters' causal grasp
<b>Figure 31</b> Average marginal effects of Left-Right self-placement on support for treatments
<b>Figure 32</b> Share of voters holding specific causal beliefs as conditioned by Left-Right self-placement
<b>Figure 33</b> The number of tax brackets and the placement of the top income tax bracket's threshold
Figure 34 General government deficit as percentage of GDP, 2000-2018 253
<b>Figure 35</b> Bivariate relationship between progressivity and top statutory tax rate on income
Figure 36 Stylized example of the corrected rates and threshold effects
Figure 37 Visualisation of the major reform events across the OECD

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## Chapter 1. Introduction

It has been over 200 years since Benjamin Franklin wrote his famous remark that nothing in this world 'can be said to be certain, except death and taxes'. We may easily brush aside this century-old admonition, though its lesson remains imperative for our type of research: if one wishes to study politics whole-heartedly, one has to take a look at taxes.

Political scientists at large have not exactly embraced this topic. In fact, scholars have been noticeably aloof from taxation and the political process that surrounds it (Steinmo 1998). The more one thinks of it, the more surprising it becomes. There is no shortage of tax references going back to the classics of our field. The Eastonian understanding of politics as 'the authoritative allocation of values' (Easton 1953) assumes the presence of 'values' (or 'revenue' to use a different term) to be spent or redistributed among citizens. State building theorists have long acknowledged taxation as one of the main activities of the state and a necessary condition for everything else it does (see Schumpeter 1918/1954, Tilly 1985, Levi 1988, Tilly 1990).<sup>1</sup>

This 'tax dearth' is too evident in much of the newer comparative research, most notably the welfare state tradition from which I come. Taxes *should* be a focal point in this literature. The post-war expansion of the Western welfare states saw a steep increase in social spending and tax revenue alike, inextricably linked as the latter provided the means necessary to fuel the former. Scholars, however, chose to focus on the spending-side drivers. Whereas the study of how the (welfare) state distributes benefits to its citizens boasts a sophisticated, varied and contested research tradition, our understanding of the whole revenue half of the equation is much less developed<sup>2</sup> (see e.g. Peters 1979, Steinmo 1993, Ganghof 2006a, Prasad and Deng 2009 for similar assessments). Hence, we lack positive theory that gets to the bottom of what it is political actors struggle over and how they do so when it comes to taxes.

The uneven attention between the two sides extends to the 'new age' Piersonian literature on welfare state dismantling (see Pierson 1994, 1996, 1998, 2001). At its core is the discussion of retrenchment and the political leeway (or lack thereof) for scaling back the expensive welfare state. The tax question is relegated, in turn, to a scope condition. The size of the state, in terms

<sup>&</sup>lt;sup>1</sup> The modern state is essentially a 'tax state', as Schumpeter (1918/1954) has it.

<sup>&</sup>lt;sup>2</sup> The discrepancy has led one study to conclude that social scientists at this point 'know much more about the *giving* than the *taking*' (Prasad and Deng 2009: 431).

of what it is able to generate in revenue, is seen as a constant, a fiscal equilibrium dictated by countervailing politico-economic pressures, and not a variable policymakers of any cloth can meaningfully change (Jensen 2019: 128-129).<sup>3</sup> Once you rely on such a proposition, it is easy to forget that taxes serve other functions than merely raising revenue. Yet, to claim that political actors have little interest or say in the politics that governs the tax-side of the welfare state is taking the argument too far, in my opinion. The one-sided focus tends to disregard reform-minded politicians who care passionately about taxation, in particular those on the right side of the political aisle who may be especially critical of the high-level revenue systems we have built and seek to change them for the better in their eyes.

Needless to say, I struggle with this truncated view of the welfare and tax question.<sup>4</sup> I do so not just because of the conceptual deficiency, but due to an empirical one as well. What was perhaps the true starting point of my dissertation was the failure to link the notion of 'welfare state resiliency' promoted by Pierson and his likes to another under-the-radar story of public policy: that tax reforms occur frequently in contemporary policymaking. The share of revenue raised by the welfare states may have plateaued over the last 30 to 40 years, but the policies needed to generate such revenue have certainly not been shielded from intervention. For example, it has not gone unnoticed that income tax systems across the OECD changed immensely during the 1980s with a spectacular reduction in their tax progressivity (Steinmo 2003). **Figure 1** shows the decline in the average top marginal tax rate on earned income

<sup>&</sup>lt;sup>3</sup> The one-eyed focus is just as puzzling if one wishes to evaluate not just spending and revenue figures but other key policy outcomes inherent to the welfare state. The promotion of equality is one of such goal. At the aggregate level, the structure of tax rules and legislation – how *much* revenue the state raises and from *whom* it is taken – is one of the main channels through which states can affect the redistribution of income and wealth from rich to poor, and hence the national level of inequality (OECD 2008b). One cannot fully describe the net effects of the welfare state without also taking this component into account.

<sup>&</sup>lt;sup>4</sup> Historically, research on taxation has largely been left to economists in our neighboring research fields. The intent of my dissertation is certainly not to neglect their contributions (Hakelberg and Seelkopf 2021b). Yet, as noted by Steinmo (1998), they tend to have different analytical foci than most political scientists. Economists, it seems, take normative positions and are explicitly interested in assessing what the government ought to do to 'fix' or improve the tax system according to key societal goals, often through an 'efficiency lens'. Political scientists, instead, tend to focus on explaining *what* governments actually do, and why they do it. There is certainly room for both approaches.

across the five largest OECD economies from 72% in 1978 to 48% in 1988,5 a 24 percentage point drop in just 10 years. The two spearheads of what was dubbed 'the conservative revolution', Reagan in the United States and Thatcher in the United Kingdom, oversaw even steeper cuts: the US marginal tax rates on income fell from 70% to 28% during this period, while the UK rates fell from 98% (!) to 40%.<sup>6</sup> These sweeping reforms were part of a broader trend all across the OECD, where top marginal rates were scaled down, the number of tax brackets was reduced, and tax bases were broadened by reducing loopholes and exemptions (see Steinmo 2003, OECD 2011b). One can reasonably argue that the tax policy was in fact the leading edge in this new political tide and the biggest victory of the invigorated political Right<sup>7</sup>; they may have changed the redistributive nature of the tax systems much more than they ever succeeded in scaling back the welfare state. The reduction in tax progressivity has since contributed to the massive rise in income inequality across the Western world since the 1980s (Pikettey 2013, 2020a).8 Considering how much ink has been spilled over the 'new politics' of the spending-side, I am baffled how little has been said about the huge transformation on the tax-side of the welfare state, mentioned at most as a side note in existing literature.

<sup>&</sup>lt;sup>5</sup> As evident from **Figure 1**, the average marginal rate peaked at 84 percent (in 1947) in the immediate post-war years.

<sup>&</sup>lt;sup>6</sup> The 98% was a composite rate to some extent, as the top rate of income tax was 83% at its highest. A surcharge of 15% raised the top rate on investment income to that level.

<sup>&</sup>lt;sup>7</sup> For a more comprehensive analysis of these changes, see Blyth (2003).

<sup>&</sup>lt;sup>8</sup> The inequality story is not the main focus of this dissertation, however.

**Figure 1** Marginal tax rates on the highest incomes in the five major OECD economies, 1900-2019



Source: Pikettey (2020b).

**Notes:** The figure shows the average marginal income tax on the highest incomes in the five largest OECD economies as of present: France, Germany, Japan, the United Kingdom, and the United States.

### 1.1 Developing the puzzle

The institutionalist may point to the ensuing period of relative stability as a token of tax policy returning to normalcy: after the massive transformation of income tax systems in the 1980s, marginal tax rates have exhibited less fluctuations from the 1990s to this day, as per **Figure 1**. It was perhaps the lone 'punctuated equilibrium' to borrow an agenda-setting term (see Baumgartner and Jones 2009). My interpretation is different, though, as this stability claim loses much of its credibility when one begins to scratch the surface.<sup>9</sup> Even after the 1980s, tax reforms are still widespread (OECD 2016, 2017, 2018, 2019d, 2020). Take my native country of Denmark as an example, where policymakers have adopted no less than five significant tax reforms since the year 2000 (Statistics-Denmark 2016), always accompanied by intense political scrutiny. The same goes for the US where both recent Republican presidents made tax

<sup>&</sup>lt;sup>9</sup> My intent is not to say that the tax-side, if defined by stability rather than change, does not deserved further scholarly investigation into the causes of such pattern of stability. Rather, my goal is to establish the fairest picture of how much change the tax policy has undergone, before developing good theoretical explanations to this pattern.

reform their legislative top priority and, subsequently, enacted major revisions of the income tax code. Within the last few years, countries such as Australia, Austria, the Netherlands, and Sweden have all reformed one or more key policy parameters pertaining to their income tax schedules (OECD 2020). Yet, the top marginal tax rate, the policy indicator that perhaps gets the easiest attention, has not been the locus of all these reforms. A wider array of tax instruments have been adjusted, instead. In fact, how these reforms can be crafted to promote unequal outcomes and conceal adverse effects on the 'average' taxpayer has been debated in the existing literature (see e.g. Bartels 2005, Hacker and Pierson 2005).

The tax story of recent years seems, therefore, to have reached a crossroads. We know there is plenty of policy changes going on beyond the top marginal tax rate. However, we have yet to land on one convincing, overarching story of 21st-century tax policy. I can easily understand why it is the case after studying the policy field for the duration of my PhD. One needs only to take a brief look at the available policy data to get a glimpse of just how diverse these country-level stories are. The OECD started systematically tracking legislative income tax data of its member states from 2000 onwards, and they are the best vardsticks at our disposal for comparative analysis. From what we see in Figure 2, they tell a story of immense spatial and temporal variance, even after the 1980s. The figure shows the income tax schedules across 21 often compared OECD countries in 2000 and in 2018, respectively. Intuitively, the slope reads as the rate of personal income taxation a taxpayer must pay in each country given their income level. Personal income levels are, thus, shown on the x-axis, and the marginal rate paid in percentages is on the y-axis. The sharp jumps in rates signal that the taxpayer with a marginal increase in income exceeds their current tax threshold and enters a new tax bracket.<sup>10</sup>

**Figure 2** is *the* key figure of the dissertation in many ways. A source of great inspiration and frustration at the same time, it contains a staggering amount of policy information and numerous puzzles in need of further dissection. I will unpack some of them here. What jumps out first is of course the great variety in policy legacies across the OECD countries. It is clear when we inspect their respective starting points of this period (the grey schedules).<sup>11</sup>

<sup>&</sup>lt;sup>10</sup> The threshold values are standardized according to the average wages in each country (in 2000) to ensure the fairest spatial and temporal comparisons.

<sup>&</sup>lt;sup>11</sup> Much of it reflects different legacies of 'tax regimes' discussed at length in a rich literature of its own. However, it also captures that countries had different reform tracks prior to 2000, the demarcation year of my analysis. Some countries had already reformed their income taxes quite significantly at this point (e.g. the United Kingdom), while others had been slower or more unwilling to reform.



Figure 2 Development of income tax schedules across OECD countries, 2000-2018

Source: Own visualization based on OECD (2019b).

**Notes:** The grey line represents the 2000 income tax schedule in the respective country, while the dashed, black line is the 2018 schedule. The amount of taxable income is expressed as percentage of the average wage in 2000. To ensure comparability, the *x*-axis is curbed to four times average wages. It means the figure neglects policy changes designated taxpayers at the very top of the income distribution. The statutory rate includes only central government rates in the PIT (personal income tax) rate schedule, excluding any sub-central rates as well as compulsory surtaxes. Germany is excluded, as it has a 'special', progressive income tax, where the marginal rate increases monotonically with increasing taxable income (OECD 2011b: 30-31).

In 2000, all countries relied on some shape of progressive income taxation,<sup>12</sup> i.e. a two-tier rate system as a minimum. Yet, the shape of progressivity varied a lot, as the 'steepness' of the schedule carries a direct link to the redistributive nature of the system. Generally, countries with a vertically steep schedule have a large degree of redistribution built into their income taxes, as the marginal tax rates are much higher on the higher than on the lower incomes. Here, the rich end up paving the much higher share relatively speaking. In contrast, countries with a flatter curve that features more moderate 'jumps' from one bracket to the next are less redistributive, all things equal. Compare here the neighboring countries of Austria and Switzerland to see the difference. While the former schedule exhibits a steep rise in the marginal rate paid, even for incomes below the average wage level, the slope of the Swiss schedule rises much more modestly from the bottom to the top of the income scale. On the whole, there are huge discrepancies between marginal tax rates across countries: at the bottom, in the middle and at the top of the income scale, and at what income levels they kick in.<sup>13</sup>

The figure shows, second, large policy differences in the number of tax brackets. Intuitively, these read as the number of 'steps' across the tax schedules. Tax brackets are one of the key defining features of a country's tax structure. Their number carries a direct link to policy complexity, as I argue throughout the dissertation. One can think of the perhaps simplest tax system conceivable, a flat-rate tax for all taxpayers, and contrast this to the most complex imaginable, one in which all taxpayers have a unique tax rate according to their positions in the income distribution (and perhaps a myriad of other 'horizontal characteristics'). In practice, the number of brackets is usually higher than one and lower than ten, as per **Figure 2**. It helps to compare Ireland and New Zealand to get an understanding of the variation. They are two countries with relatively similar profiles when it comes to progressivity. In the baseline year, their schedules featured two and four brackets, respectively. The Irish jump from the base rate (22%) to the top rate (44%) is much steeper

<sup>&</sup>lt;sup>12</sup> Simply understood as an income tax schedule where 'the marginal rate increases with pre-tax income' (Hillman 2008: 674). In theory, one could easily think of a 'regressive' schedule with decreasing marginal rates, though this is rarely the case in practice.

<sup>&</sup>lt;sup>13</sup> Here is a good time to remind the reader that the figure only displays the central government rates, hereby excluding sub-central rates, making one-to-one cross-country comparisons misleading in some cases. For example, Denmark had a combined (representative) local and regional tax rate of 32.1% in 2000, not shown, on top of the central government tax rate shown here, making actual tax burdens much heavier than they immediately appear from the figure.

than New Zealand's, which has smaller continuous increases in the marginal rates (15%, 21%, 33%, and 39%). It is tempting to think of progressivity, discussed before, as a direct function of the number of brackets, yet as I elaborate in the subsequent chapters, there may be (but there is not necessarily) a strong link between the two.

I have touched upon the cross-sectional variance, but the puzzles obviously extend to the temporal dimension as well. Figure 2 definitively dispels the notion that tax policies have stood still in recent years: income tax rules are not the same in 2018 as they were in 2000.14 In most countries, there is a pretty strong resemblance between the policy in the baseline year and 18 years after; the reverse finding would be much more surprising. But the figure reveals significant country variation in the *size* of policy change. One group of countries - Portugal, Switzerland, and the United Kingdom to name some have experienced relatively minor changes in the income tax schedule on the surface; the grey and the dashed lines are virtually congruent.<sup>15</sup> Contrast this pattern of stability to other countries – Australia, Finland, the Netherlands, and Spain – which have seen larger overhauls of their tax systems. In all these cases, the slopes of the dashed lines are less steep (i.e. less progressive) compared to their starting points: marginal tax rates have been severely cut. It is clear that both groups, the incremental and the major reformers, contain a diverse set of countries, and some broad cluster typology cannot stand alone as a good explainer of this policy variation. Neither can theory that puts its main explanatory power on common functional pressures as causes of policy change, e.g. globalization effects and tax competition.<sup>16</sup>

Finally, **Figure 2** shows not only a different size of policy change but in different *ways* as well. The notion of different paths to tax reforms is not prominent in the literature, but it is key to the argument I forward in the dissertation. The figure reveals two models of reform: one centered on (reducing) tax *rates*, and one centered on (raising) *thresholds* limits, e.g. on when to pay higher marginal tax rates. The models work along the different axes: changes in the rates shift the horizontal lines up- and downwards depending on whether policymakers decide to raise or lower rates, while changing the

<sup>&</sup>lt;sup>14</sup> Otherwise, the dashed line (2018) would have overlaid the grey line (2000).

<sup>&</sup>lt;sup>15</sup> Yet even here, tax policies have not been shielded from significant reform, as my in-depth case studies of the UK policy in **Chapter 7** reveal.

<sup>&</sup>lt;sup>16</sup> I acknowledge, of course, that the main focus in the dissertation is on the income tax system and not other forms of taxes where such functional explanations may be more fruitful. I regard theory on the impact of international competition is well-suited for explaining the relatively uniform change in, for example, corporate tax policies across the OECD (Swank and Steinmo 2002, Swank 2016).

thresholds corresponds to horizontal shifts, either left or right. Marginal rates have been reduced significantly in some of the aforementioned reform cases such as the Netherlands and Spain. But take Denmark and Sweden as different examples then. Perhaps not as visually intuitive, these countries have seen substantial policy change, as raising thresholds on tax brackets has exempted a large group of taxpayers around the average wage from paying the top marginal rate, which would have applied to them in the absence of reform.<sup>17</sup> Lowering rates and raising thresholds are distinct ways of cutting taxes: both are associated with loss of governmental revenue, all things equal, leaving more earned income in the hands of the taxpayer. Yet, the few scientists who study income tax policy seldom distinguish between the two modes. I must mention, too, that **Figure 2** shows empirical nuance, as most countries have altered both their rates and thresholds, when comparing 2000 to 2018. It is not a hard proposition of either-or. The main point is that it is not straightforward, from the figure alone, to explain why some countries have chosen a predominantly rate-based reform track, while others have used thresholds as the main vehicle of policy change. Against this backdrop, the overall research question, which I seek to address in the dissertation, can be stated as follows:

What is the scope of (income) tax policy reform in the OECD from 2000 onwards? And why do we observe different types of reform?

### 1.2 The main argument

The diverging pattern sets the stage for the dissertation, as it constitutes a genuine policy puzzle without easy and obvious answers. On the one hand, it calls for an even closer look at the content of policy, the dependent variable, that goes deeper than the superficial findings we can derive from **Figure 2**. Pursuing the question in depth automatically enables us to formulate better answers for the major blank spots left by the spending-biased welfare literature: we get a clearer picture of contemporary tax policy. As we go into uncharted scholarly territory, it requires, first, thoughtful considerations of the relevant parameters to study which tie into a conceptional discussion of what is the actual object of conflict when political actors struggle over taxation. I can start by addressing what the politics of taxation is *not*. Political fights today do not concern the design of the whole institutional structure that governs the tax

<sup>&</sup>lt;sup>17</sup> The income distribution among taxpayers is obviously not constant over time, making these examples are stylized. We would need to know the specifics of the distribution in each year to draw the precise conclusion. I will return to the relationship between threshold limits and income levels throughout the dissertation.

code, i.e. whether we should have an income tax at all, or whether the tax system should be progressive in its scheme or not.<sup>18</sup> Systems are not scrapped by reformers; they are patchworks of new policies layered over existing ones. My point here is not that institutional legacies are unimportant to study, as I will stubbornly claim the opposite. They are vital for shaping actors' incentives and attention to a specific component of the tax scheme in need of reform from a population of virtually endless possible components to target. But it is then important to be precise with what we deem the relevant 'tax institutions'. I elaborate on this point later.

My position is to look at the marginal changes in tax policy outputs, which carries two key implications. First, studying changes speaks to the importance of the status quo, the existing tax rules, as the reference point from which political actors – elites and voters alike – evaluate new politics. It is in line with what the broad reform literature within the welfare state tradition advocates. Second, and more important, a focus on policies allows me to dig into the choice of instruments: which specific tax rules are policymakers most (or least) likely to target with their reforms? It is a novel question. Some conceptual building blocks have been presented in the relatively scarce tax literature, as the political (i.e. electoral) support towards new forms of taxation is thought to depend on their concentration on specific and resourceful groups as well as their visibility (see e.g. Martin and Gabay 2018). If the goal is to avoid backlash, the view is that policymakers must raise revenue, assumed to be their key policy goal, relying on dispersed, invisible (or 'indirect') forms of taxation. It makes broad-based consumption taxes more attractive than say income taxes. What has never been considered, however, is how these concepts travel to the level of the individual policy instruments, which are what policymakers target in real-life politics. They do not change income taxes per se; they change specific policy components within the income tax code.

A main conclusion from the dissertation, inspired directly by **Figure 2**, is that tax instruments are not interchangeable substitutes. When it comes to the income tax schedule, the cornerstone of the tax system, reforming the tax *rate* is simply not the same as reforming the tax *threshold*. We know this in part

<sup>&</sup>lt;sup>18</sup> I am in line with Beramendi and Rehm's (2015) observation that the fundamentals of the tax system tend to be based on compromises reached decades ago, and contemporary policymaking tends to be about marginal changes within a generally accepted institutional framework. In that sense, the core parameters of the tax system are exogenously determined. This view implies by no means a denial of the possibility of tax policies changing over time. However, systems generally move slowly and change only rapidly as a result of major political compromises at specific historical moments.

from our neighboring field of economics. Their theory teaches us that the rate is the more powerful tool of the two for affecting equality and efficiency, two key tax goals besides raising revenue, fostering the strongest behavioral responses in terms of work, investment and savings decisions at the micro-level (Milasi and Waldmann 2018).<sup>19</sup> Yet, there needs not to be a perfect relationship between the *real* and *perceived* policy effects. In fact, politics can enlarge such 'objective' economic impact assessments. What matters in this realm is not always the 'true' economic effects of new policy measures; perceptions and causal beliefs are at least as vital, in my view. Policymakers may draw inspiration for their causal arguments to promote a certain tax policy from economists, but they are not obliged to stick to them and use them in a fair manner. They may downplay or ignore the unfavorable effects of their preferred tax solutions, and they may exaggerate the favorable ones or downright make up convenient arguments that are beyond the backing of economic theory. I intend to show throughout the dissertation that the struggle over taxation is in many ways a struggle over conflicting causal beliefs at its core. Supporters and opponents of new tax rules and legislation do not merely disagree on which policy outcomes (i.e. growth, equality, and revenue) are important to give more or less political weight; they seem to disagree on what these policy outcomes *consist of* on a more ontological level. I build evidence to show that these partisan differences extend to the level of elite actors in the three case countries I study, and survey evidence to show that it applies to groupings at the voter level as well.

I argue, further, that there is an added political layer to this discussion that extends down to the instrumental level. My argument is in line the visibility proposition advanced by Pierson (1994), as the rate is the more visible way of cutting taxes (or raising them for the matter). The rate is the fundamental feature of the tax code, as it figures front and center on monthly paychecks. A taxpayer will, if they pay slight attention, notice whether the statutory rate has decreased, and it is easy to understand how this change carries immediate consequences for their (improved) standard of living. Decisions on tax thresholds, at what income level a certain tax rate kicks in, are more difficult to comprehend, even though the impact may be substantial. Lowering or raising the threshold for the top marginal tax rate in a given country will, for example, alter the tax burden of high-income earners, even if the rate itself remains constant. Yet, such terms as 'shrinking the tax base' or 'raising the threshold' are not as intuitively translated into how it impacts the living standards of individual taxpayers. In the dissertation, I show that it is not merely a theoretical proposition. Evidence from a novel survey experiment, fielded among Danish

<sup>&</sup>lt;sup>19</sup> At least, it is the standard answer in the mainstream neoclassic growth models.

voters, estimates that at most half of the electorate are able to get this causal mechanism right; i.e. to correctly link the rising threshold to lower tax burdens for the affected taxpayer.<sup>20</sup> In my view, it spills over into policymaking, as reform-eager politicians will likely resort to ways of changing taxation that augment their connection to more popular policy tools while distorting or hiding their connection to unpopular ones, echoing another of Pierson's (1994, 1996) core claims. The rate should then only be cut if it is not a widely unpopular idea to do so.

The distinction between rates and thresholds enables me to shed light on the 'what has happened' question at the macro-level. I show, using novel tax indicators I construct from OECD policy data, that virtually all countries have pursued a policy track with the intent to cut the level of income taxes over the last 20 years, rather than to raise it.<sup>21</sup> The pattern makes sense, because policymakers need to actively cut income taxes to prevent tax hikes by default, i.e. bracket creep. In that sense, the status quo favor those who want higher tax revenue. But while cutting has been the norm, the means have differed significantly. The countries fall into the two predominant reform tracks: one group has relied mainly on rate-driven reform, most notably by lowering tax rates for the middle-to-high income earners, while the other group has enacted threshold-driven reform, raising tax bracket limits more than inflation during the same period. There is some temporal variance to this story, defined by the Financial Crisis. From 2000 to 2010, we witnessed a period clearly devoted to tax-cutting policies across the OECD. The picture then reversed in the five recovery years from 2010 to 2015, where we saw a number of reforms aimed at increasing income taxes, facilitated by the need for fiscal consolidation in the crisis aftermath. Rates, especially, were raised in countries such as Iceland, Ireland, Norway, the Netherlands, and Portugal during this time. From 2015, tax-cutting reforms seem to have re-emerged on the agenda, although at a slower pace than in the early 2000s.<sup>22</sup>

These macro results evoke natural interest in the 'who' and 'why' questions: who has been the dominant political agent responsible for the changes we see, and why have they pursued the different paths? My claim is that we need to look no further than to those partisan actors that already populate our

<sup>&</sup>lt;sup>20</sup> I show that the numbers are around 70% for changes in the marginal tax rate.

<sup>&</sup>lt;sup>21</sup> Counting major reforms of the income tax code, the number of tax-cutting event outweigh the number of tax-hiking ones more than 2:1, as we shall see in **Chapter 6**.

<sup>&</sup>lt;sup>22</sup> I do not present a strong, monocausal explanation as to why the reform pace across countries has slowed in recent years, although I will provide some speculative answers in the round-up discussion of the dissertation.

theories on the welfare state, yet are keen on neglecting the tax issue. Then, it should come as little surprise that the political Right is the proactive force pushing to change the status quo of income taxation, i.e. to cut taxes as we see as the predominant trend. The Right may have come to appreciate and defend certain policy areas of the welfare state (Jensen 2014) and are not all-out welfare sceptics. But it leaves them with plenty of political space to go after the distribution of the tax burdens that go into funding social policies. Cutting income taxes seems like the silver bullet for Right parties, as it fulfills two broad policy goals at once. It accommodates, first, the material interests of their core voters, the middle-to-high income voters, and hence has a strong political pleasing effect. The point is sufficient in itself to understand why the Right is so committed to the tax question. But Right parties with strong ideological convictions are also more likely to put emphasis on the positive economic consequences of income tax cuts. If they hold the 'Right' causal beliefs, they are perhaps more willing to accept policy that increases in inequality and lowers revenue yields as the necessary evils to promote employment and economic growth.

My view of this relationship is straightforward. We need to understand Right parties to understand the dynamics of income tax policies. If they can get away with it, they always prefer to cut income taxes, and they prefer to cut tax rates rather than expand thresholds due to the greater growth-stimulating effects. Such beliefs are hardwired. There is an asterisk to this story, though, as the Right elites are not mere free agents when holding political power and the opportunity to change things. They face obvious fiscal challenges, as they cannot set the income tax rules they want without, at least, first considering the budgetary ramifications of such decisions. If they are willing to bear those costs, then comes the politics of it all: slashing tax rates may be popular among core voters and likeminded stakeholders but is likely to spark significant opposition from the political Left and the public opinion, which do not share similar beliefs about the virtues of tax cuts. And since the immediate causal impact of cutting the marginal tax rates is not easy to blur, it leaves the Right in a potentially vulnerable spot. These are factors that may restrain them from carelessly pushing their first-order preference. However, I establish that there are plenty of case examples as well as macro-statistical evidence that suggest the Right's willingness to go after lower rates. It invites the question whether we can say something systematic about *when* the Right pursues different sets of policy strategies.

This is where institutions come into play. My dissertation goes to great lengths to show that just how the Right tries to cut income taxes is contingent upon the configuration of the tax system. My interpretation is thus a familiar one for scholars of partisan politics: it is a struggle between actors of conflicting causal convictions set in a specific institutional framework. The contention implies that we cannot derive a fixed set of policy strategies adopted by the Right that travels smoothly across space and time. Their reference point is always the status quo. One can, of course, highlight a host of institutional rules and settings that leave a certain mark on policy, but based on the in-depth study of the policy area, I wish to point to the two key domestic tax institutions, already mentioned, that shape the political room to maneuver to a significant degree: (1) the number of tax brackets in the tax code, and (2) the level of progressivity built into the schedule.

The two affect the policy process in different ways. The number of tax brackets, first, guides instrument choice. The extreme (theoretical) case is again the simplest tax system conceivable, the one flat-rate tax for all. Here, the Right, or the Left for that matter, struggles to find fiscally sound ways to cut tax rates on targeted voter groups, such as the middle class or top income earners, as the prime instrument available is *the* rate. In the second-most simple system – the two-tier one – the Right may target either the basic rate paid by all taxpayers, the top rate paid by the richer, or re-define the threshold limit that demarcates the higher tax bracket. The two latter are the obvious policy targets of the Right. Though the Right may prefer to cut the top rate, the visibility of such a move attracts significant blame attribution, dampening the inclination to go this route. When the number of tax brackets is low, the politics of income taxation shifts its focus to the threshold, the less visible component. The main struggle then becomes when the tax brackets should set in,<sup>23</sup> while politics centered on rates are rarer instances.

Contrast instead the simplest systems to those with four, five, or six tax brackets (high B). Here, the number of policy parameters augments considerably, leaving reform-willing politicians with more instruments to 'work with'. Since the brackets are now more narrowly defined, reforms of either rates or thresholds – especially for the higher rates – should also be less costly from a revenue standpoint. The choice of policy is also less confined to the thresholds because it is now possible to fine-tune a single bracket's rate level without the

 $<sup>^{23}</sup>$  For the Right especially, the discussion on whether the top rate targets the 'right' segments of taxpayers is a less tough sell than discussions on whether the richest should pay a reduced marginal tax on all of their incomes. The location of the threshold is also key. If located much closer to – or even below – the median wage earner, raising it becomes much easier to justify than if the top rate kicks in at very high wage levels.

risk of changing the redistributive profile of the whole system. Hence, the politics of income taxation tends to focus on both rates and thresholds in a context of high B.<sup>24</sup>

The progressivity of the schedule, in turn, guides the policy priorities of the Right, i.e. where on the income distribution their focus lies. In highly progressive tax systems (e.g. the United Kingdom and the United States), where tax burdens fall disproportionally on the wealthier income groups, the Right should muster a strong push for cutting income taxes on these particular income brackets. Due to the steepness of the tax schedule found here, Right parties are better positioned to *sell* political rhetoric framing the high marginal taxes at the top end as the chief structural problem of the income tax code.

In low progressivity settings (such as in Denmark), the picture becomes murkier. Here, the Right is not only concerned with how the steep tax slope affects work incentives among the highest paid wage earners. Easing tax burdens on low-to-middle income groups is given more equal priority due to their relatively high marginal tax rates, which is the result of the much flatter tax schedule. Whether or not taxes discourage labor market entry for fringe groups<sup>25</sup> is, as I show, a major structural issue in tax discussions (often in the form of 'work versus welfare' trade-offs). The Right's tax focus is therefore broader. I find that the Right fights for more widespread tax cuts, for the poorer and the richer alike. Yet, I also argue that the Right's tax strategy is generally more 'defensive' in these settings, because their political opponent – the Left – has a more valid claim of getting richer income groups to pay a larger share of the tax burden. Here, what may actually be the true token of success is whether the Right can function as a 'safeguard' against even higher income taxes.

**Table 1** sums up my findings on the Right's tax strategies in a neat twoby-two table. Another way to summarize the theory on institutions is I expect the strategies to be the 'cleanest' in settings with many brackets and high progressivity, where the Right should be less constrained and motivated to pursue

<sup>&</sup>lt;sup>24</sup> Another attractive strategy by the Right, in the high B context, is to push for 'simplification' of the tax schedule, i.e. decrease the number of tax brackets. It involves either abolishing or merging existing tax brackets, which requires definition of both a new rate and threshold for the merged bracket. It creates a high degree of policy uncertainty, which the Right can exploit to push otherwise unpopular policy propositions behind the need for simpler tax rules. If *B* is relatively low to begin with, then discussing how to further simplify the schedule with even fewer brackets is a much less effective strategy.

<sup>&</sup>lt;sup>25</sup> Referring to low income wage earners, the unemployed, or other groups receiving social assistance.

tax cuts for the high income earners. In contrast, the strategies should be the most confined in low B/low P settings, as the Right needs to split their policy focus across different income groups and cut taxes via thresholds rather than rates. I generally find this to be the case empirically. Both when studying the long-term macro findings across the OECD, but grounded with case study evidence covering three of the four corners of **Table 1**. The locus of income tax cuts have been much more geared towards thresholds by the Right in the low B cases of Denmark and the United Kingdom, whereas Republicans in the United States have more overtly attempted to slash marginal tax rates. At the same time, the cuts enacted by the Right in the UK and the US have been much more skewed towards the top income groups over the last 20 years than in Denmark where the strategy pursued by the Right parties has been more broad-based.

		Progressivity of the tax schedule	
		Low	High
Number of brackets	Low	Thresholds cuts at the bottom and at the top <b>(Denmark)</b>	Threshold cuts at the top (United Kingdom)
	High	Mix of cuts at the bottom and at the top	Mix of cuts at the top (United States)

Table 1 Summary of the Right's policy strategy in different income tax regimes

### 1.3 The approach and plan of the dissertation

It is clear from the summary of the argument that I make some relatively strong assumptions about the qualities of tax instruments and how they translate into the process of policymaking. In addition, the strategies pursued by the Right are complex, since they differ across institutional contexts. It means that there is no single way to test the argument convincingly. The empirical approach of the dissertation is therefore to combine different methods and data sources, so-called triangulation, which hopefully in concert will persuade the reader of the argument's validity.

The dissertation takes on the challenge of drafting a novel theoretical framework on how to study income tax policy dynamics while drawing on a lot of the good concepts we know already from the extensive partisan and public policy literature. As a first step, **Chapter 2** introduces the main concepts of the rate and the threshold. Income tax systems are – needless to say – incred-ible complex legal entities, but resolves around two fundamental questions: (1) *who* or *what* should be taxed, and (2) *how much*? For policymakers, it translates into defining the tax bases, usually in the form of tax brackets when

discussing income taxation, and setting the respective rate(s). The chapter also lays out the three main functions of tax instruments and defines in what specific ways politicians can seek to alter income tax rules.

**Chapter 3** turns the attention to the key political agent within this domain, i.e. those on the Right. They are defined as the Liberal and Conservatives parties, who are united in their fight for lower income taxes. Existing theoretical accounts leave them with little political agency to reform. My starting point is, instead, that the Right elites are motivated by strong causal beliefs about the virtuous effects of income tax cuts. Their inclination to prefer lower taxes over, say, more social spending is hardwired and something worthwhile to pursue despite economic costs.

Then, **Chapter 4** ties the theoretical framework together. I argue here that Right parties, ideally, wish to cut marginal income tax rates as much as possible, especially at the top end of the income scale where the associated revenue costs are low. But the political price to do so can be too high, as it is a visible and politically contentious move. Altering tax thresholds is, in turn, associated with much more confusion in terms of the causal impact. If the cost of successfully raising threshold is to abandon the first-choice ambition of cutting tax rates, this may be a reasonable trade-off for some Right elites. Further, the chapter expands on the two institutional factors (see **Table 1**) and how they shape the political room to maneuver.

**Chapter 5** is the first of the empirical chapters. Here, I specifically look at the variations in policy trends at the aggregated level. Because we do not already have indicators that pick up the crucial distinction between rates and threshold, I point to a way forward and construct novel ones based on OECD's comparative Tax Database. These measures leverage the information we can obtain from studying the yearly changes that occur in countries' formal income tax laws. Using them, I study first the aggregated policy developments for each instrument type over the last 20 years. I flesh out that countries have taken quite different paths policy-wise, and that institutions partly explain these varying patterns. Most notably, countries in the low B group, i.e. those with tax schedules that have relatively few tax brackets, do not experience any long-term cuts in tax rates, while there is much larger variation, and hence different policy paths to take, within the high B cluster.

Having established the broad trends, **Chapter 6** takes the same data on and examines the year-to-year instances of policy reform. It enables us to build statistical models of predictions to determine what augments the chance of major tax reform in a given country. Here, I obviously look at the impact of Right governments and find that they – on average – are a large driver of taxcutting reforms across the OECD, especially if the reform contains mainly cuts to the tax rates rather than changes to tax thresholds. It comes with a key asterisk, though, since the Right only increases the likelihood of reforms that target the high-income segments, not for those lowest on the income scale. I show the effect is more pronounced in settings of high tax progressivity, i.e. where the rich already carry the relatively larger share of tax burdens.

**Chapter** 7 attempts to unpack the details of the Right's tax strategy and to do so, I turn to case studies of Denmark, the United Kingdom, and the United States. The three were chosen as aligning on the different ends on the institutional variables and thus hold diverse policy legacies. Case studies allow a much better view into the concrete mechanisms of change that underlie the macro findings. Using specific tax reforms enacted by the Right as my starting point, I find differences in their specific policy design as well as their tax rhetoric that are large enough to substantiate the validity of my institutional claim.

In **Chapter 8**, I switch gears and test the key assumption made in the dissertation on the 'visibility mechanism'; the notion that voters have a better causal grasp of rates as compared to thresholds. I put the proposition to a novel test by fielding two survey experiments among a sample of Danish voters with the goal of tapping into how proficient voters are at identifying the 'true' causal change of tax reforms done via either instrument type. The tax evaluated is the top marginal income tax rate in Denmark ("topskatten"), and I find that instrument choice matters significantly for voters' visibility as well as support for reform: rates *are* easier to comprehend than thresholds to the tune of at least 10 percentage points. Further, the results show that the causal confusion is strongly linked to political indifference on the part of voters, as they do not oppose even radical reform proposals to cut or raise income taxes if they do not properly understand how they impact. It is not even the case for voters with a strong Left-Right identification.

**Chapter 9** provides the main conclusions and I try to unfold the implications of the dissertation I draw distinctions and similarities to the study of spending-side policies and argue, among other things, that the impact of the policy *default* has a lot say when trying to explain why parties on the Left and Right are incentivized differently towards changing policy: the Right must actively cut income taxes to avoid bracket creep, while the Left must make sure that the generosity of social provisions is not dismantled in real terms. I discuss then the perhaps hidden tax trade-off of the Right that becomes evident from the work in this dissertation: the conflict between taxing as simply as they possibly can, eliminating tax brackets and exemptions, while on the other hand keeping the maneuverability of having a lot of these policy instruments at their disposal for future reforms. Though the rate and the threshold are the core instruments when it comes to income taxation, I also discuss the avenue for including the concept of tax exemptions even more in future research as well as considering what role social security contributions play in the design of income tax policies. I end with a discussion of the prospects for (further) income tax reforms over the coming years.
# Chapter 2. Clarification of main concepts

In the following, I define the main concepts used in the dissertation: the income tax policy and its main policy components – the rate and the threshold.

In theory, a dissertation centered on the tax issue could have gone down a number of different paths. I explain my reasons for focusing on income taxation, which I see as distinct from other forms of taxes: it is at the center stage of political and economic discussions and, hence, the natural domain to study when seeking to establish, first, the central policy trends of recent years, and, second, how actors struggle over the policy design. How to study it in comparative manner is not given, however. As a tool to reduce the vast complexities that are inherent to this domain, I argue that we need to distinguish between two key components to describe policy variance in a meaningful sense. I will look at tax *rates* and *thresholds* as separate entities. They are the two cruxes of income taxation. The *tax bracket* is then what fuses the two.

After going over what (income) taxes *are*, I look at what taxes *do*, i.e. their policy effects. Tax instruments are used to achieve three, often conflicting, policy goals: raise revenue, redistribute, and incentivize economic activity. I argue that it is important to take all three into account in order to develop a nuanced understanding of why partisan actors, such as the Right, wish to change the policy status quo. Finally, I define the population of possible reform strategies: which instruments can policymakers fine-tune, exactly, if they seeks to cut income taxes. I examine in depth how each measure affects the tax liability of the taxpayer in the form of the *average* and the *marginal* tax paid.

### 2.1 Studying income taxation

A key starting issue for a dissertation devoted to taxation is to establish *which* tax policy to study. It is clear from what has be written already that there are a number of different ways to proceed. Both a concept clarification and a theoretical demarcation are therefore warranted.

Before defining the term 'tax policy', let us first clarify the term 'tax' for good measure. According to OECD's working definition, on which I rely, taxes are 'compulsory, unrequited payments to the government' (Messere, et al. 2003: 7, OECD 2021c). They are unrequited in the sense that individual tax-payers do not receive social benefits and services from the state in proportion to the taxes they pay (ibid.). Taxes and 'welfare' are in that sense orthogonal.

The element of compulsory relates, of course, to the consequence of non-compliance, as the failure to pay a tax, along with evasion and avoidance are punishable by law.

The first function of the tax is to generate revenue to the state. Modern states thus stand on two feet: their public expenditure system and their tax system, which constitute the 'fiscal system'. They two are inextricably linked, as states depend on revenue as much as on expenditure (Peters 1991).<sup>26</sup> As such, taxes are not the only source of public revenue but do provide the vast majority of resources available to the state, particularly in advanced industrial democracies (Barnes 2018: 2).27 So before policymakers can decide on spending, they have to identify, collect and administer taxes within the scope of their country's tax system. Here, rules have to be defined on multiple levels. The tax system contains not only the narrow legal rules and norms regarding 'who must pay' taxes and 'how much' (Steinmo 1993: 1), it provides regulations on how to collect and administer taxes, and it includes specific institutions that are responsible for defining tax norms and their implementation (Kiser and Karceski 2017). In a nutshell, the tax system is an institutional structure combining a 'tax policy' and its administration. It is important to distinguish between the two sets of tasks, since the dissertation focuses on the politics of determining the former, not on administration and collection.<sup>28</sup> Gauging what is a 'good' tax administration is a different undertaking altogether.

Having established how the tax systems align within the greater fiscal system of the state, we can now dig deeper into the notion of the 'tax policy' itself and its constitutive entities. Here, we dig into a conceptual layer that contains all the objects that can be taxed, as seen in **Figure 3**. The tax policy is thus the mix and aggregation of different forms of taxation that come in different shapes and sizes. The four main domestic taxes are income taxes<sup>29</sup>, indirect

<sup>&</sup>lt;sup>26</sup> It echoes Justice Oliver Wendell Holmes' often-cited remark that 'taxes are what we pay for a civilized society'.

<sup>&</sup>lt;sup>27</sup> Tax revenues are distinct from other sources used to finance state activities, most notably *rents* stemming from state control over key economic resources (e.g. oil, minerals, or marine resources). *Loans*, or *fiscal deficits* to use a different label, are of course another key source of potential revenue and an important residual category to include, as I show in the later chapters.

<sup>&</sup>lt;sup>28</sup> I allow, of course, administrative matters to shine, insofar as they are direct or indirect causes of the tax policy, i.e. if policymakers decide to change policies specifically to make them easier to administrate. Through my in-depth work on income tax policies, I find this is rarely the prevailing motivation of reform.

<sup>&</sup>lt;sup>29</sup> Income taxes are often further split into *personal* and *corporate* components and studied as such to mirror their distinction within countries' tax codes.

taxes on goods and services, taxes on property and inheritance, and social security contributions (SSC) (Barnes 2018: 3). Together, they make up over 95% of tax revenues collected in the OECD (OECD 2021d). Social security taxation is perhaps the odd one among the four, at least according to the common understanding of a tax. Typically, they are levied on payroll and are thus a tax on labor income (though often framed as a 'contribution'), with a certain percentage of the tax split between employer and employee. The counter-argument would hence be that SSCs and income taxes cannot reasonably be separated in practice.<sup>30</sup> But the 'unrequited' feature of our tax definition is generally not met here, as the contribution typically grants access to more earmarked, contribution-based entitlements.

Figure 3 Conceptual overview of the personal income tax and its constitutive elements



**Notes:** In 2017, the OECD averages for revenue share for each tax type was: 23.9% for personal income; 9.3% for corporate profits; 32.4% on indirect taxes; 5.8% for property and inheritance taxes; and 26.0% for social security contributions.

One common way to categorize the four is based on the condition of their impact, i.e. to distinguish between 'direct' and 'indirect' taxes. Direct taxes are levied on the tax object directly (e.g. the income earner), while indirect taxes are extracted in a more hidden manner. Classic examples of the latter are value-added taxes, excises on goods and services, and to some extent the

<sup>&</sup>lt;sup>30</sup> The OCED often presents the so-called 'tax wedge' as one measure of the extent to which the tax system discourages employment. The wedge is thus a composite measure that includes personal income taxes, social security contributions, as well as direct payroll taxes for the few countries that have them.

aforementioned SSCs if withheld and extracted at the source. A lot of comparative scholars continue to rely on this binary classification to explain fiscal illusion: indirect taxes are per definition less visible to taxpayers, thus allowing policymakers to tax and raise revenue with less political resistance (see e.g. Wilensky 2002, Sausgruber and Tyran 2005). However, if this was a good guide to understanding the issue of visibility and tax consent, it meshes poorly with the patterns of tax protests we have witnessed for the last 30 years, as one recent study by Martin and Gabay (2018) suggests. The authors demonstrate, using a novel dataset on tax revolts covering 20 OECD democracies, that indirect and supposedly invisible taxes on trade and consumption have proven the most politically contentious, especially when they are concentrated on specific consumer groups or industries (ibid.). Although it is one study, its findings should push us to sharpen our thinking about which qualities make different forms of taxation more or less feasible. It does so in two ways that align with the spirit of this dissertation. First, it directs us to look a lot closer at the politics involved on how to tax. I side with Barnes' (2018: 14) similar assessment of the issue, as she hit the nail on the head: 'the political saliency of different types of taxation is better seen as an outcome of the processes of tax politics – and one in need of explanation - than a set of natural and immutable facts.' I humbly believe the findings of the dissertation are a good first step in this direction. Second, the study by Martin and Gabay (2018) trains us to think critically about what should be the proper unit of analysis when studying tax policy. Their findings guided my work in the initial phases of the project and later to push a main contention of the dissertation: that the (lack of) visibility of tax measures is not only tied to forms of taxation but also to specific tax instruments *within* the boundary of each of the different tax types.

Of the four domestic taxes, I decided, for several reasons, to focus on personal income taxation.<sup>31</sup> For one, it reflects a pragmatic choice of constraint. All taxes are not alike in the same way that all forms of social spending are not. Hence, I consider it a near-impossible feat to capture the huge complexity governing dissimilar tax types in one, unified framework on taxes.<sup>32</sup> Less is certainly more. One could have easily decided to do a monograph that studies the

<sup>&</sup>lt;sup>31</sup> I demarcate them as taxes levied on income stemming from wages, social transfers (e.g. pensions, security cash benefits) and the like, as long as they are liable to income taxation. They are, in essence, the tax objects that make up the *gross* income of individual taxpayers. Taxation on capital gains, properties, wealth and inheritance does not fit under this description.

<sup>&</sup>lt;sup>32</sup> In a similar vein, we do not have one unified theory on 'welfare' or 'social spending' that tackles all complexities related to each spending area of the welfare state, which we know include vastly different policy drivers.

other main tax types in depth (e.g. the VAT or social security contributions). The latter would have aligned with another recent call from Barnes (2018: 14) to move 'beyond the politics of income taxation' to build a broader understanding of the politics of the tax system. While I sure recognize the need for further investigation into such taxes, I do not think our knowledge about the income tax is set in stone either.

Income taxation is the natural focal point to me. It is front and center of tax systems in all advanced democracies and in virtually all cases one of the largest single sources of state revenue<sup>33</sup> (OECD 2021d). In that respect, it meets a clear relevance criterion when the goal is to develop a comparative theory of tax policy. Second, income taxes attract a lot of public scrutiny. Virtually all citizens become acquainted with them as wage earners and are consequently thought to hold strong opinions on their own tax burden.<sup>34</sup> Further, a number of recent studies on tax preferences suggest that voters have relatively clear views on the ideal setup of the income tax schedule and whether current income tax policies should be made more or less progressive compared to the status quo (see e.g. Barnes 2015, Ballard-Rosa, et al. 2016, Roosma, et al. 2016, Berens and Gelepithis 2018). Other accounts like to emphasize the complex workings of the income tax schedule and claim that voters, although clear on principles, suffer from cognitive biases when they evaluate specific policy proposals. They seem misinformed and have a weak understanding of which, and how much, taxes they pay (Sears and Citrin 1985, Roberts, et al. 1994, Bartels 2005). All in all, it makes income taxation an intriguing domain for studying the link between how reforms are crafted by policymakers and presented to the public and the degree of support from taxpayers. Further, what has become abundantly clear through my empirical work is that income tax, not other forms of taxation, is the beef when politicians discuss major tax reform. It is not that other tax types cannot play a role in these reform talks, but they are more often than not the side-story; they can, for example, be the alternative revenue source needed to lift income tax burdens, the main reform goal to begin with.

<sup>&</sup>lt;sup>33</sup> According to the OECD, revenue stemming from personal income taxation comprised between 19 (Portugal) and 54 percent (Denmark) of all tax revenues in 2018 among the 21 mature OECD countries on which my cross-national analyses are based.

<sup>&</sup>lt;sup>34</sup> On a pure anecdotal level, when I reveal to family, friends and acquaintances that I am writing a PhD on taxation politics, the attention virtually always turns to 'problems' related to the income tax code, and disappointment naturally ensues when I dismiss that I have the authority to ease their individual tax burdens.

Finally, personal income taxes tie directly into the redistributive conflict of the welfare state, the political fight over which has been meticulously examined. What is special about income taxes is that the tax objects are so clearly defined according to income levels, usually in the form of tax brackets.<sup>35</sup> It structures a clear alignment of the material interests of bounded income groups. And it links to the partisan actors, as there is no way around the income taxation question for those who are interested in redistributive outcomes. As I show in **Chapter** 7, parties' key tax initiatives aim, more often than not, at changing income tax rules. It is easy to take a clear stance on the redistribution issue via income tax proposals that target a specific segment on the income scale (e.g. the proposal to either increase or decrease marginal tax rates on high- or low-income earners).

Summing up, the combination of large-scale revenues involved, the vested interest by taxpayers, the locus of most major tax reforms, and the innate redistributive conflict should only augment the political conflict over policy design.

### 2.2 What taxes are: the policy instruments

Over what is it then, precisely, political actors struggle when it comes to income taxation? There are, of course, different levels at which conflicts can unfold. At the most aggregate one, politics can revolve around the broadest policy outcome: what should be the proper level of income taxes in society, understood as the revenue intake of the state, and the related issue on policy dynamics; should the current revenue level be lowered or raised? The next obvious step is then to look at the distribution of these taxes, i.e. which income groups should carry what loads. The two are, unquestionably, important parameters to study due to their effects on key economic outcomes, as I elaborate in **Section 2.3**, so existing research has pivoted, for good reasons, on these dimensions, often referred to as (1) 'levels' and (2) 'progressivity' (see e.g. Barnes 2015, Beramendi and Rehm 2015).<sup>36</sup> In theory, these parameters can be set orthogonally. One can easily imagine a nice two-by-two table of outcomes: the

<sup>35</sup> Contrast this to, for example, welfare benefits which may be conditioned on income but often also on more complicated 'horizontal' characteristics, such as employment status, age, or dependent children to name a few (Barnes 2015: 58).
<sup>36</sup> Levels refer to the overall amount of taxes levied on individuals and households – in other words the *absolute* level of tax burdens. Progressivity refers to the distribution of the tax burden – that is the *relative* share – across income groups.

low/high *level* case combined with the low/high *progressivity* case. In practice, they exhibit a strong negative correlation across countries (Hertel-Fernandez and Martin 2018), as laid out in **Chapter 3**.

Politics is not just a struggle over outcomes, though. This coarse take on politics reveals little about how an actor wants to achieve their preferred policy outcomes, e.g. higher income tax revenue or greater economic equality in society. Politicians must use specific policy instruments that generate the desired results, and conflict over such are often where the true political disagreements arise. In my view, we need to dig deeper into the structure of the income tax code to properly address this perspective.

Everyone who has studied taxation knows it is not an easy task; real-life tax structures are painstakingly complex to comprehend, not just for the average citizen but for field experts as well.<sup>37</sup> The intuition behind the tax code, however, is a simple enough idea in the abstract. The basic task of policymakers is to set the rules that decide which rate of income tax the taxpayer must pay at a given level of income. If we take them in reverse order, they cover the questions 'who' must pay and 'how much'. Separating the two has at least helped structure my way of thinking about the policy options available, since it parcels out the two core choices at the level of policymakers: decisions on (1) tax *rates*, and on (2) tax *bases*. As I rely on the terminology for the remainder of the dissertation, let us first dwell on their definitions. The tax rate is perhaps the most intuitive to the reader, and it is, put simply, the ratio (usually expressed as a percentage) at which a taxpayer is taxed.<sup>38</sup> A tax rate of 20% thus means that 20% of what is being taxed is payable in income taxation. The

<sup>&</sup>lt;sup>37</sup> Albert Einstein was famously quoted as saying that 'the hardest thing to understand in the world is the income tax." My humble guess as to why taxation in general and income taxation specifically have been left alone by students of public policy is due to this complexity, as it is not intuitively obvious how to attack the question. It took a serious, dedicated effort on my part to derive the distilled concepts I present here.

<sup>&</sup>lt;sup>38</sup> There are several ways to present a tax rate. The two most common are the *average* (or effective) rate and the *marginal* rate. The average rate is the ratio of the total amount of taxes paid relative to the total tax base, expressed as a percentage. With a proportional tax, the tax rate is fixed, and the average tax rate equals this rate. In the case of multiple tax brackets, the average rate typically increases with higher taxable income through tax brackets, asymptoting to the top tax rate paid by the taxpayer. The marginal rate, in turn, is the tax rate on (additional) income set at a higher rate for incomes above a designated higher bracket threshold. It can be expressed mathematically as  $\frac{\Delta TL}{\Delta TI}$  where TL is the total tax liability, and TI is total income. Alternatively,  $\frac{ML}{MI}$  where ML is the *marginal* tax liability, and MI the marginal income.

tax base is perhaps a bit trickier to grasp. It represents the object or the amount liable to taxation (such as income or wealth) and to which the tax rate applies (OECD 2021b). It is often referred to as the 'taxable income'. So far so good.

The simplest tax code conceivable, barring complete abolishment of all income taxation, is the 'flat tax', i.e. income is taxed at the same rate over the full range of possible incomes. The average and the marginal tax rate would be the same. For example, with a flat tax rate of 10%, a person with €10,000 of taxable income would pay €1,000 in taxes, and a person with €50,000 of taxable income would pay €5,000 in taxes. Also simple enough.

The strict flat rate system remains an ideal type, though, as tax bases are usually diversified in two important fashions. First, we rely on progressive income taxes, as noted, which is often ensured through the creation of multiple tax brackets that link a specific rate to a specific tax base. A tax bracket thus refers to a range of income subject to a certain income tax rate. Each bracket has a lower and upper threshold amount, delimiting the bracket. It means when we are referring to the 'tax base' as the generic concept, we are, in practice, talking of the threshold values that govern which subset of an income is liable to the specific tax rate. I prefer, therefore, to use the term 'thresholds' to be as concise as possible when I refer to the different tax bases that are created by the bracket structure.

The progressivity of income taxes is ensured, as the additional brackets apply only to taxpayers with ever-higher incomes: lower incomes fall into tax brackets with relatively low rates, while those with higher earnings (also) fall into brackets with higher rates. Let us revisit the example from before for illustration. If we add a new bracket – a 20% rate starting at  $\pounds 25,000$  – to the same baseline as above, the higher income ( $\pounds 50,000$ ) would still pay the 10% rate on the first  $\pounds 25,000$  of income but is now taxed with a marginal rate of 20% on the remaining  $\pounds 25,000$ , resulting in a total tax bill of  $\pounds 7,500.^{39}$  The person earning  $\pounds 10,000$  is, in turn, unaffected by the new tax bracket, since their taxable income is below its lower threshold. In theory, one could as easily imagine a *regressive* bracket structure in which the rate decreases as the amount subject to taxation increases. However, it is very difficult to find real-life examples, perhaps since it violates an 'equal-sacrifice principle' (Hillman 2008: 679).<sup>40</sup> Another look at **Figure 2** (from **Chapter 1**) confirms the progressive structures across the OECD; the income tax 'staircase' is progressively

<sup>&</sup>lt;sup>39</sup> The tax liability (TL) is calculated as follows: TL = 0.10 \* €25,000 + 0.20 \* (€50,000-€25,000) = €7,500.

<sup>&</sup>lt;sup>40</sup> The equal-sacrifice principle dates to John Stuart Mill and holds that the utility loss from paying taxes should be (roughly) the same for everyone, regardless of their

climbing in all cases, rather than having the marginal rates falling with rising incomes. But there is still a sizable variation in both the number of tax brackets and their thresholds. One example of this pertains to the placement of the top income tax bracket, shown in Figure 4, i.e. when taxpayers earning the highest incomes enter the bracket with the highest marginal rate in their respective countries. In **Figure 4**, the lower thresholds for the top income bracket have been standardized according to country-specific average wages (AW) to ensure comparability. The differences are staggering comparing the bottom and the top. In three countries – Luxembourg, Ireland, and Belgium – this income tax bracket takes off on taxable incomes below average wages, while it hovers around the AW in Iceland, New Zealand, and Denmark. For other countries, the bracket starts only for taxable incomes many times the amount of the average wages: 6.4 times the AW in Germany, 8 to 10 times in United States, Switzerland, and Japan, and finally, a stunning 23 times in Austria.<sup>41</sup> It illustrates just one of the ways that tax bases differ significantly from country to country.

The second major way to modify tax bases involves tax exemptions, i.e. the removal of a tax liability that would have otherwise been imposed. They come in many shapes, forms and names, but they generally fall into one of two categories: *allowances* and *credits*. Both reduce the tax bill but in different manners. Allowances (or *deductions*) reduce the amount of income the individual pays taxes on, which takes us to a core distinction between 'income' and 'taxable income'. Taxpayers are thus allowed to subtract the relevant deductions from their income before calculating how much taxes they owe. A credit is, instead, a dollar-for-dollar reduction in taxes owed *after* the tax liability is calculated.

income level. The principle takes into account the diminishing marginal utility of income whereby constant (or decreasing) marginal tax rates impose smaller marginal *sacrifices* in lost utility on high-income individuals (Hillman 2008: 679). Think of it this way: to a person who earns  $\pounds$ 1,000,000 a year, paying  $\pounds$ 10,000 in taxation will make very little difference in their life, while it will make a big difference to a person earning only  $\pounds$ 30,000 a year.

<sup>&</sup>lt;sup>41</sup> The average wages in Austria were €43,731 in 2018, and the top income tax bracket commenced, first, at the threshold value of €1,000,000, from where one pays a 55 percent rate on the subset of income above. The next-highest bracket was the 50 percent rate, paid on taxable income in the range from €90,000 to €1,000,000.

# **Figure 4** Placement of the top income tax bracket expressed as ratio of average wages, 2018



Source: Own calculations based on OECD (2019b).

Though the concepts of allowance and tax credit are relatively simple constructs, they are also main drivers of legal complexity. Allowances and credits can, first of all, be either universal or specific to certain classes (e.g. those with work income, union membership, and/or dependent children). The notion of *tax expenditure*, a major topic in American public policy literature, fits under this description (Howard 1997, Hacker 2002, Mettler 2011; see Morel, et al. 2018 for a broader discussion on the concept). The complexity of the income tax code increases guickly with the number of allowances. It then becomes ever more difficult to comprehend all the specific exemption rules and the conditionality that govern them. Navigating the tax brackets and the income tax staircase is one thing, but mastering the often hundreds, sometimes thousands, exemptions built into modern tax codes is an entirely different endeavor. This politics of deductions is, hence, obviously important to the study of income taxation, but we must acknowledge at this point already that it is very tough to investigate them in a comparative framework due to the enormous country-level variation in their scope and design.

Returning to the distinction between rates and thresholds, one way to formulize these income tax parameters is as follows. The best reference case is, again, to start as simple as possible. The calculation of the tax liability (TL) in the flat-rate system with no tax allowances becomes a simple linear function of personal income (PI). The formula is:

**Notes:** As an example, the top US income tax bracket commenced at a taxable income of \$500.000 in 2018. With an average wage level at \$61.449 in the same year, this gave the US ratio of 8.1.

 $TL = R_1 * PI (1)$ 

where  $R_1$  denotes the single tax rate in question. In this example, the personal income (PI) becomes the taxable income (TI) by definition. But the calculation is seldom as simple as such. When the number of tax brackets exceeds one, the formula needs to reflect the changes in marginal rates, as the taxable income increases. Second, allowances, and going from the personal to the taxable income, must be factored in. The tax liability then follows a more complex formula:

$$TL = R_1 * TI + (R_2 - R_1) * (TI - T_1) * i(TI > T_1) + ... + (R_k - R_{k-1}) * (TI - T_j) * i(TI > T_j) (2)$$

**Formula (2)** looks a bit messy, but let us take it step by step. First, the tax liability now depends on the two main policy components R, the marginal rates, and T, the bracket thresholds. k then specifies the number of marginal rates in the income tax schedule in the given year, while j is the number of brackets. k is defined as j + 1, as the number of marginal rates must exceed the number of brackets by one.<sup>42</sup> I allow the expression to include allowances by replacing PI with TI, the taxable income defined as the personal income minus all applicable allowances. As noted, it is not an easy task to calculate in practice.<sup>43</sup> Finally, i are indicator functions. They designate whether the taxable income is above the particular (lower) bracket threshold whereby it would apply when calculating the tax liability. I can formalize i as:

 $i: T \rightarrow \{0,1\}$  defined as  $i: T = \begin{cases} 1 \text{ if } TI \ge T \\ 0 \text{ if } TI < T \end{cases}$  (3)

We can also express **Formula (2)** in more intuitive terms. It states that the tax liability is derived by first calculating the amount of taxes stemming from the basic rate ( $R_1$ ), which applies to a taxpayer's total taxable income. That is the first term on the right of the equal sign. Then, we multiply the marginal, additional tax rate ( $R_2 - R_1$ ) for the next bracket in the schedule with the specific subset of the income (TI –  $T_1$ ), as long as the taxable income still exceeds the lower tax threshold in question. If not, the threshold has no relevance for that particular taxpayer (and the indicator function i takes the value 0). The formula can be easily generalized to handle a varying number of tax brackets, as the second step of the calculation is repeated for each new rate level of the

<sup>&</sup>lt;sup>42</sup> It is because all taxpayers still have to pay the *basic* or *starting* rate of income tax in the absence of any income-specific brackets. It is essentially  $R_1$  we know from **Formula (1)**.

<sup>&</sup>lt;sup>43</sup> One could add possible tax credits (TC) to the formula calculation of the tax liability, but I have refrained from doing so in the example to keep it as clean as possible.

given structure until the final marginal rate  $(R_k - R_{k-1})$ . The sums of all terms are then added to generate the total tax liability.

When deconstructed, the politics of the income tax can thus be changed by tuning two main parameters: the rates and the bracket thresholds. Subsumed under these options persists the possibility of changing the number of tax brackets in themselves, i.e. by adding or abolishing a tax bracket. Finally, one can modify what counts as taxable income, and what is possible to deduct.

# 2.3 What taxes do: understanding their functions and trade-offs

I understand if the reader is confused at this point: there seems to be a strong case for more simplicity when it comes to policy. We have witnessed plenty such calls in recent years from various stakeholders on either side of the political spectrum (Loft 2015: 13-23). As a thought experiment, one could imagine a tax policy where all tax objects – whether it be taxpayers or corporations – pay the same tax rate. One would then only have to estimate the overall revenue needs of a given country, the total amount of incomes earned, and the total number of tax objects. From here, it is not an unmanageable mathematical task to calculate the tax rate for all tax objects to provide the sufficient revenue to finance the spending-side outlays. Yet, it is not as easy as such. We know the tax policy needs to balance other considerations than merely simplicity. In fact, the tax policy is perhaps the most crucial tool available to modern-day governments. Sven Steinmo, a towering figure in the tax literature, fittingly described taxation as a 'multifaceted instrument' that aims at solving multiple, but often conflicting societal goals:

Any taxation system embraces a complex mix of competing goals, ambitions, and considerations. Raising revenue, redistributing income, encouraging savings, stimulating growth, penalizing consumption, directing investment, and rewarding certain values while penalizing others are just some of the hundreds of goals that any modern government tries to promote with its tax system. Indeed, taxation is a major instrument, if not *the* major instrument, through which governments try to affect the private sector (Steinmo 1993: 3-4).

Steinmo's observation is vital to bear in mind if we wish to understand why political actors often end up choosing policy solutions that augment rather than reduce complexity. Turning to the thought experiment once more, the push to apply a flat-rate tax system to an otherwise progressive tax slope would have a major impact, not least on the economic distribution. It would result in massive shifts in tax burdens: rich taxpayers would presumably experience great net gains in their disposable incomes, while the poor are the net

losers in this exercise. That consequence is probably, by itself, sufficient to explain the political infeasibility of this reversed Robin Hood strategy.

The revenue need cannot stand alone. Generally, referencing Steinmo, we often distinguish between two other main functions of taxes (Avi-Yonah 2006). First, a *redistributive* function, aimed at reducing the unequal distribution of income and wealth that results from the normal operation of a market-based economy. This function has been a topic of fierce debate over time, and different theories of distributive justice can be used to support or reject its legitimacy (ibid.). It ties into the discussion on 'tax fairness' and is often referred to as the principle of 'vertical equity'.<sup>44</sup> The redistributive function serves to justify the reliance on progressive tax structures, figuratively that 'those with the broadest shoulders should bear the greatest burdens'.<sup>45</sup>

Second, a *regulatory* function that is often linked to the principle of *efficiency*, i.e. taxes should be used to raise the greatest amount of revenue while creating the least possible negative economic consequences. Because taxes affect the behavioral choices of economic agents, it is often used to steer societal activities in the directions desired by governments (ibid.). Taxes become the 'carrot and stick', as raising taxation on a particular object or activity is thought to discourage it, while lowering or removing taxation is expected to bring more of it. This is probably one of the oldest, and most recurrent, observations in the literature. For example, if the state taxes wage incomes too much, it is thought to dampen work incentives to the extent that it deters productive enterprise and, consequently, economic growth (according to some political accounts); the carrot in taking on additional work is then too small.<sup>46</sup>

<sup>&</sup>lt;sup>44</sup> It is common to distinguish between *vertical* and *horizontal* equity. The latter describes the idea that those who have the same amount of wealth, or similar level of income, should be taxed at the same rate as others within the same income bracket. This principle has also contributed to the major complexity of modern tax codes, as policymakers have tried to adjust taxation (often in excruciating detail) to accommodate a huge variety of occupational, personal or family circumstances.

<sup>&</sup>lt;sup>45</sup> Just how progressive policies should be has, of course, been a major bone of political contention.

<sup>&</sup>lt;sup>46</sup> The obvious measure, if one values efficiency, would then be to lower tax burdens on labor income to boost work incentives. But even here, there may be countervailing regulatory effects at play, what micro-economists deem the so-called *substitution* and *income* effect. If net wages increase (after a tax cut), work becomes relatively more profitable than leisure activities (substitution effect). However, with higher net wages, taxpayers can maintain the same standard of living with less work (income effect). Of course, the sizes of these effects are highly contextual and difficult to estimate with good precision, in part because they cancel each other out. I am not in the business of settling any debate on the (positive) effects of tax cuts, I will leave that to

The reason it is worth considering these four objectives – simplicity, revenue sufficiency, redistribution, and efficiency - is, as mentioned, that they conflict. Optimally, one would choose to tax in ways that optimize all four: simple, easy-to-comprehend taxes that raise revenue and the levels of redistribution and economic welfare all around, and discourage so-called 'undesirable' economic activities. Yet, no single tax measure is expected to do this. Let us, for example, contrast the goals of redistribution and efficiency first. Underlying this is perhaps the most essential trade-off in economics. Okun (1975) dubbed it 'the big trade-off' and explained the efficiency loss stemming from redistribution by the metaphor of the leaky bucket: 'The money must be carried from the rich to the poor in a leaky bucket. Some of it will simply disappear in transit, so the poor will not receive all the money that is taken from the rich' (ibid.: 91). The textbook version is slightly more elaborate. Redistributive policies (such as progressive income taxes) are thought to distort economic incentives, leading to suboptimal economic outcomes, distorting work, savings, and investment decisions. For example, the poor who are receiving welfare and other transfer payments, paid for by tax revenues, are expected to have less incentive to work because their transfers may be reduced or stripped from them entirely, as they begin to make work income. Similarly, the rich have less incentive to work due to high marginal tax rates that take a large fraction of their additional incomes, leading them to engage in substitute activities instead or plotting ways to avoid paying steep tax rates altogether.<sup>47</sup>

The third corner, the revenue-raising component, features in the trade-off as well. On paper, one could think of tax measures that serve to increase either equality or efficiency without hurting the other goal in the process. Say we cut the basic rate of income taxation, we expect this to affect efficiency positively, as work incentives are strengthened, mainly for lower income groups whose marginal rates are affected. It does so without (significantly) increasing inequality in disposable incomes.<sup>48</sup> Yet, it is enormously costly in terms of forgone revenue, as the cut is universal for everyone with a taxable income. The

economists. Yet, I will say that it is important to recognize that political actors who seek to alter existing tax policies may put weight behind the argument that reinforces their preferred solution rather than the one that seems to undermine it.

<sup>&</sup>lt;sup>47</sup> Okun, a master of metaphors, explained that 'high tax rates are followed by attempts of ingenious men to beat them as surely as snow is followed by little boys on sled.'

<sup>&</sup>lt;sup>48</sup> Bear in mind that cutting the basic income tax rates benefits the rich as well, as they will also pay a lower rate on the subset of their income that falls into this lowest tax bracket, unless some phase-out mechanism is put in place. Meanwhile those without a taxable income, typically the poorest of all, do not gain directly from the measure.

*size* of the cut may be moderate only, but the *scope* is as wide as it is can be. This revenue gap, hence, creates a different optimization problem that needs to be dealt with. One way to think of the issue is by looking at the basic fiscal equation of the state; government spending (S) must equal whatever the state raises in revenue via taxes (R) and loans, or *deficits* (D) by different name:

S = R + D(4)

Policymakers facing a revenue drought  $(R \downarrow)$  must balance this expression using one of three options, or a combination hereof. They can either cut spending accordingly  $(S \downarrow)$ , perhaps an unfeasible proposition for different reasons as I shall return to in **Chapter 4**; they can raise revenue by imposing other taxes elsewhere  $(R \uparrow)$ ;<sup>49</sup> or they can accept a larger state deficit  $(D \uparrow)$ , or, in rarer instances, a smaller state surplus than previously.<sup>50</sup> If they consistently choose the latter option, it may involve unsustainable debt accumulation over time.

The revenue, redistribution, and regulatory functions thus form a 'fiscal trilemma' (Alm and Sheffrin 2013), and their mutual trade-offs are crucial to our understanding of the politics of income taxation. Then we have not even weighted the grounds for simplicity that also tend to go against some of these functions. While the study of economics may inform what the better policy choices would be for balancing them, it is ultimately up to policymakers to decide where to situate 'optimally' on the trilemma. From what we know of contemporary politics, we expect policymakers of different cloth, in different contexts, to choose different optimizations. I elaborate on why in the subsequent chapters.

# 2.4 Ways to cut income taxes

By now, we have established what income taxes are, and what taxes more generally do. But before turning to the politics surrounding these issues, why and how certain policymakers wish to change income taxation, I think it is helpful to map the various ways they *can* change policy. Thus to address what politi-

<sup>&</sup>lt;sup>49</sup> Raising other forms of taxation risks reducing, or downright undermining, the positive tax effects. To give an example, if policymakers choose to finance personal tax cuts at the lower end of the income distribution with hikes to the VAT, as regressive a tax as they come, low-income taxpayers will disproportionally carry the burdens of the tax shift, and all positive redistributive effects of the reform will be washed away. Of course, there can be other valid reasons that justify shifting tax burdens from income to consumption.

<sup>&</sup>lt;sup>50</sup> The negative deficit (D) is, hence, a state surplus.

cians may prefer to do, we should understand the population of possible reform strategies from which they can choose. Here, I will not explain the nittygritty of how new policy can be strategized, crafted and implemented at the practical political level. I will discuss that in subsequent chapters. Rather, I will expose the instruments that can be tuned, and how each change affects the rate of taxation. I look, specifically, at the ways politicians can *cut* the level of income taxation, the one side of the coin, yet these demonstrated effects should extend neatly to a situation where politicians wish to raise the same taxes, only reversing the effect signs.

A key insight that follows from **Formula (2)** is that the tax liability is a function of the taxable income as well as the governing tax rules. The change in the latter thus affects classes of taxpayers with different levels of taxable income unevenly: some may benefit a great deal from a specific tax cut, understood as a reduction in their tax liabilities, while others may be unaffected by that same measure. Therefore, the change in policy needs to be evaluated against a yardstick, e.g. a reference taxpayer. We also know from **Formula (2)** that the rate(s), the bracket thresholds, and the number of tax brackets are main instruments at the policymakers' disposal when it comes to reform, along with measures that regulate the size of what is deemed taxable income. The personal allowance, the amount of tax-free personal income, is arguably the most important such measure.

To flesh out these reform strategies, **Figure 5** shows a representation of a fictitious income tax schedule, depicted with the level of earned income on the *x*-axis and the marginal rate paid on the *y*-axis. It is a progressive schedule, similar to the actual country schedules found in **Figure 2**. It features three tax brackets and a tax-free personal allowance.<sup>51</sup> The profile thus depends on six policy parameters that in concert are sufficient for drawing the schedule: the PA, the respective rates for each bracket ( $R_1$ ,  $R_2$ , and  $R_3$ ), and threshold values demarcating the transition from the first to the second bracket ( $T_1$ ) and from the second to the third bracket ( $T_2$ ).

<sup>&</sup>lt;sup>51</sup> One could argue that the income range defined by the personal allowance (PA) is to be viewed as a distinct, additional bracket that links a specific tax rate (in this case *zero*) to a specific tax base. If counted this way, the example features four brackets instead of three. Yet to ensure transparency and comparability across country tax structures, I rely on the OECD's (2011b: 30) method of counting the number of 'nonzero' bracket, i.e. brackets with an actual tax rate attached (R > 0). The zero-rate brackets are, hence, excluded when I compute the number of tax brackets in a given country year.





**Notes:** AW represents the reference taxpayer earning average wages. R abbreviation for tax rates, T for threshold limits, and PA for personal allowances. The grey shaded represents the income tax liability of the AW taxpayer.

The reference taxpayer I need is plotted from the *x*-axis, in this case a person earning AW. This income falls in the second bracket, i.e.  $T_1 < AW < T_2$ . This means that before any reform, the person pays taxes as follows: no income tax on the first subset of income corresponding to the PA; then they pay the basic rate (R<sub>1</sub>) times their entire taxable income (AW – PA); plus the marginal additional rate for the second bracket (R<sub>2</sub> – R<sub>1</sub>) times the specific subset of income that lies above the bracket threshold (TI – T<sub>1</sub>). The size of their tax liability corresponds to the area – shaded with grey – delimited to the left of the AW reference line and below the tax schedule. In this example, it is easy to see that their marginal tax rate is R<sub>2</sub>, their tax rate on additional taxable income ( $\Delta$ TI). It is also clear that the tax liability of our reference taxpayer is unaffected by the rules governing the highest tax bracket and the rate set (R<sub>3</sub>); they never enter the bracket as long as AW is less than T<sub>2</sub>.

Having identified the six parameters in play, I can now consider the potential reform measures one by one. **Table 2** provides an overview of each strategy and how they affect the taxes paid by our reference taxpayer. As stated, I look at cuts, and all of them involve an immediate reduction in government revenue if enacted. Let us start with what is perhaps the most intuitive way to cut income taxes, i.e. to cut the tax rates on the three brackets. As noted, these moves correspond to shifting the schedule downwards on the *y*axis, while maintaining the same anchors on the *x*-axis; the PA and bracket thresholds stay where they are, while the horizontal lines move closer towards zero.

Instrument	Reform measure	Average tax rate	Marginal tax rate
R1	The tax rate is reduced on tax bracket <i>below</i> the AW	$\downarrow$	No impact
$R_2$	The tax rate is reduced on tax bracket containing the AW	$\downarrow$	$\downarrow$
<b>R</b> <sub>3</sub>	The tax rate is reduced on tax bracket <i>above</i> the AW	No impact	No impact
Tı	The upper threshold is raised on tax bracket <i>below</i> the AW	$\downarrow$	↓ if AW moves into a lower bracket
$T_2$	The upper threshold is raised on tax bracket containing the AW	No impact	No impact
РА	The personal allowance is raised	$\downarrow$	↓ if AW is lower than new PA

#### **Table 2** Population of income tax strategies and their impact on tax rates

Source: Inspiration from Table S.2. in OECD (2011a).

**Notes:** All reform measures involve an expected loss in governmental revenue. These impact assume that the average tax rate is positive before changes to the tax code are implemented. R abbreviation for tax rates, T for threshold limits, and PA for personal allowances.

Tuning each of them influences the AW taxpayer differently, though. Reducing  $R_1$  obviously affects their tax liability, as they now pay a lower basic rate on the taxable income; their average tax rate thus becomes lower than previously.<sup>52</sup> Yet, since the bracket limits stay put, changing  $R_1$  leaves their marginal tax rate unaffected, as per **Table 2**.<sup>53</sup> What does alter the marginal rate, however, is the decision to lower  $R_2$ , the rate on their current tax bracket. Because the entire slope within the bracket is shifted downwards, it affects the marginal rate for any additional income earned. The move obviously affects the average rate as well because of the lower rate paid on their income above  $T_1$ . One cannot judge from this stylized example whether cutting  $R_1$  or  $R_2$  affects the average rate the most; it obviously depends both on how much each rate is cut and on the specific location of  $T_1$  in relation to the TI. It is the direction

<sup>&</sup>lt;sup>52</sup> The total amount of taxes paid thus goes down, while the total income stays the same.

<sup>&</sup>lt;sup>53</sup> I distinguish between the average rate and the marginal rate, as they – with reference to the functions of taxes – are expected to affect tax objects differently. Economic theory generally teaches us that marginal taxes are more crucial for incentives (Andersen and Maibom 2020); marginal decisions (such as whether to work more or invest more) depend mainly on marginal incentives (e.g. extra income after taxes), and much less on average 'burdens'. As we shall see later, it clearly spills over into the arguments used by policymakers to justify policy changes.

of the effects that is of prime interest here. Lastly, lowering  $R_3$  has no impact on our AW taxpayer's average or marginal rate, as such a move only affects income earners where TI >  $T_2$ , i.e. those with the relatively highest incomes.

If we turn our attention to the three remaining parameters – PA, T<sub>1</sub>, and T<sub>2</sub> – these determine the placement of the vertical lines in **Figure 5**.Tuning them, thus, shifts their location either closer to or further away from the *y*-axis. Cutting taxes would imply the latter. For example, raising the personal allowance from its current level shifts the first of the vertical lines rightwards. It counts as a tax cut for anyone with taxable income above the existing PA, since more of their income is made tax-free, all things equal. The average tax rate is therefore reduced. The marginal rate is kept the same, though, except for the exceptional case if the PA is raised to such an extent that PA > AW, whereby the latter would not be liable to income taxation at all. Then the marginal rate becomes zero, in other words.

Raising the upper threshold for  $T_1$  works along the same lines. It lowers the average rate paid by the reference taxpayer, as it effectively expands the tax base to which the basic rate (only) applies and shrinks the base for the additional rate. Put simply, they pay a lower tax rate on a larger subset of their income than they did before. Yet, the marginal rate is again unaffected, unless the raise pushes  $T_1$  past the AW, whereby the taxpayer switches into a new, lower tax bracket with a reduced rate. The contrast to cutting the (marginal) rate directly is, of course, clear when we study the rightmost column in **Table 2**: if one wishes to reduce the marginal rate paid by a given class of taxpayers, the only sure way to do so *is* to cut the rate that applies to their current tax bracket. Raising the threshold limits can, but may not, yield a similar result.

The instrument left is  $T_2$ , which demarcates when to pay the top rate. Equivalent to  $R_3$ , it has no impact on tax liability if we only consider scenarios where  $T_2$  must be raised, since it regulates incomes well above the AW.<sup>54</sup> In fact, the same logic would extend to tax cuts on all potential brackets that are beyond the scope of the reference taxpayer: no move impacts their tax rates.

Rounding up, I regard **Figure 5** as a stylized representation of the income schedule and the ways one can cut income taxation. It is equally clear that the six measures presented cover virtually all imaginable real-life reform scenarios: measures that target tax brackets *below* or *above* the reference taxpayer as well as their bracket.<sup>55</sup> The one scenario for which the reader may still need

<sup>&</sup>lt;sup>54</sup> If we allowed T<sub>2</sub> to be lowered as well, we could imagine a scenario where T<sub>2</sub> was pushed so far leftwards that T<sub>2</sub> < AW. Such change would cause both the average rate and the marginal rate to rise, all things equal.

<sup>&</sup>lt;sup>55</sup> Here, we again look beyond the myriad of potential special allowances and credits one could draft to cut taxes.

clarification is the one where the number of tax brackets is not fixed. What if, for example, one wishes to eliminate a specific tax bracket and go from a threeto a two-tier schedule? It has clear empirical relevance. But it should be evident from the above that in order to evaluate whether changing the number of brackets impacts the average and the marginal tax rates of a given taxpayer, we need specific details on the schedule before and after reform: which bracket is abolished, and which rates and thresholds govern, then, the remaining brackets? If one, for instance, decided to remove the third top bracket in the example, effectively turning  $R_2$  into the top marginal rate, it equates to status quo for the AW taxpayer but translates into a sizable tax cut for the richest. I return to this discussion in the subsequent chapters on how adding and abolishing brackets may be an appealing reform strategy.

# Chapter 3. Right parties and income taxation

Having defined income taxation, first, I proceed to look at the central political player(s) within this domain: the parties on the political Right. Taxation links naturally to them. They seem, more than other partisan actors, determined to reduce the amount of income taxation paid. Consequently, they need to be at the heart of the analysis, if we seek to explain the policy dynamics of the 21<sup>st</sup>-century, a period where reforms designated to cut income taxes have been the norm.

In this chapter, I wish to elaborate on why cutting income taxation is so appealing to the political Right. To keep a clear and crisp meaning of what I deem 'the Right', I rely on the literature standard, and the term, as I use it, covers the (mainstream) Liberal and Conservative parties. Next, I review what we know from existing studies about the relationship between the Right and income taxation. One would assume that it is reasonably well described, yet theoretical and empirical accounts on parties, more generally, and income taxation tend to downplay the notion of political agency: parties are either reduced to strong revenue maximizers (as per public choice theorists), or they are required to bite the bullet and live with progressive tax schemes to fund the spending commitments of the welfare state (as per political economists). However, none of the two perspectives seems accurately to describe the income tax dynamics we witness today's politics.

I then present *my* theoretical take on (Right) parties. It starts at the elite level, conveying a top-down logic. Further, it stands for the notion of political agency. Current elite actors of the Right are to a wide extent motivated by *causal beliefs* about the virtuous effects of tax cuts (vis-à-vis the Left, for example) rather than merely being driven by a strong representation component.<sup>56</sup> Rightist parties, guided by the core political value *freedom*, expect not only positive economic effects from lowering taxes in terms of efficiency; cuts are also compatible with the normative preference for a performance-based distribution of goods that rewards individual ambition and diligence. This intersection of norms and perceived benefits is what makes lower income taxes so attractive; in the eyes of the Right, tax cuts are, if not a magic wand that

<sup>&</sup>lt;sup>56</sup> I do not discard the influence of representation altogether. Of course, there may be some truth to the claim that the Right ultimately seeks flatter and lower income taxes that benefit the higher income groups in society, who continue to be among its core voters.

solves most issues, then perhaps the most effective tool for improving macroeconomic performance. Further, I argue that these causal beliefs manifest themselves in the way the Right perceives the benefit and cost-side of tax cuts; they tend to promote economic gains one-sidedly, while downplaying or neglecting the adverse effects on inequality, social provision and the budget balance.

### 3.1 Definition of Right parties

The literature on how to categorize political parties and their families is among the most extensive in political science. For this reason, I do not wish to think too much outside the box when setting up a definition of Right parties. Instead, I choose to follow Schmidt's (1996) often cited classification of the Left-Centre-Right trichotomy,<sup>57</sup> with parties being ascribed their respective label in accordance with their historical class representation and their broad position on redistributive issues. One clear advantage of this three-way split is that it parcels the variation within the group of non-leftist parties and, hence, mirrors the location of Christian Democratic parties and other Centrist parties on the political spectrum (ibid.). The category of the Right, as it is defined and used, then ends up consisting of Liberal and Conservative parties.

This broader category reflects a parsimonious way of looking at Right parties, but it contains, of course, a noticeable country variation across party system configurations and cleavage structures. What constitutes the strong political force of the Right hence differs; in some cases, it is a Conservative party, in others, a Liberal party, or both might be strongly represented. Yet, the pooling is sensible here since the two groups are generally aligned on tax and welfare issues (Schmidt 2010). These mainstream Right parties support capitalism, the market economy, private property rights, economic orthodoxy, and low public spending (ibid.) They tend to be less aligned on social issues, for example, with Liberal parties tilting more towards 'libertarian' and Conservatives lining up more 'traditional' on whichever exact label we give the poles of such cleavage dimension. The point is that these differences matter less when we discuss income taxation. Further, I wish to make it clear that I distinguish the mainstream Right from the newer, authoritarian right-wing populist par-

<sup>&</sup>lt;sup>57</sup> Schmidt credits the earlier works of Cameron (1984, 1985) and Blais and his collaborators (1992).

ties. Despite their wide emergence and parliamentary representation, especially in recent years, they seldom reach executive power.<sup>58</sup> My use of terms such as 'Right' and 'right-wing' does not include these parties.

The focus on the Right is both theoretically justifiable and empirically warranted. While the immediate post-war periods belonged to the political Left, as documented extensively in the welfare state literature, whereby they were arguably the more interesting phenomenon to study (Jensen 2014), it has since changed. The mainstream Right has formed the government for long stretches in many countries, especially over the last 30 to 40 years. Table 3 provides some numbers to back this claim. According to the Comparative Political Dataset collected by Klaus Armingeon and his colleagues, since 2000, 46 percent of the cabinet parties' parliamentary seats in Western democracies, which I study, have been held by politicians belonging to parties on the Right.<sup>59</sup> In fact, all 22 of the countries included have had Right participation in government at some point. Fewest in the continental countries Germany (6%) and Austria (14%) where Christian Democracy rules. Most in Denmark (76%), the arch-typical Social Democratic welfare regime, and in Japan (74%), the Conservative stronghold. Not having a positive theory on what happens during those periods is unsatisfactory.

<sup>&</sup>lt;sup>58</sup> Their political platform is typically much more founded on social (e.g. immigration) than economic issues. Some nationalist populist parties carry extreme anti-tax and anti-government views, while others promote an extensive welfare state for the in-group (welfare chauvinism).

 $<sup>^{59}</sup>$  To compare, the Left held 32 percent and the Centre held 21 percent of office party seats.

Country	Right cabinet parties' seat
	shares
Australia	0.70
Austria	0.14
Belgium	0.42
Canada	0.51
Denmark	0.76
Finland	0.40
France	0.57
Germany	0.06
Iceland	0.49
Ireland	0.58
Italy	0.46
Japan	0.74
Luxembourg	0.21
Netherlands	0.37
New Zealand	0.48
Norway	0.41
Portugal	0.45
Spain	0.57
Sweden	0.31
Switzerland	0.54
United Kingdom	0.45
United States	0.52
Mean	0.46

**Table 3** Right seat share as share of all cabinet parties' seat shares in parliament,2000-2018

Source: Comparative Political Data Set 1960-2018 (Armingeon, et al. 2020).

**Notes:** N = 22. The table displays the country averages for the variable 'gov\_right2', which measures the relative power position of right-wing parties in government based on the their seat share in parliament, measured as the share of total parliamentary seat share of all governing parties.

# 3.2 Our scarce knowledge about (Right) parties and income taxation

One way to disentangle the relationship between partisan politics, more broadly, and income taxation is to establish what we know from existing research. As stated in the introduction, relatively few political scientists have taken a swing at this proposal, despite its obvious relevance to a number of literatures. Much of the theorizing and empirical research have come from economists of different cloths).<sup>60</sup> These studies generally share commonalities in their approach to taxation but depart from different starting points when it comes to the basic questions (a) what drives partisan actors, and (b) what is the chief function of taxes.

One set of predictions comes from public choice economists (Barnes 2018). Their analyses typically rely on a strong office-seeking assumption (cf. Strøm 1990): government's main goal, regardless of its political leaning, is to get re-elected. It pursues this aim by choosing tax policies that maximize its total expected support (see e.g. Hettich and Winer 1984, 1988, Kenny and Winer 2006). Public choice economists focus mainly on the revenue-raising and efficiency functions. They argue that governments must tax in politically, as well as economically, sensible ways: they seek to raise as much revenue as they can and minimize the negative effect on political support. Voters are seen as self-interested and harmed through the direct loss of income and the deadweight costs associated with negative behavioral responses.<sup>61</sup> It generates predictions that taxes will be raised in a relatively 'efficient' manner in terms of the trade-offs between political costs and economic losses. Lower revenue yields and more elastic economic behavior or political opposition (at the voter level) will tend to lower reliance on particular types of taxes (Barnes 2018). As such, the literature is not interested in income taxes per se but rather in the reliance on income taxes relative to other forms of taxation.

It goes without saying that a strong rational choice approach would benefit from the integration of more sophisticated explanations of political choice when it comes to actors' informational priors and their motivations. We know, as political scientists, that their reliance on a 'complete information' assumption is unrealistic in real-world politics. Just like their voters, Right party elites are not perfectly rational agents. Yet, this view that policymakers hold exhaustive information on the marginal political and economic costs and benefits of several different tax types and are somehow able to choose the policy sweet spot seems exaggerated to say it the least. I will address the proper role of voters and their informational biases, both with regards to theory (in **Chapter 4**) and with novel data (**in Chapter 8**). Further, I will show how party leaders

<sup>&</sup>lt;sup>60</sup> Recently, we have witnessed a spike in the interest on tax matters in the political scientist community at large. The newly released impressive Handbook on the Politics of Income Taxation edited by Lukas Hakelberg and Laura Seelkopf (2021a) and its 25 contributions is indicative of the broad surge in the number of scholars taking stock of the tax question from theoretical different angles.

<sup>&</sup>lt;sup>61</sup> In turn, the probability of voter support is positively affected by the government's provision of public goods and services funded by the same revenue.

of the Right from time to time miscalculate how to position themselves on tax questions, and how this can have serious electoral repercussions.

A second criticism of this public choice approach relates to predictions on policy, or the lack thereof. It reveals little about *how* policymakers then choose to tax from a pool of different policy instruments at their disposal. It references the earlier discussion on rates and thresholds from **Chapter 2**. Consequently, there are several ways and means to achieve higher and/or lower levels of taxation. While such economists' view may provide us with a framework to explain variations in the state's revenue outcomes (operationalized as the size of the state and the distribution between tax sources), it cannot tell us anything meaningful about the specific policies that must lie behind such revenue intake.

Finally, one can also comment on the even trickier issue of policy motivation. Viewing taxes only through a lens of re-election ambitions seems to disregard any impact of partisan and/or ideological influence on tax outcomes *ex ante*. This concern of taxing as efficiently as possible undoubtedly reflects one important dimension in the design of tax policies, yet as we know from the previous chapter, it is certainly not the sole objective policymakers need to weight. It is important to note that my rebuttal does not say that office-seeking motives cannot (at all) influence parties and party leaders when they decide on taxation. Any nuanced study of party behavior should recognize that such considerations are almost always present in some capacity, especially for *core* mainstream parties (Kraft 2017), along with different motives that are potentially in conflict with parties' re-election ambitions (Strøm 1990, Müller and Strøm 1999). But to say that office motives are what matter (almost) exclusively is taking the assumption too far.

Another strand of the literature defined by political economists focuses more on the redistributive component when studying tax drivers. The main question it tries to solve is why the redistributive effects of tax systems vary across time and space. These studies are more party-centric from the outset and have a keener eye for how the struggle over key tax outcomes among political actors is motivated by different policy goals. What gets the most attention is the puzzling negative link between the level of tax revenues raised in countries and the progressivity of their distribution (see e.g. Steinmo 1993, Kato 2003, Ganghof 2006b, Beramendi and Rueda 2007, Prasad and Deng 2009). Both large government (i.e. high revenue levels) and high progressivity (i.e. disproportionate taxation on the highest incomes) should have – at least in their direct effects – a positive impact on redistribution, as long as the social benefits of the welfare state do not channel taxes directly back to the richer taxpayers. If the politics of taxation is *only* about redistribution, we should expect co-variation of the two across countries: high levels of progressivity should go along with large government. As noted, this is not the case: countries with the largest tax revenues (and as it turns out, the largest welfare states) do not have the most progressive tax systems.<sup>62</sup> This literature tends to take the level of revenue as the underlying cause for how tax systems are structured: the large and resilient welfare state requires a large revenue, and (progressive) income taxation is not sufficient to fund the major spending commitments.<sup>63</sup> High tax rates on relatively lower incomes as well as revenues stemming from one or more regressive tax sources (such as payroll or consumption taxes) are needed to supplement.<sup>64</sup> What ends up stealing much of the focus then, as for the public choice theorists, is the relation between income taxation and the reliance on other tax sources.

But how does partisan politics fit into this story? The puzzle surrounding the size and distribution of income taxes, paired with the idea that we expect the Right (Left) parties to seek less (more) redistribution, points to a pattern in which Right governments pursue lower levels of revenue, but rely on more progressive forms of taxation to ensure this goal (Barnes 2018). Timmons (2005) argues that this is due to a 'contractual' underpinning for different parties. Because of a more credible commitment to the kind of spending policies their voters prefer, the Right is able to levy a higher share of the tax burdens on their core constituents – higher-income voters. The symmetrical argument is made for Left parties and their ability to tax poorer voters.

It is important to note, however, that there is little consensus on this mechanism, as smaller-n studies within counties, and also within tax types, tend to find that Right governments pursue less progressive taxation rather than the opposite (see Ganghof 2006a). The discrepancy may arise, of course, from what they are trying to explain in terms of the temporal scope conditions. It may be true that the spending-side needs drove the design of revenue politics in the formative years of the welfare state, but it may be equally true that the

<sup>&</sup>lt;sup>62</sup> It therefore mimics 'the paradox of redistribution' on the spending side of the welfare state (Korpi and Palme 1998).

<sup>&</sup>lt;sup>63</sup> The nature and causality of this relationship have been debated too. Some argue that an efficient tax system (in terms of generating revenue) facilitated the growth of the large state (Kato 2003), whereas others claim that political pressures for more spending caused the welfare state to increase its revenue capacity (Lindert 2004, Ganghof 2006b).

<sup>&</sup>lt;sup>64</sup> It is a widespread view in this literature that advanced democracies have reached an upper limit when it comes to extracting revenues via income taxation. If effective tax rates on labor were to increase (significantly), work incentives will diminish for a large share of the population, which would then worsen the budget balance by shrinking the size of the economy and the tax base (Beramendi and Rueda 2007: 631).

same is not necessarily a good explanation of the current policy dynamics within the established frame. Nevertheless, I do meet the claims of the political economists insofar as the institutional structure should matter a great deal when it comes to policymaking. Consequently, a main contention in the dissertation is a rather simple one: partisan actors operate within the confines of existing tax rules that guide their policy focus. What I try to add, as I elaborate in **Chapter 4**, is a better understanding of what the relevant institutions are, and how they specifically shape motives and actions in contemporary politics.

The inconsistent understanding of parties extends not only to the main theoretical camps within the tax literature; it is also found empirically in more recent large-n cross-national studies. What do they tell us about the effect of parties, in general, on dependent variables related to income taxation, and of Right parties in particular? The best overview I have come across has been put together by the German political economist Niklas Potrafke (2017), who carried out a major, impressive meta-study on the effects of partisan politics in the OECD on a number of key social and economic policy outcomes.<sup>65</sup> Table 4 briefly summarizes the studies that specifically look at income taxes. Restricting the policy scope in this way limits the return to a meager five studies. The table recapitulates these accounts with regards to their choice of dependent variable, choice of partisan measure, as well as their main substantive findings. It has to be noted that not all studies reviewed are exclusively interested in partisan effects; in some analyses, government ideology serves rather as a control or moderating variable.<sup>66</sup> Even so, they are still useful when gauging all evidence out there on the macro-link between parties and income taxation.

Two main lessons can be learned from **Table 4**. First, there is little variance when it comes to choice of output indicator, i.e. what elements of the income tax are under review. Four of the five studies rely on effective tax rates on labor in some version. It is a deliberate methodological choice in all cases. For example, Angelopoulos and his collaborators (2012) refrain from analyzing statutory income tax rates and the temporal changes herein. Though they recognize them as vital policy indicators, they 'cannot capture the complexity

<sup>&</sup>lt;sup>65</sup> His analysis, which includes panel studies featuring OECD countries from the 1960s onwards *and* a measure of government ideology, includes a whopping 95 studies on spending-side outcomes but just 24 on taxes; about a 4:1 ratio.

<sup>&</sup>lt;sup>66</sup> Not surprisingly, a good part of the partisan tax studies relate to the larger literature on international tax competition where domestic factors such as government affiliation are never the main explanatory variable. These studies are also more preoccupied with corporate and capital income taxation than say income taxation (see e.g. Garrett and Mitchell 2001, Swank and Steinmo 2002, Plümper, et al. 2009, Genschel and Schwarz 2011, Osterloh and Debus 2012, Swank 2016).

of the tax system nor provide a clear indicator of the implied tax policy' (ibid.: 621). It reflects the 'one of many' critique I discussed in the previous chapter: to draw a distinctive conclusion from the rate, one needs to view it in concert with the specific threshold cutoffs, the structure of tax brackets at large, and some reference taxpayer. The authors prefer, instead, the effective tax rate (averaged over all taxpayers) as it also factors in the size of the whole tax base. This way, the measure expresses the ratio between the tax revenues collected on incomes and the corresponding tax base, which can be obtained from detailed national accounts (see Mendoza, et al. 1994 for a detailed walkthrough of how to compute these measures). The studies by Plümper and colleagues (2009) and from Swank and Steinmo (2002) justify the use of effective tax rates as the only tax measures that allow them to compare labor and capital tax burdens, the latter being their prime research interest. While the strength of this measure lies in their unidimensional quality and the chance to compare, one cannot escape the fact that it is a composite measure, reflecting an average tendency. Referencing the prior distinction between rates and thresholds, the effective tax rate says little in itself about which changes at the instrument level contribute to the rising or falling rate. One has to dig deeper if one is interested in policy. Further, it reveals nothing about whether an average is representative of the tax burdens of the non-average, e.g. income groups far below or far above the average or median income.

Second, the table proves that the relationship between the political Right and income taxation has largely been abandoned in large-*n* research. Only one of the five studies in question (Sakamoto 2008) explicitly models the effect of right-wing governments (measured as a dummy variable based on cabinet shares) on the share of GDP raised in income taxes. It finds that states' income tax revenues were lower under Right cabinets than under other types of governments (especially in the period 1982-2001). Two studies (Cusack and Beramendi 2006, Angelopoulos, et al. 2012) use different ideology measures that account for the policy positions of cabinet parties on a general Left-Right scale, both Right government and non-Right governments. Cusack and Beramendi (2006), using the *center of gravity* measure based on the Castle-Mair coding of party positions, finds a significant effect of ideology on effective tax rates on labor, with more left-leaning cabinets raising rates on average.<sup>67</sup>

<sup>&</sup>lt;sup>67</sup> The interpretation of the results is also consistent with right-leaning governments cutting effective tax rates – or simply not raising them as much as left-leaning governments do.

Study	Dependent variable(s)	Partisan measure	Effect (Left)	Time period	Countries	Parties as main X
Angelopoulos et al. (2012)	Effective tax rates on labor	<i>Expert surveys</i> , both Budge et al. (1993) and Castles and Mair	0	1970-2000	16	Yes
Plümper et al. (2009)	Effective tax rates on labor	<i>Cabinet shares</i> of left-wing and Christian democratic parties	0	1975-2004	23	No
Sakamoto (2008)	Individual income tax revenues (% of GDP, level)	Cabinet dummies for right-wing, center and left-wing governments.	o (Left)/ – (Right)	1961-2001	18	Yes
Cusack and Beramendi (2006)	Effective tax rates on labor (five- year intervals)	Cabinet and Legislative <i>center of gravity</i> (based on Castle and Mair)	+	1965-1995	14	Yes
Swank and Steinmo (2002)	Effective tax rates on labor	<i>Cabinet shares</i> of left-wing and Christian democratic parties	o (Left)/ + (CD)	1981-1995	14	No
Notes: Information for the	table is largely drawn from Potrafke'	's (2017) meta-study on the impact of $_{ m I}$	partisan polit	ics in OECD pa	inel studies.	

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In turn, Angelopoulos and his co-authors (2012), relying on a series of expert survey indicators, find no significant effect of ideology on the same outcome.<sup>68</sup> The remaining two (Swank and Steinmo 2002, Plümper, et al. 2009) must be interpreted with caution, as neither models the partisan effect as the main explanatory variable. Both seem to indicate, however, a null-relationship between the shares of cabinet seats held by the Left and effective tax rates. Swank and Steinmo (2002) do find a positive statistical relation between Christian Democratic partisanship, another control variable in their analysis, and the dependent variable, but do not reflect upon the cause of this finding. In conclusion, **Table 4** does not say much about how parties impact income taxation given the small sample size of studies and their inconsistent findings. This holds especially for the parties on the Right.

There is a lot work to be done. When it comes to theory, we need to build a better party-centric model that does not just shoot at the tax issue from one trench and that is premised on more realistic assumptions about how politicians think of tax matters, and what they can reasonably comprehend. With respect to empirical work, we need proper testing on the party-ideology link that goes beyond the reliance on average tax measures, with the hopes of developing a more nuanced understanding of which instruments, along with which parts of the income schedule, are the most likely targets of reform.

# 3.3 The limits of socioeconomic explanations

The central underlying question is: when will current income tax policies be successfully altered (or kept constant, for that matter) by the political Right? I suggest, following Starke (2006), that it is best approached through a conceptual dichotomy of (a) the motives or interests and (b) the opportunities of political actors. The logic is, in simple terms, that only when the group of political actors has both the desire (whether genuine or instrumental) and sufficient political leeway to change the status quo in a given direction should we expect change in that direction. Building my framework, I therefore first discuss the Right's motives for tax reform (in this chapter) and then consider how they link to the central tax institutions (in **Chapter 4**).<sup>69</sup>

<sup>&</sup>lt;sup>68</sup> They also employ a host of robustness tests and sensitivity analyses modelling the data as year-to-year variables and in five-year periods that are comparable with the Cusack and Beramendi (2006) approach.

<sup>&</sup>lt;sup>69</sup> Hence, I follow the principle of what Pierson (1994: 13) perhaps said most concisely: 'To be persuasive, accounts (...) must combine microscopic and macroscopic analysis. They must consider both the goals and incentives of the central political actors and how institutional rules of the game and the distribution of political resources structure their choices.'

Why would Right parties and the elites that populate them seek to cut or raise income taxation? For a political scientist, the vast and proximate literature on welfare state expansion and retrenchment seems a logical basis for answering this question because it has produced a host of approaches to thinking about political motives for reform. The two most prominent are probably the *power resource theory*<sup>70</sup> and the *new politics* perspective (cf. Pierson 1996). A third, less prominent, perspective redirects focus to the significance of the elite ideas and causal beliefs (Starke 2006: 111-112; Horn 2017). Below, I outline some shortcomings of the dominant approaches and develop a theory of policy-seeking Right actors whose causal beliefs are key to understanding their motives for tax reform.

The power resource theory is the main proponent of the view that voters are motivated by redistributive concerns. Authors like Korpi (1983), Esping-Andersen (1990), and Huber and Stephens (2001) see the politics of the welfare state as a power struggle between the haves and the have-nots: on the one side, the labor movement representing low-income individuals; on the other side, Right parties and employer associations representing high-income groups (Jensen 2014: 15). The benefit of redistribution for the poorer is straightforward, since it both increases their absolute material living conditions and decreases their sense of relative deprivation. The antagonism on the part of the richer is equally easy to understand, since they have to foot the bill, which will decrease their absolute living conditions and potentially their sense of relative well-being, as the gap in social status between the poor and rich becomes smaller (ibid.).

In this literature, parties of certain party families (Gingrich and Häusermann 2015, Häusermann and Kriesi 2015) are seen as representing these welldefined social constituencies, whose interests they are confined to advance in the arena of parliamentary politics. Parties that grab political power are then expected to convert their voters' preferences into policies (Schmidt 1996), as

<sup>&</sup>lt;sup>70</sup> One could distinguish the power resource approach on one side, inspired by sociology, and partisan theory on the other, an economics-inspired theory on the effects of political representation (see e.g. Hibbs 1977, Castles 1979, Schmidt 1996). The basic tenet of partisan theory is that policy outputs vary in accordance with the ideological orientation of cabinet parties that, in turn, is determined by the preferences of their social constituencies. The latter offers a more generic approach to studying all types of public policy. But when it comes to the welfare state question (or redistributive issues, generally), the predictions of the theories overlap to a significant degree: the Left should favor redistributive policies, while the Right wants to scale them back. Alas, I do not see the need to make a strong distinction between them here.

long as those preferences do not conflict with other predominant organizational goals (cf. Strøm 1990), and they are not blocked by from doing so by veto players (cf. Tsebelis 1995). It is a clear bottom-up theory in that respect; parties do what their voters want, and parties' positions can be inferred from their formal classification and the constituencies they represent and vie for.

The theory was developed with the spending-side in mind, yet on the surface, our expectations of partisan effects on income taxation should be relatively clear-cut when extended to the revenue-side. It is tempting to view, like the political economists, these policies as different means towards the same redistributive goals. The area should a most-likely case for strong partisan politics. If anyone, Right parties, backed by self-interested high-income voters, are the actors who are expected to seek less egalitarian outcomes and pursue this via policies aiming for lower and flatter income taxes (Cusack and Beramendi 2006, Ganghof 2006a). The explanation seems empirically grounded, as a number of recent accounts focused on micro-level drivers seem to confirm this picture (see e.g. Barnes 2015, Ballard-Rosa, et al. 2016, Roosma, et al. 2016, Berens and Gelepithis 2018). These studies find that the income status of voters matters a lot for the formation of tax preferences. High-income voters are, on average, less likely to support high tax levels and progressive income taxation (Barnes 2015). It is hardly a surprising result.

However, we know from the wider party literature that this assumed causal chain, from voters to parties, is threatened. Not only have class divisions and party constituencies become more blurred (e.g. Gingrich and Häusermann 2015, Kevins, et al. 2019), resulting in greater dealignment between party constituencies and the parties themselves. The core groups historically affiliated with both Left and Right parties have shrunk, and among those voters who still belong to the traditional groups, the predictive force of income and class has decreased due to factors such as cognitive mobilization, improved access to higher education, erosion of confessional ties, and, not least, the emergence of new conflict structures that sometimes cross-cut the old ones. The claim is therefore not that these economic groupings at the voter level have ceased to matter entirely for vote choice, as the share of high-income respondents voting for the Right is still and consistently relatively higher than the shares voting for other party types. Yet, the divisions are not important enough, in my opinion, to form the backbone of a theory that describes contemporary right-wing income tax policy.

The second part of the causal chain, that parties implement policies in accordance to the demands of their voters, could be equally problematic. The assumption seemed plausible as long as the alliances between social constituencies and parties were stable. But as these groups shrink, fringe, and emancipate themselves from traditional political allies, and their interests become more heterogeneous, it is less clear which group interests 'policy-seeking' parties represent. It seems at least as plausible to assume that parties that act under conditions of increased uncertainty tend to use a different cognitive anchor that preserves their capacity to act politically (Budge 1994: 445-447). This line of reasoning has also inspired much of the work on the 'cartelisation' of party systems, championed by the likes of Richard Katz and Peter Mair. It has convincingly argued how (mainstream) parties have 'withdrawn into the closed world of the governing institutions' (Mair 2006: 45), as the institutionalized connections between parties and increasingly disengaged voters became weaker (Katz and Mair 2009). Rather than parties solely meeting their voters' demands, this party system configuration entails a reversed flow of causality, where party leaderships, more independent of their bases, can act more as they wish and exploit the informational asymmetries from doing the actual governing to their own advantage (Blyth and Katz 2005).

One could instead posit that reform-minded politicians are perhaps simply pandering to the broader public (i.e. the median voter) rather than their constituencies of vester vears. It meshes with the office logic promoted by the public choice economists. I see at least two superseding reasons, one general to contemporary party politics and one specific for taxation, as to why the direct, causal influence of voter preferences should not be exaggerated.<sup>71</sup> First, the literature on strategic blame avoidance, echoing the asymmetry of informational flows just mentioned, has described the extensive arsenal of manipulative strategies available to politicians.<sup>72</sup> Not only are voters thought to be ill informed, on tax matters especially (Bartels 2005), and short-sighted (Wenzelburger, et al. 2019); politicians actively subvert their understanding of reform content by using complex instruments at their disposals (Green-Pedersen, et al. 2012, Jensen, et al. 2018), by masking the true distribution of gains and losses through manipulation of timing (Hacker and Pierson 2005, Tepe and Vanhuysse 2010), and by bundling policy changes into larger reform packages that also include (symbolic) compensatory elements (Weaver 1986, Lee, et al. 2020). Moreover, this is even reinforced by the use of strategic framing. It can take the form of causal narratives such as 'there is no alternative' (Pierson 2001, Wenzelburger 2011, Elmelund-Præstekær and Emmenegger 2013, van Kersbergen and Vis 2014) or normative discourses of fairness, rights, and deservingness (Slothuus 2007, Elmelund-Præstekær, et al. 2015).

<sup>&</sup>lt;sup>71</sup> I do not argue that voter preferences and public opinion regarding taxation do not (at all) matter for policy in this domain. I certainly think they do in broad terms, but they are not the prime motivational drivers in my view.

 $<sup>^{72}</sup>$  Barbara Vis (2016) has conducted an excellent comprehensive review of this literature.

Such strategies are clearly not always and automatically successful, but this literature does demonstrate, beyond any doubt, the existence of significant political agency and a reverse flow of influence from parties to the electorate.<sup>73</sup> While less explored empirically, this logic should travel neatly to the tax domain. Tax cuts – or hikes for that matter – are not a straightforward vote winner<sup>74</sup> when we look at the views of the median voter, implying that purely office-seeking parties ought to be more reluctant to pursue such policy than has been the case over the last many years. Together, these arguments lend credence to the notion of relatively autonomous parties.

An alternative explanation that draws on Paul Pierson's (1994, 1996, 1998, 2001) emphasis on vested interests in the *new politics of the welfare state* could be that parties of all cloths face pressure from well-organized and politically influential interests groups whom it would be electorally unwise to challenge. A similar type of argument on interest group influence can be put forward with regards to tax cuts and has been, especially in the US experience (see e.g. Hacker and Pierson 2005, Mettler 2011), where we have witnessed examples of powerful political donors putting on the pressure to deliver income tax cuts. But these arguments also have to confront Pierson's original point about well-organized interest groups, the so-called welfare state clientele, that we surely expect to resist the drain on revenue stemming from tax cuts, especially if coupled with direct spending cuts. In my view, interest group explanations can at best contribute to understanding any self-reinforcing political dynamics surrounding those (larger) reform events.

# 3.4 A proposed model of Right party elites

Instead, the frequent use of arguments made by Right politicians that link income tax cuts to favorable economic gains arguably indicates a third mode of explanation: *elite ideas*. One way to see why ideas matter is the negative argument that structures matter less than they used to.<sup>75</sup> But there is certainly also

<sup>&</sup>lt;sup>73</sup> Newer research suggests that parties have much leeway to shape public opinion, as a relatively large proportion of voters tend to follow their party when it changes its policy position. Slothuus and Bisgaard (2020) find that these effects exist not merely in experimental labs but also in real-world political settings.

<sup>&</sup>lt;sup>74</sup> I substantiate this claim of low popularity in with cross-national data from the European Social Survey in the next chapter (**Chapter 4**) and with my novel survey data on Danish voter's reform preferences in **Chapter 8**.

<sup>&</sup>lt;sup>75</sup> Beyond the arguments I have presented, it is worth noting that politicians' rationality, a key assumption in the representation-based approaches, could be flawed, at least occasionally, and that their perceptions of the economic, political, and electoral

a positive case to be made. In my view, political actors should not be conceptualized as mindless vote-seekers for whom policy is purely 'instrumental'; political parties as organizations and politicians as individuals pursue votes and office in part for other reasons. In strategic terms, this simply amounts to 'policy-seeking' behavior (Müller and Strøm 1999) with actors 'seeking policy for its own sake' (Budge and Laver 1986). But as Starke notes, 'one obvious reason' political actors might want to pursue reforms, especially those who are out of step with what the majority of voters wants, 'may be ideological' (Starke 2006: 113). It is tough to grasp the Right's continuous staunch commitment to lower taxes without adding this take on motivation.

To unpack this rather vague insight and understand the substance of these more ideationally based 'policy-seeking' motives, we must engage with the ideas actors hold with regards to taxation. It implies too that we need to alter our basic assumptions about why parties, and the elite actors who populate them, act. First, the focus on *ideas* or *causal beliefs* naturally re-arranges our theoretical attention to the elite level, more specifically to the Right's party leadership. What becomes worthwhile are *their* ideological beliefs, not so much their voters'. Second, among the multitude of approaches subsumed under the header 'ideational', the notion of *policy paradigms*<sup>76</sup> (Hall 1992, 1993) has had a lasting influence. In Hall's classic definition, they are an:

overarching set of ideas that specify how the problems facing them are to be perceived, which goals might be attained through policy and what sorts of techniques can be used to reach these goals. Ideas about each of these matters interlock to form a relatively coherent whole that might be described as a policy paradigm. Like a gestalt, it structures the very way in which policy-makers see the world and their role within it (Hall 1992: 91-92).

Blyth (2003: 11), whose concept of *economic ideas* derives from Hall's notion, elaborates and states that such ideas 'provide agents with a *scientific* and a *normative* account of the existing economy and polity, and a vision that specifies how these elements should be constructed.' They constitute an 'interpretative framework' that helps agents to navigate their environment, especially in times of crisis. They reduce uncertainty and empower actors with blueprints

environments 'might well be irrational' (Wenzelburger 2011: 1156). Interpretive political struggles over the definition of problems and the meaning of events can be quite loosely connected to any underlying 'objective' reality (see e.g. Widmaier, et al. 2007, Hay 2011, Matthijs and Blyth 2018).

<sup>&</sup>lt;sup>76</sup> Hall demonstrated the potential of this approach by explaining policy changes based on the transition from Keynesianism to monetarism In the United Kingdom in 1979 and 1989.
to propose a particular solution.<sup>77</sup> The intersection of the definitions suggests that *ideas* can be regarded as a cognitive frame that provides actors, or more specifically Right party elites, with two closely intertwined set of beliefs: specific causal beliefs about the interplay between government, the economy and society at large (the *ontological* or the *cognitive* component) and beliefs about the norms and values that should be maximized as the basis for the assessment of the status quo (the *normative* component) (Horn 2017: 117).

Regarding the substantive content of the Right's belief systems on taxation, it is useful to trace the ideological origins of the partisan divide for answers. There is widespread consensus among theorists that the Left-Right dichotomy can be traced back to the competing core values of *equality* and *freedom*, which again find institutional expression in a preference for either market allocation or reallocation of market results via the (welfare) state (Bobbio 1996, Jahn 2010).<sup>78</sup> To the extent that equality is regarded as the more basic value, then redistribution of market results via welfare state transfers and taxation is regarded as a desirable means. However, if freedom is the more fundamental value, market allocation is the weapon of choice, as market results are perceived as just and efficient, and inequality is seen as a legitimate outcome of different individual choices (Horn 2017: 119-120). This nexus constitutes the intellectual anchor for this alternative account of partisan motivation and interest.

What are then the norms and ontological beliefs of the Right, and how do they link specifically to income taxation? Alexander Horn (2017) addresses the first question in detail, as his proposed concept of 'market ideology' seems to capture the normative and ontological Right end of this fundamental Left-Right dichotomy. In terms of economic policymaking, he posits, for example,

<sup>&</sup>lt;sup>77</sup> The more recent literature on the impact of ideas on public policy is largely in line with the main ideas voiced by Hall and Blyth. Policymakers are perceived to hold certain causal beliefs and normative convictions, ideas that serve as cognitive frames that filter perception and are crucial for the construction of interests (Horn 2017: 113). In a nutshell, ideational scholars depart most notably from traditional representation-based approaches by relying on the proposition that ideas of policymakers are crucial for the construction of interests, whereas the notion of policy goals is merely a by-product of interests that is commonly rejected (Béland and Cox 2011, Hay 2011).

<sup>&</sup>lt;sup>78</sup> Bobbio (1996) does a formidable job of tracing this distinction back to different images of human nature. In his view, the conviction that people are fundamentally equal and that inequalities must therefore be justified with good arguments belongs on the Left (Rousseau is the leading exponent of this idea). In contrast, the persuasion that people are essentially distinct or unequal marks the anthropological origin of the Right (the leading exponent of this idea is Nietzsche).

that parties on the Right tend to see a weak economy as a consequence of (too much) state intrusion into largely self-regulating markets. In this view, employment depends on the market-clearing price of labor. If it is not priced on free-market terms, it renders full employment impossible. This friction is caused by public interference in the form of too high tax levels, which increase the price of labor, and generous unemployment compensation, as social benefits constitute the reservation wage that, if too high, offsets incentives to work (ibid.: 135).

Parties on the Right thus expect a positive economic impact of lower taxes and welfare cuts, which they believe will bring the labor market closer to its market equilibrium by lowering the price of labor, and strengthen incentives to work and to invest, which will lead to further economic growth and lower unemployment down the line. The Right also thinks that lower public spending has a positive net effect on the budget, despite its negative effects on domestic demand, which it regards as less vulnerable than the Left does. In turn, the stronger work incentives and market efficiencies are seen as beneficial to growth, and they are regarded as having positive secondary effects on tax revenues. Think of the so-called Laffer curve here, where lower tax rates may boost tax revenues, as more workers switch from leisure to productive activities (substitution effect). The Right's policy response during crises is therefore to 'tighten the belt' (i.e. to cut spending) and keep tax levels low. In addition to this austerity preference, tax and welfare cuts are compatible with the normative preference for a more performance-based distribution of goods, which rewards individual ambition and the spirit of free enterprise and meritocracy (ibid.: 135). In their eyes, unequal outcomes are perceived as legitimate of different individual choices, as long as equal opportunities and equal access were ensured. The Right, invoking a formal concept of equality, remains skeptical of large-scale redistribution and state intervention, as these actions are regarded as an infringement upon, or an outright violation of, individual freedom and self-ownership (ibid.: 119).

Summing up, the normative dimension of Right ideas includes traditional freedoms such as the promotion of negative freedom rights, fair competition and an equal access imperative, while the ontological dimension covers neoclassical and laissez-faire positions, i.e. views of the economy as self-regulating and state intervention as distorting market incentives, and tax and spending cuts as boosting economic growth and employment.

Describing the Right and their causal beliefs about taxation and economic policy in this was is, of course, a generalization, and one perhaps too coarse to successfully cover all the parties subsumed under this label at all times. But if we take these general descriptions and apply them to the income tax question and the aforementioned functions of revenue, redistribution, and efficiency, we should be able to derive a relatively clear goal hierarchy as to what we expect Right parties to go after.<sup>79</sup> When putting Okun's trade-off to the test, we expect Right to prioritize efficient taxing over equality.<sup>80</sup> On the question of revenue, we expect the Right to be much more comfortable than other parties accepting a policy that lowers the revenue yield, since the large state is seen as an obstacle rather than a solution to key macro-economic goals. But I argue that the impact of these causal beliefs often goes beyond priority. They shape the way the elites evaluate policy consequences on a more fundamental way. Subscribing to Right ideas tends to make one magnify the potential benefits of tax cuts, likely exaggerating the positive effects on economic performance beyond the 'actual' impact, while at the same being unaware of, or at least downplay that their preferred policy may carry adverse effects on inequality, social provision, and the budget balance.

The next and obvious question is how these core values and beliefs of the Right translate into the pursuit of specific policy. This chase is likely not going to be the same. Because their starting points, understood as their institutional contexts, vary. To understand how Right elites handle the whole instrument question and go about strategizing in different settings is the topic for the next chapter.

<sup>&</sup>lt;sup>79</sup> An added advantage with this ideological approach to interest is that it allows, potentially, such rightist causal beliefs to affect politics, even when the Right does not hold executive political power. The ideas of the Right may inspired, or downright persuade other actors. Early in my project, I was, for example, dumbfounded looking at cases where the Left enacts income tax reforms that bear close resemblance to what we would have expected the Right to do in a similar position. We have seen plenty of examples – over the last 20 to 30 years – of leftish governments cutting income taxation in ways that increase the level of inequality in society. These 'anomalies' are difficult to explain if we assume parties only cater to specific group interests. If the elite's causal beliefs are what is put at the heart of the analysis instead, the analysis does not need to stop there.

<sup>&</sup>lt;sup>80</sup> I am not blind to the notion that lower and less progressive income taxes also accommodate the direct material interests of a large group of the Right's core voters. But a key point I try to make is that these parties, and their voters, are not just selfish and self-rewarding. This policy is in accordance with causal beliefs that deem it as fair and that carry positive economic consequences beyond narrow self-interest. In my view, this is a much more positive take on the Right's tax motivation than simply being 'anti-redistributive for the sake of being anti-redistributive'.

## Chapter 4. The income tax strategies of the Right

After laying the theoretical groundwork in the previous chapters, I will now build the frame by answering the question: what specific policy strategies do we expect the Right to pursue in different contexts? It start with the simple, generic answer. I posit that Right politicians wish to cut income taxes when they can get away with it. That is not saying a lot, but I can get a little more specific.

Power comes with political responsibility. Even the most ideologically committed Right elites are not merely free agents when they hold executive power and, thus, have the best position to reform; they must deliver solutions to a wide array of problems in society, which may crowd out the tax question; and they must consider potential criticism for enacting tax-cutting reform from their main political opposition, the parliamentary Left. I argue that these mechanisms spill over into instrument choice. While lowering the (marginal) tax rates may be the Right's preferred mode of cutting, this strategy may prove too politically contentious, meaning the Right will often times refrain from reforming, or reform in ways that invite less political conflict.

The argument builds on the premise that the politics surrounding instrument choice (as presented in **Chapter 2**) matters. The rate is arguably the most *visible* feature of the tax code, from the standpoint that it is easy to link changes in policy to changes in the taxpayers' post-tax incomes. Cutting taxes in this fashion invites political conflict. Changing tax thresholds lends more confusion in terms of its causal effects; when threshold limits are raised from their current levels, it is not *that* obvious that the outcome of this change is lower taxes on incomes above the existing threshold(s). We can describe the basic maxim that reform-eager Right politicians will likely resort to ways of cutting income taxes that augment their connection to the more popular (or the least unpopular) policy tools, while not touching those they know are 'third-rail politics'. If the cost of successfully raising thresholds (vis-à-vis the status quo) is to abandon any political ambitions to cut tax rates, that just may prove to be within their 'zone of acceptable outcomes' (cf. Weaver 2000, Hacker and Pierson 2005).

Finally, I argue that countries' existing tax legacies do a lot to moderate the Right's political incentive structure. Two components are key: (1) the number of brackets in the current tax code, and (2) the level of progressivity built into the tax schedule. They shape the policy process in distinct ways. The former defines the slate of available instruments to tweak. When the number of tax brackets is low, there are few policy parameters that policymaker can target. Altering the rate becomes both a fiscally expensive and highly visible way to cut taxes. Here, the Right policy strategy shifts to the threshold(s), the less visible component. When the system features a higher number of brackets, the list of potential instruments to reform augments. This makes it possible to target a broader array of instruments, and the Right can choose to target rates and thresholds alike without compromising the entire redistributive profile of the income tax schedule. The progressivity, in turn, guides the policy priority of the Right, i.e. where their focus lies across the income distribution. In highly progressive tax systems, where higher income groups are taxed disproportionally more than the lower ones, the Right's political target should be those heavy burdens towards the top, as, they would argue, the efficiency gains from cutting taxes are the strongest there. In settings with low progressivity, where both the low-to-middle and the high income groups face relatively high marginal tax rates, the Right should pursue to cut income taxes much more broadly.

#### 4.1 The politico-economic constraints of the Right

For the political Right, cutting income taxes seems like the silver bullet, as spelled out in **Chapter 3**. It aligns with deep ontological beliefs on the harming effects of state intrusion into self-regulating labor and product markets, and it meshes with a normative preference for a performance-based distribution of goods in society. Hence, Right elites with strong ideological convictions expect tax cuts to facilitate a lot of positive economic and social outcomes.

One can, therefore, reasonably ask why we do not always see the Right pushing single-mindedly for such cuts in our observations of day-to-day politics. Especially when they control the political executive and are in a good position to reform the political status quo. We can, of course, point to a number of potentially constraining factors, referencing insights from the broader partisan and public policy literature. For one, students of politics acknowledge that Right parties have both multiple commitments and policy goals to pursue when in power. The government status comes with a great responsibility to deliver solutions to a large number of policy problems that exist in society (Green-Pedersen and Mortensen 2010, Jensen and Seeberg 2015), not just those that revolve around income taxes. If a government, of any partisan cloth, ignores pressing societal issues, it may be accused of being unable to deliver solutions,<sup>81</sup> which is likely to hurt its standing among the electorate and, hence, its long-term re-election prospects. Consequently, Right parties may find that the tax question is crowded out by more pressing issues on the political agenda, over which they are not in tight control.

Second, and referencing the state's fiscal equation presented in **Chapter 2** (and the policy trilemma innate to it), the Right cannot set the income tax rules they want without first considering the opportunity costs and the budgetary ramifications of such decisions.<sup>82</sup> Some would argue it is a tough nut to crack for Right parties, especially, who are viewed as agents that wish to promote fiscal discipline and have a strong preference for low budget deficits (Hibbs 1977, Horn 2017). They would then need every tax revenue they can get their hands on to keep public budgets 'out of the red'. Recent empirical studies question this latter assertion. In fact, studies of debts politics in the post-war period suggest that the Right is on average more prone to debt accumulation in what we would deem 'normal economic times' than cabinets of different political color, as the Right is seemingly willing to accept more fiscal slack. During recessions, such as the one ensuing the recent Financial Crisis, right-leaning cabinets increase the debt less, or 'tighten the belt' more, than other types of governments (Müller, et al. 2016). Thus, the Right engage more in what we call pro-cyclical fiscal policies. These findings moderate the general notion that the Right are supposed to care more about fiscal responsibility. Or to put it more bluntly, they care only about debt accumulation when the economy is in turmoil, not when it is booming or running on normal.<sup>83</sup> With reference to the link between spending (S), revenue (R), and deficits (D), this may be indicative that the Right more often are willing to carry the fiscal costs of cutting (income) taxation, i.e. to finance tax cuts with larger deficits (or smaller surpluses). Of course, such strategy leans on some sort of backstop, as severely mismanaging the public finances is not exactly popular among voters either.

<sup>&</sup>lt;sup>81</sup> It runs this risk, even if the government bears no direct responsibility for these problems, and even though many of them may not be amenable to government solutions (Green-Pedersen and Mortensen 2010: 262).

<sup>&</sup>lt;sup>82</sup> The fiscal leeway to cut taxes may be further limited, since many policy solutions to the aforementioned problems on the political agenda may require the government to spend more to solve them practically or at least to mitigate them politically.

<sup>&</sup>lt;sup>83</sup> A recent study by Alonso and Ruiz-Rufino (2020) of the Eurozone countries during the aftermath of the Financial Crisis shows that the established Right, in contrast to the Left, is not punished as much electorally for enacting harsh fiscal interventions during times of economic turmoil.

Being willing to cave in on a strict fiscal discipline does not reveal anything, however, about how to situate on the two remaining pillars, the spending-revenue nexus. Given the Right's ideological point of departure (see **Chapter 3**), we may posit that their most straightforward policy strategy would be to cut income taxes, and hence accept lower revenue yields, while concurrently cutting social spending as much, or almost as much, to maintain a relatively balanced budget.<sup>84</sup> Yet, drawing on insights from the welfare state literature, one will probably tell you that it is a naïve answer due the strong, vested pro-welfare interests (Pierson 1996). The welfare state has created its own constituencies, which explains, so the theory goes, its tremendous resilience (ibid.).<sup>85</sup>

Such opposition is reinforced at the partisan level, where the Right's main political rival, the parliamentary Left, still a force to be reckoned with, is keen to play the role of watchdog. The Right can likely come up with a number of persuasive arguments to cut income taxes. But if the Right as much as ponders such policy, especially if they intend to target the highest incomes, the Left opposition would in all likelihood use the opportunity to cry foul and try to frame the proposal as a bad deal for the majority of taxpayers. The Left will pressure the Right to come up with goods reasons for prioritizing tax cuts over social spending (or 'better welfare' to employ an often-used expression).<sup>86</sup>

It is an equally tough sell for Right politicians if we take a look at the voter level. They know they are up against deep-seated voter aversions against sig-

<sup>&</sup>lt;sup>84</sup> As Jensen (2014) correctly notes, the notion that Right politicians simply care about slashing spending across all welfare domains is a severe misconception. He argues this notion is especially true for life course-related welfare programs, such as health care and pensions. Right parties should be inclined not only to oppose spending cuts here, but in fact willing to spend *more* on the schemes that benefit middleto-high income earners the most.

<sup>&</sup>lt;sup>85</sup> One of the strongest observations of state budgets in recent years is that the size of the budget seems to be in a broad equilibrium. Since the 1990s, the average tax revenue as a percentage of GDP has clearly plateaued across the OECD (Jensen 2019). No matter the specific causes of this floor effect, the take-away is simple but crucial: the size of the budget stays about constant, and Right parties are thought to have limited scope for enacting new income tax rules that involve major decreases in revenue.

<sup>&</sup>lt;sup>86</sup> It should be a viable strategy from the Left's perspective because assessments of policy impact are based on perceptions rather than hard facts, as I lay out in **Chapter 8**. If large voter segments are convinced that a new policy is bad for them, irrespective of the actual policy content, they will likely turn their backs on the Right government.

nificantly reducing the size of the (welfare) state. Those have been documented in countless surveys across the OECD democracies spanning decades. One of the most cited studies of mass public preferences, the European Social Survey's (ESS) fourth round collected in 2008,<sup>87</sup> asked respondents in a number of European countries how they would prioritize between a government policy of less taxes *or* more spending, starting from the state's current level. I summarize the descriptive findings in **Table 5** for 13 of the Western European countries that are included in the country sample used in this dissertation, though the results do not differ much from those we find in the Central and Eastern European countries.

The respondents were asked to state their preferred development for the state budget and reply on a scale from 0 to 10, with 0 indicating a preference for lower taxes, and 10 a preference for more spending.<sup>88</sup> The table shows the mean response sorted in descending score order by country. The columns to the right show the group of responses split into groups of those who clearly prefer lower taxes (0 to 3 on the answer scale); those who prefer the status quo or close to it (4 to 6 on the scale); and those who prefer more spending (7 to 10 on the scale). The rightmost column in **Table 5** presents the share of committed tax cutters minus the share of committed spenders to get a sense of the relative weights of these 'fringe' groups.

<sup>&</sup>lt;sup>87</sup> It is one of few cross-national surveys that explicitly employ questions about voters' (broad) tax policy preferences. Most of these multi-country surveys almost exclusively study public preferences in spending areas, referencing the similar imbalance between the study of spending and the study of taxes. In the ESS, the tax questions come in two shapes: (1) respondents are asked to prioritize between lower taxes and more spending (D34, the question results I present here); and (2) respondents are asked to evaluate how much taxes two persons, one earning twice as much as the other, should pay (D35)?

<sup>&</sup>lt;sup>88</sup> One reason I like the ESS version of the taxes versus spending choice is that it explicitly highlights the cost-side of each policy, i.e. that lower taxes come with the price of reduced social spending, and vice versa. It tackles the potential criticism from those students of tax attitudes who advance the 'something for nothing' syndrome (see Sears and Citrin 1985, Edlund and Sevä 2013), i.e. that people do not understand the direct link between spending and revenue policies and therefore can exhibit irrational simultaneous preferences for much lower taxes and much higher spending.

		Average	Shara		Shara	
	Sample	(o = tax less, 10 = spend	taxes (reply o-	Share SQ (reply 4-	spending (reply	Taxes minus
Country	size (n)	more)	3)	6)	7-10)	spending
Denmark	1,578	5.98	0.10	0.51	0.39	-0.29
Finland	2,156	5.89	0.07	0.56	0.36	-0.29
Norway	1,533	5.60	0.09	0.62	0.29	-0.20
Sweden	1,760	5.44	0.16	0.53	0.31	-0.14
Netherlands	1,732	5.28	0.12	0.66	0.22	-0.10
Spain	2,220	5.28	0.15	0.60	0.25	-0.10
United Kingdom	2,280	5.23	0.21	0.50	0.29	-0.08
Ireland*	1,723	5.20	0.22	0.51	0.27	-0.05
Switzerland	1,751	5.11	0.15	0.67	0.19	-0.04
Belgium	1,738	5.06	0.16	0.66	0.18	-0.02
France	2,012	5.04	0.19	0.61	0.20	-0.01
Portugal	1,758	4.91	0.23	0.57	0.20	0.03
Germany	2,600	4.81	0.20	0.65	0.15	0.05
Mean		5.30	0.16	0.59	0.25	-0.10

**Table 5** Citizens' views on changing the size of government, lowering taxes vis-àvis spending more

Source: European Social Survey,  $4^{th}$  round (2008).

**Notes:** The exact wording of the question was as follows: "Many social benefits and services are paid for by taxes. If the government *had* to choose between increasing taxes and spending more on social benefits and services, *or* decreasing taxes and spending less on social benefits, which should they do?" Respondents could answer on an 11-point scale: O "Government should decrease taxes a lot and spend much less on social benefits and services", 10 "Government should increase taxes a lot and spend much more on social benefits and services". Don't know answers and refusals are not included here, though they are generally at a low number in each country. Field work in most countries started in September 2008 and ended in the early months of 2009. \*: Field work in Ireland did not overlap with the remaining countries; it began in September 2009 and ended in March 2010.

What stands out in **Table 5** is, of course, the lack of a clear tax and spending preference if we first gauge the average tendencies. It is evident that the mean position varies between countries, but what seems the main take-away is that it does so within relatively narrow confines on the answer scale, from 4.81 in Germany, the electorate most devoted to cutting taxes among those surveyed, to 5.98 in Denmark, the one most committed to (more) spending, alongside the other Scandinavian countries.<sup>89</sup> The statistical difference is there, and one could spend plenty of time fleshing out the explanation(s) of the individual country differences. But focusing on the broader picture, the gap between the maximum and minimum countries amounts to less than 12 percent of the full

<sup>&</sup>lt;sup>89</sup> 5.30 is the average of averages across the 13 Western European countries.

theoretical variation. All country means are, further, relatively close to the scale midpoint of 5.0, the value we could reasonably interpret as a *status quo* preference on this particular issue. There is nothing in the average scores that indicate strongly a skewed distribution, and a unimodal commitment among voters to change the size of government in an upwards or downwards direction.

In theory, we can think of a number of other distributions that could generate average scores close to the middle of the scale, as we see here. But the rightmost columns, which group responses based on their answer scores, reject the notion that these means are merely an artifact of large 'extreme' segments on both sides that cancel each other out statistically: the vast majority of respondents align at or very close to the middle of the scale, resembling a normal with relatively steep bell curve. In all countries, more than half of those surveyed gave 4, 5, or 6 responses;<sup>90</sup> in Belgium, the Netherlands, and Switzerland, up to two thirds of respondents. If we look at the average across countries, six out of ten voters (59%) prefer the status quo between spending and taxes, while one in four wants more spending (and higher taxes). A mere 16% prefer lower taxes at the cost of reduced spending, and while this number differs slightly across countries, it aligns close to the macro trend in all cases.

These results confirm what we suspected already: cutting taxes at the cost of other (spending) priorities is generally *not* a popular proposition among large segments of voters.<sup>91</sup> The majority wish to keep the status quo.<sup>92</sup> I use the term 'generally' very deliberately here, as there may be variations in just how unpopular different *ways* of cutting are. It may be a good time to point out that the ESS question approaches the tax question in the broadest possible way; it does not look at support for the specific policy solutions that we have

<sup>&</sup>lt;sup>90</sup> They represent three of the 11 possible replies, and it does not require extraordinary mathematical skills to see that if answers were distributed randomly, or close to it, the share of respondents aligning in these middle categories would be *much* less than half.

<sup>&</sup>lt;sup>91</sup> Another interpretation of these numbers is to say that there is a non-trivial residual share of voters that actively push for tax cuts. From what we know of partisan representation (see **Chapter 3**), we expect the Right's core voters to be overrepresented in this group.

<sup>&</sup>lt;sup>92</sup> A strong *status quo bias* or *reference point bias* among individuals is well documented in political life and in various economic and psychological settings, as originally suggested by Daniel Kahneman and Amos Tversky (1979). One can speculate if this is the dominant explanatory mechanism at play here, although the notion that voters 'know what they have, not what they are getting' makes a lot of sense in my view.

established they may choose from.<sup>93</sup> I reference my prior discussion on the population of income tax strategies (in **Chapter 2**), which may in terms of their political feasibility. I expand on these arguments in the subsequent chapter sections.

What are the implications of politics? If we return to the initial question why the Right does not simply slash income taxes when presented with the opportunity, we can now name several constraining factors. The party leaders of the Right are not political novices, and cutting income taxation is not only associated with tangible opportunity costs in terms of what other policies that must be sacrificed, it invites political resistance from both the average voter and the Left. Alas, we should expect pursuing tax cuts to be a difficult and potentially costly enterprise for the Right.

### 4.2 Right parties and their ideal reform strategies

The highlighted constraints are indicative, in my view, of a schism the Right faces between which policies they wish to pursue in the absence of such factors, and which policies they seek because of them.<sup>94</sup> To me, it is a necessary thought experiment to consider, as we can sometimes observe a large gulf between the Right's 'broad vision' rhetoric on (income) taxes, and what they actually accomplish if we measure the concrete legislative wins. It sets up a framework for studying what causes this disconnect, the whole in-between process of politics.

Before I dive further into the Right's preferences at the different stages of politics, I will elaborate on how I understand and employ the term 'preferences'. My intention is to stay true to the actual meaning of the term, i.e. a greater liking for one alternative over one or more other alternatives. Yet, many spatial models of policymaking rely on this notion that parties and elite actors have fixed 'ideal points'. I am, generally, skeptical of this, since an approach that looks only at actors' 'first choice' preferences may fail to consider how specific issues and policy solutions reach the political agenda in the first

<sup>&</sup>lt;sup>93</sup> The ESS survey question does also look at *income* taxes specifically, as this dissertation does, but treats taxes as a broader entity. The survey planners may have had good reasons to choose this general question frame, but it causes confusion about what precisely respondents weigh in their responses. As I argued in **Chapter 2**, income taxation is probably among the first to come to mind when one discusses taxes. In any event, it is rare to find surveys, especially vast cross-national ones, that specify different tax types and instruments.

<sup>&</sup>lt;sup>94</sup> Or to frame it in another way: between their 'first choice' of policy and what they see as more feasible policy options that have a better chance of surviving the political process.

place. How a solution presents itself for a vote may lead the same set of decision makers to endorse vastly different policies. I am much in line with Hacker and Pierson's (2005) assessment of such collective choice situations, as they have argued that politicians' exact preferences are less critical to think of than their 'zones of acceptable outcomes' – 'those outcomes that they will accept in a choice between the default position and that alternative' (ibid.: 42). Here, we can substitute the term 'default position' with the policy status quo. But these outcomes can be ones which consider distinctly second-best. Such zones of acceptance are usually much more fluid, amorphous, and permissive than politicians' ideal points, reflecting not just the preferences of the individual or collective actor, but also shifting economic, electoral and coalitional settings that require difficult tradeoffs.<sup>95</sup>

With that said, I still believe it is an instructive conceptual exercise to contemplate first which policy the Right would turn to if nothing was in their way. This task of disentangling the 'ideal' policy preferences of the Right is, of course, not an easy one, in particular due to two set of circumstances. First, everything we can reasonably observe on what the Right, in principle, wish to do policy-wise is already shaped by the existing context of politics. The two cannot be studied separately. It implies, for example, that public displays of preferences available to us, e.g. party manifestoes, speeches, political debates, are constructed in those real-world political settings with all those potential constraining factors I just listed. It is, thus, difficult to imagine that one can tap an unpolluted measurement of what the Right and its elite actors would do if we, say, took away the budget constraint and the strong political opposition groups. To get closer to a valid answer, one could try to talk directly to the relevant political actors – party leaders and other high-ranking party officials - to separate ideal preferences from second-order ones. While it is an issue such actors might prefer to talk about behind closed doors, access to high-level politicians is still difficult to come by. Even if access is obtained, it is difficult to differentiate between mere storytelling (and ex post justifications of certain decisions as outcomes 'they desired all along') and facts (Wenzelburger 2011: 1160). It is likely that even those caught in the middle of events are so heavily

<sup>&</sup>lt;sup>95</sup> Elites may thus try to fill the agenda with their acceptable options and to keep off less desirable options that they would otherwise feel pressure to accept. According to Hacker and Pierson (2005: 42), they can also use policy framing and design to expand other politicians' zones of acceptance. By placing alternatives within a larger frame that makes it difficult for fencesitters to adopt a stance of public opposition (i.e. 'tax cuts: yes or no?'), the one setting the agenda can often create significant leeway to craft policy details – especially when they are able to lessen the visibility of the thorniest tradeoffs (ibid.: 42).

influenced by what goes on in their political surroundings that they cannot themselves think of specific political solutions that disregard them. It renders it a near impossible exercise, then, to nail the Right to one ultimate set of concise policy goals that are detached from the case(s) one is studying.

Second, preferences over income taxation are tough to separate not only from *politics* but from existing *policies*. Existing tax rules, which a country has in place, become the yardstick for elite actors to draft and evaluate new proposals. Another way to frame it is that ideas for reform are simply not drawn at random from a pool of possible solutions; they are, most often, proposals of marginal change that either add to or subtract a little bit from what is currently there. Then the comparison between the 'before and after' is made. For example, does a party's bid for income tax reform raise or lower income tax rates compared to the policy status quo? Does the party's bid, if we look at its policy effects, boost or harm economic growth in society?

It is not difficult to see why such a reference point is needed when we talk about preferences. Because tax rules differ across countries, so should both the 'true' tax preferences held by the Right and the reform strategies they pursue. A certain rate or tax bracket may exist in one country and figure as the Right's prime reform target but may not exist in the next country where the Right, as a result, will be more preoccupied with cutting income taxes by other means. Against this backdrop, I do *not* claim that we cannot draw any generalizable conclusions on the Right's preferences; I expand on how specific tax institutions shape what reform-willing policymakers should choose to target in the coming sections. Further, I do, still, think there are commonalities to how Right parties should generally attack the income tax question regardless of their varying starting points.

It traces back to their shared causal beliefs. Because the Right expects positive economic consequences of lower taxes, I posit that they work, from the outset, to change those policies that are associated with the largest potential policy effects (in the positive direction from their point of view, obviously). **Table 2** in **Chapter 2** neatly summarized the list of potential reform measures available to them in 'standard settings', identifying six main policy parameters they can tune: three versions of the tax rate (R) (the rate on the tax bracket below, containing, or above a particular wage earner's income), two versions of the bracket thresholds (T) (the threshold limit on the bracket below and containing the wage earner) and the size of the personal allowance (PA). It is not difficult to see which of these the Right, on paper, should have the greatest affinity for changing. What counts the most, in terms of policy effects, are the marginal tax rates,<sup>96</sup> and as mentioned earlier, the surest way to reduce them is simply to cut statutory rates as much and as widely as possible. Lowering the rate implies shifting the tax schedule downwards, reducing the marginal rate of income tax paid across the entire tax bracket in question. The policy is expected to carry adverse effects on redistributive outcomes in a lot of instances, yet the Right sees them as legitimate and a cost worth paying, as long as they are produced by a free market with fair competition.

When it comes to lowering taxation by raising the threshold limits on tax brackets, effects on economic incentives, and redistribution for that matter, work along the same lines but in smaller magnitude. Raising thresholds implies moving the tax schedule rightwards in a horizontal manner. As shown in **Section 2.4**, such policy only affects the marginal rate for those specific taxpayers just above the existing threshold limit who now find themselves in a new tax bracket with a presumed lower marginal rate than before. Such incentive effects do not extend to taxpayers across the whole tax bracket in the same way as with rates. I argue, therefore, that the Right, if allowed to choose without fiscal and political constraints, would generally prefer lowering income tax over raising thresholds.<sup>97</sup>

An important adjunct is, of course, that the expected policy impact depends not only on the choice of instrument, rates versus thresholds, but certainly also on its location on the income scale. Evidently, cutting the bottom (or base) rate should not have the same incentive effects as cutting the rate at the very top. For example, low-income earners are unaffected by cuts to rates that apply to the richest taxpayers only.<sup>98</sup> One could speculate long and hard

<sup>&</sup>lt;sup>96</sup> To reiterate a key point, the Right does not simply go after marginal rates, because it is what mainstream economy theory teaches them is the key parameter affecting marginal decision-making. It is a pursuit that is reinforced by their deep-seated causal beliefs, it seems, on the virtuous micro and macro level economic effects of lower marginal rates.

<sup>&</sup>lt;sup>97</sup> One key aspect not featured in the trade-off, as presented here, is obviously the *size* of the proposed policy change. If the Right faced a choice between one policy that involved large rises in the threshold limits of tax brackets and another that involved only a miniscule reduction in tax rates, I would naturally expect them to lean towards the former, with size overwriting any affinity for certain instruments. The preference of rates over thresholds hinges on an 'all things equal' assumption on this variable.

<sup>&</sup>lt;sup>98</sup> As stated earlier, we cannot draw the similar conclusion for the reverse case, since rate cuts at the bottom benefit the rich as well, as they pay a lower rate on the subset of income that falls into these particular brackets. Their marginal tax rates, crucially, are unaffected.

on whether the Right is equipped with a general preference on how to prioritize between cuts at the different ends of the income scale. The goal of taxing as 'flatly' as possible, i.e. lowering the tax rates at the top (close) to the same level as those at the bottom, is a notion supported by Right claims of tangible efficiency gains, since higher marginal rates are continuously more damaging to economic activity, and it is obviously also backed by the representation logic, as the Right still caters to a large share of the medium-to-high income taxpayers. Yet, as I make clear later in this chapter, I think policy legacies too play a crucial role in explaining just how much the Right is oriented towards the specific segments on the income scale.

# 4.3 Bringing in the politics: the visibility and feasibility of rates and thresholds

At this point, the arguments I have presented on how to distinguish between instrument types are largely still in the economists' court. This is to say we can borrow from their theories to establish the expectation that tax instruments vary with regards to their effects on efficiency, equity, and revenue intake. We can, of course, add a 'beliefs' layer by stating that the perception of both the size and importance of each effect differ depending on the beholder. For example, the Right is expected to care much more about the potential efficiency gains stemming from low taxes and to anticipate much larger such effects than their Left counterpart.

I argue that we need to add an additional political layer to this discussion about why instrument choice matters that much. It considers the notion of political costs, which we have been circling at this point, more explicitly. In my view, it is tough to reasonably describe the whole politics surrounding income tax reform without first recognizing that these different instruments, i.e. the rate and the threshold, are not governed by the same political logics. They are talked about in dissimilar ways, and they certainly do not spark the same level of conflict when brought onto the political agenda. I think *that* realization is crucial to explaining, for example, why the Right, despite their affinity for lower marginal tax rates, often end up settling for less. In a nutshell, politics can trump, or at least heavily moderate, pure economic considerations. This assertion is rather simple one, but it is a novel contribution to a tax literature that generally lacks good theory to explain 'the political salience of different types of taxation' (Barnes 2018: 14).

One of the dissertation's main contentions is the two cruxes of income taxation and that each type of instrument has built-in qualities that make them more or less *visible* to its recipients, the taxpayers, understood as how easy it is to grasp in what way reforming them impacts the tax liabilities on those groups the reform is intended. Can one, for example, easily link the policy change to whether affected groups must pay more or less taxes going forward? Similarly, there are qualities that make them more or less politically *feasible*, i.e. the immediate fiscal and political costs to reforming them. For example, how likely is it that changing that particular instrument would spark significant political backlash in the process or would be enormously expensive in terms of forgone revenue? While the two components, visibility and feasibility, are separate qualities in theory with their own causal mechanisms, I argue that they tend to go together when we study the main instruments of the income tax code. I posit that changing tax rates is both a *more* visible and *less* politically feasible way of reforming the income tax system. More, I posit that changing threshold limits is a *less* visible and *more* feasible path of reform.

How the Right chooses to design income tax reform should, therefore, weight potential economic benefits against these more political considerations. In the same manner that Right elite actors wish to lower marginal tax rates as much and as widely as possible, they are certainly also keen on changing policies by using strategies that augment their connection to more popular elements of reform while distorting, hiding or not engaging in the more unpopular initiatives to avoid electoral punishment. My arguments thus rest on the key proposition that steep tax-cutting reforms are not particularly popular among the majority of voters; a notion that is well supported in cross-national surveys, as previously shown.

The visibility argument bears strong resemblance to the core claim of Pierson's (1994, 1996) classic argument on 'the new politics of the welfare state' that focuses on spending-side politics. A prerequisite for the electorate to punish politicians for enacting unpopular policy is that voters are able to link events such as a declining standard of living to specific policy choices and, in the end, individual politicians and parties (Jensen, et al. 2018: 163). Without this 'causal chain of responsibility', voters cannot react to the changes they oppose. According to Pierson (1994: 20): 'those engage in efforts to initiate unpopular policies will try to lower visibility of their reform by complicating the reconstruction of causal chains that would allow voters to exact retribution'. In my view, the logic should travel rather smoothly to the study of income taxation. Case studies (e.g. Bartels 2005, Hacker and Pierson 2005) have already convincingly shown that the deliberate crafting of policy design - and the blurring of perverse policy effects - can mitigate the potential backlash for the type of tax-slashing reform that only a small minority of voters would support if they were given a larger palette of reform options from which

to choose.<sup>99</sup> We know from the blame avoidance literature that there are different ways to achieve causal blurring,<sup>100</sup> but the most straightforward is to select policy instruments that by design make it difficult for voters to evaluate the negative effect, or unpopular elements of a reform (Pierson 1994; see also Weaver 1986). In turn, the more visible instruments can be used to attract credit claiming when such opportunity manifests itself.

If we dive further into this visibility claim, at least three dimensions point to why the rate is the more visible instrument choice. The first pertains to how frequently the instruments are presented to the taxpayers. The rate is arguably the fundamental feature of the tax code, as it figures front and center on monthly paychecks, the tax bill taxpayers are most accustomed to seeing. Taxpayers will, if they pay slight attention, notice whether their statutory rate has been increased or decreased. In contrast, the threshold limits of tax brackets are usually not explicitly reported on paychecks. Instead, they are figures tied to taxpayers' annual income. Taxpayers need only to juggle these numbers a few times a year (when filling out their advance statements and tax returns), and individuals will likely not pay as much attention to the change in such figures if they only change slightly from one year to the next. I posit that the general awareness about the specific monetary values that decide when one tax bracket begins and another one ends will be lower than the collective knowledge of the 'ongoing' rate at which newly earned income is taxed.<sup>101</sup>

<sup>&</sup>lt;sup>99</sup> Both studies look at the 2001 Bush tax cuts and conclude that this bill passed although the content was sharply at odds with broad public preferences. It did so largely by virtue of its policy design. Central features of the reform cannot be explained without taking into account how Republican legislators, among other things, 'front-loaded' cuts to marginal tax rates on the bottom 80 percent of the income distribution, while gradually phasing in significant tax cuts for the wealthiest Americans over the long run (Hacker and Pierson 2005). The cartoon featured in Larry Bartel's article illustrates this point with humor. Homer Simpson, the common man, does not recognize that he is being robbed. He is happily celebrating his visible, immediate, but relatively modest tax cut, but he fails to see the less visible, less immediate, but much larger rewards reaped by Mr. Burns.

<sup>&</sup>lt;sup>100</sup> The strategies generally come in three broad categories: *manipulating procedures* of political decision-making, *manipulating perceptions* of those who are adversely affected by reform, and *manipulating payoffs* by tweaking the incidence of gains and losses among those targeted (Pal and Weaver 2003, Vis 2016).

<sup>&</sup>lt;sup>101</sup> Further, the simple interpretation of numbers may contribute to voters reacting more strongly to rates. The rate is, by definition, bounded between 0 and 100 percent, and a 1 percentage point change on the scale is perhaps easier to comprehend and remember than if, say, threshold limits, typically a large monetary amount in the

The second dimension taps into how interpretable the two sets of instruments are in terms of causal impact. Starting again with the rate, altering this parameter should have consequences for the taxpayer's living standard that are relatively easy to comprehend; if the rate goes down, the immediate disposable income increases, and vice versa. The direction of the policy change is thus linked to the person's tax liability: a lower rate means fewer taxes to pay. It is an uncomplicated mechanism. In contrast, decisions on tax thresholds, at what income level a certain tax rate kicks in, are more difficult to comprehend. Lowering or raising the threshold on the top marginal income tax, for example, alters the tax burdens on high-income earners, even if the rate itself remains constant. More importantly, there is an opposite rather than a symmetrical relationship between the policy direction and tax liabilities. Policy that increases the (upper) threshold limit has the effect of lowering taxes on the richer taxpayers, as per **Table 2** in **Chapter 2**. This causal impact is, hence, not obviously intuitive. Trained students on tax matters, and hopefully those who have attentively read the dissertation thus far, will likely get the basic mechanism right, but I posit that the average taxpayer struggles with technical terms such as 'expanding the tax base' or 'raising the threshold' and with grasping their policy impact.<sup>102</sup> A non-trivial share of taxpayers will likely adopt the strait-up false interpretation; confusing a raise in the threshold limits with a higher tax liability, and vice versa.

The third dimension relates to the political nature of how each instrument must be changed (from the status quo) in order to impact taxpayers. It may sound like a banal issue, but it makes a vast difference in terms of the overall visibility. The rate is, also in this respect, easiest to monitor. Statutory tax rates are legislatively decided upon, and their obvious, but certainly not unimportant, feature is that they stay at the exact same level until the policymakers decide to alter them. If the top marginal tax rate is at 40%, it stays there until it is actively changed.<sup>103</sup> It is, again, not the case with thresholds limits. It is true that the nominal levels are set by legislators, but the complicating factor is that the impact of thresholds on tax liabilities is as much a function of changes in income. Since nominal income levels are generally rising over time,

tens and hundreds of thousands (depending on the value of the currency, of course), were raised or lowered by the same percentage change.

<sup>&</sup>lt;sup>102</sup> I have spent three years scrutinizing the causes and effects of income tax policy and will still sometimes struggle with intuitively grasping this odd relationship, a positive policy change (higher threshold) causing a negative policy impact (lower taxes), before I sit down, concentrate and mentally disentangle it.

<sup>&</sup>lt;sup>103</sup> The key proposition is that any such reform of the rate is expected to generate political scrutiny.

even political non-decisions on adjustments of tax thresholds become vital and hence an expression of politics, as more and more taxpayers will be pushed into a higher tax bracket, a phenomenon known as *bracket creep* or *fiscal drag* (Alt, et al. 2009: 1218). Indexation, a prime example of a so-called 'invisible' policy instrument (see e.g. Pierson 1994, Lindbom 2007, Green-Pedersen, et al. 2012), is a popular tool to circumvent 'tax hikes by default', but then the choice of adjustment rate is obviously key. If threshold limits are made to increase a slightly lower rate, it will probably escape the notice of most taxpayers, especially because the effect will manifest itself over years. Thresholds that are indexed at a lower rate than the rate of rising incomes will entail a sizeable increase in tax liabilities over the long-term and, hence, declining living standards.<sup>104</sup> Yet at that point, it is not clear from the point of view of the taxpayer where to direct the blame.<sup>105</sup>

These three parameters – frequency of exposure, interpretability, and mode of policy change – all pull in the direction of rates being the more visible instrument. To rank them is, of course, an exercise of comparison, and my arguments, as they are presented, reveal little of the instruments' absolute level of visibility however one operationalizes and measures it. Is the rate, for example, actually visible in a meaningful sense, or is it just the less tough of two difficult concepts to grasp? Yet to me, the comparison between them is the whole point. Why I see the need to mention this is because a relatively long literature subscribes to the view that taxpayers' knowledge is defined by cognitive biases and limitations. These types of accounts tend to emphasize that

<sup>&</sup>lt;sup>104</sup> Quite analog to the discussion of 'creeping disentitlement' on social benefits that are indexed *not* to rise at the same level as wages, hollowing out the recipients' purchasing power over time (van Kersbergen and Vis 2014: 180)

<sup>&</sup>lt;sup>105</sup> Countries generally deal with this issue of threshold adjustment in different ways. An automatic adjustment of income tax brackets to price or wage developments is legally binding in many OECD states, including the Scandinavian countries, the United Kingdom and the United States (OECD 2007). Here, the ongoing adjustment of tax thresholds is expected to be partly outside the control of policymakers. However, the adjustment yardstick varies; in Denmark, all thresholds in the personal tax law are regulated by the so-called §20 rule that indexes them according to the wage development in the private labor market, while the United States indexes tax brackets according to the price changes captured by the CPI, the growth rate of which is typically lower than for that of wages. Countries with no regular legally binding tax bracket indexation, like Germany and France, update threshold limits more sporadically to keep up with inflation. As far as I can tell, no analyses prove that either type of indexation policy is associated with more or less fiscal drag over the long run. However, there are good reasons to expect that an ongoing adjustment of bracket limits generates less political scrutiny from taxpayers.

most ordinary citizens are remarkably ignorant about the complex workings of the tax code and the policy options under consideration (see e.g. Sears and Citrin 1985, Roberts, et al. 1994, Bartels 2005). The conclusion drawn from these studies is, basically, that politicians can manipulate voter attitudes in any fashion they see fit to get the reform they seek, which would not be possible if voters actually knew what was transpiring. While it should not surprise us that such shortcomings exist in the tax realm, this maxim that public opinion about tax policy is a very fragile construct certainly has nuances. My point is not that everything within the tax code is the same perplexing mess; some components are really hard to grasp, while others are easier. We should acknowledge that.<sup>106</sup> Further, while I do buy that taxpayers' knowledge of specific tax solutions can be relatively limited, if measured as the share of people that truly 'gets' these, it is not the only way that voter preferences (understood as a broad term) set up boundaries for what politicians might try to do. We know, for example, as we saw in **Table 5**, that voters are adverse to reforms that lower taxes by cutting spending, and they have very settled opinions on that matter. It certainly constricts the space of possible reform proposals from the outset of what policymakers can suggest and reasonably expect to get away it. Further, voters have strong opinions regarding, for example, the broader inequality question, as a large and stable majority of citizens across countries wants governments to take measures to reduce the current differences in income levels.<sup>107</sup> Again, the Right must take such views into considerations before they draft their exact policy intervention, even though they can probably mask some of what they wish to achieve using more invisible policy tools.

As noted, the immediate fiscal and political costs of instrument choice on top of these ascribed differences in visibility is a separate issue to consider. We are pretty familiarized with how these costs work at this point, referencing the tax trilemma described in **Chapter 2** and **Chapter 3**, but what we have yet to consider is how they may differ across the two main instrument types. Overall, I posit that reforming income taxes relying on cuts to rates is less politically feasible than reforming thresholds, especially for Right policymakers. Cutting

<sup>&</sup>lt;sup>106</sup> I am actually much in line with Alan Lewis' (1982: 71) classic summary of the tax issue: 'We have to accept that attitudes towards taxation [...] are based on less than perfect knowledge on the part of taxpayers. More realistically, attitudes should be examined for what they are – a product of myth and misperception.' I merely wish to add that the level of misperception is a factor that can meaningfully vary across the instruments within the tax code.

<sup>&</sup>lt;sup>107</sup> Using the same ESS survey data as in **Table 5**, 69% of respondents across the 13 countries surveyed either 'agree strongly' or 'agree' with this statement. Only 15% reply either 'disagree strongly' or 'disagree'.

income tax rates is thus a two-edged sword when it comes policy consequences; it is associated with all the positive economic incentives and behavioral responses the Right holds dear. Yet at the same time, the move will often have a large negative impact on redistribution, which will leave them politically exposed. The reason I use this relatively vague language is, of course, that not all cuts to statutory rates hurt the quest for equity as much. As a rule of thumb, we can predict that the higher towards the top of the income distribution, i.e. the higher the tax bracket(s), cuts are targeted, the more inequityinducing the policy will be. The reference case is the top marginal tax rate for the highest tax bracket. Cutting it involves an immediate increase in the posttax incomes of individuals in this bracket, increasing income differences between top and bottom, all things equal. While there surely may be benefits to this policy, it is easy to see how the political rivals on the left can paint the Right as a party that only caters to the richest of the rich and is not at all interested in the needs of the majority. It is bad politics, to put it bluntly, and something that risks hurting them both in the polls and in the ballot box.

We can probably agree that it is better politics to abandon those at the top and direct the cuts to statutory rates at tax brackets situated at the bottom, e.g. the basic rate. It does not significantly increase the level of inequality in society, and it is much easier to sell the policy as 'a rising tide that lifts all boats', shielding the Right from potential backlash. Yet, as I sketched in **Chapter 2**, such policy carries immense fiscal costs, because everyone gets a piece of the tax cut. The size of the cut is calculated on *all* earned income that falls into the particular tax bracket (times the size of the reduction in the tax rate). When it comes to feasibility, the Right is left with two non-ideal options on rate cuts: prioritize very wide, which is a hugely expensive proposition in terms of revenue losses, or prioritize the top, which is hugely unpopular.

Things look less bleak for thresholds. Because cuts here, i.e. raising threshold limits, merely shift the tax schedule horizontally, both the positive effects on efficiency as well as the negative effects on inequality and the amount of revenue raised are more modest in comparison. I argue that it makes them easier to swallow politically, because they carry less immediate drawbacks that tempt to activate political resistance. Further, it may be easier to spin such cuts via thresholds as a desirable policy that most people would intuitively support. For example, if one pushes a proposal to raise the top tax threshold, one could with some sincerity frame as a way to ensure that 'hard-working groups X, Y and Z should no longer pay the top marginal tax'.<sup>108</sup>

<sup>&</sup>lt;sup>108</sup> Though it will still count as a tax cut on the richest taxpayers on that subset of income that is no longer liable to the top tax.

**Figure 6** summarizes my arguments on the politics of instrument choice. It spatially aligns the two, if we assume that visibility and feasibility are constructs that can be scaled and ranked. Again, the more important thing is the relationship between them: the rate is the more visible and less politically feasible of the two. This novel approach to studying income taxation carries significant implications for how we should expect policymakers of all cloths to go about crafting new policy. The political considerations are as real as the purely economic ones, and politicians risk walking into a political minefield if they disregard the former. It implies, more specifically, that if Right elites want to pursue a first-choice strategy of slashing marginal tax rates, they will likely have to prepare for an uphill political battle. It is not a policy on which they can expect to 'credit-claim'.

**Figure 6** Sketched summary of instrument qualities with respect to visibility and political feasibility



## 4.4 Key tax institutions: the number of tax brackets and progressivity

At this point, we have derived two sets of propositions that need to be paired more explicitly. The first is that Right actors face a cross-pressure between wanting to cut income taxes in certain ways that are hard to pull off politically. The second is that countries' tax codes vary considerably, giving political actors vastly different starting points for altering existing policies. One obvious next step is, therefore, to consider how such tax institutions, specifically, affect the Right's incentive structures and strategies. Or in other words, why we should expect them to act differently across institutional contexts. Because tax systems are so complex, there is almost an infinite number of possible institutional features one can highlight to make the argument that they in some manner shape the political strategies and outputs we can observe across countries. It leaves a daunting task for the researcher. My approach was to look at relatively simple and familiar institutional constructs that, first of all, made sense from a comparative perspective.<sup>109</sup> But armed with theory only, it is difficult to sort out which factors to focus on and which ones to neglect. I began with a relatively exploratory approach and studied both macro policy trends and in-depth case studies, before I noticed two types of institutions that proved good at both explaining the policy dynamics we can observe across countries, and which provided a framework for understanding the subtle differences with regards to how the Right acts: (1) the number of tax brackets featured in countries' tax codes, and (2) the level of progressivity built into the tax schedules.

The number of tax brackets is the simplest to explain; it is merely a matter of counting how many income tax brackets have their own specific marginal rate in a given country year. It is the parameter j as defined in **Chapter 2**. What value does this parameter typically take, and what is a small or large parameter value? In the sample of 21 OECD countries selected for this dissertation, the median number was five (non-zero) income tax brackets in 2018. The minimum was two brackets as in the cases of Denmark, Iceland, Ireland and Sweden, while the highest was 18 (!) in Luxembourg. Not surprisingly, it is a fairly stable institutional trait as revealed by **Figure 7**, which shows the bivariate relationship between number of tax brackets in 2000 and in the final year of available OECD data. <sup>110</sup> Countries align either on or close to the 45-degree reference line, which indicates the perfect overlap between the two data series. In other words, the number of tax brackets a country had in 2000 is a fairly strong predictor of the same number in 2018. Inspecting **Figure 7**, we cannot draw a clear-cut conclusion on whether the number of tax brackets has

<sup>&</sup>lt;sup>109</sup> In other words, I needed to find one or more institutional features that not only bore relevance to the idiosyncrasies of one country's tax code but would also reasonably describe the many.

<sup>&</sup>lt;sup>110</sup> For the 19 countries (excluding the policy outliers Switzerland and Luxembourg), the bivariate correlation between the two yearly cross-sections is 0.54 (p-value < 0.05), not perfect proxies but a pretty high correlation. If we include Switzerland (10 brackets in 2018) and Luxembourg (18) in the sample, the correlation augments to 0.91.

generally gone down for this sample of countries, as roughly a same amount of countries aligns on either side of the 1:1 reference line.<sup>111</sup>



**Figure 7** Bivariate relationship between the number of income tax bracket in 2000 and 2018

#### Source: Own visualization based on OECD (2019b).

**Notes:** N = 19. The figure markers are jittered to avoid overlays. The dotted line represent the 45-degree reference line. Switzerland and Luxembourg are excluded from the figure because of their much higher than average number of brackets (in both years), as their inclusion distorts the visible relationship between the other 19 countries.

Because I define the number of tax brackets as a key institutional factor for my argument, it is natural to wonder what the cause of the country ranking on this variable is. Because they are certainly not randomly distributed, as we can tell. Developing a theory that explains this institutional variance is an ambition undertaking, certainly worthy on scholar interest in and by itself, but it is simply outside the scope of this dissertation.<sup>112</sup> Instead, I treat the number of

<sup>&</sup>lt;sup>111</sup> Belgium, Denmark, Finland, France, and Spain all had a higher number of brackets in 2000 than in 2018, which tells us that their schedules have been simplified according to this parameter. These are the cases below the 45-degree line). In turn, Austria, Canada, Japan, Norway, Portugal, and the United States all had a higher number of brackets in 2018 than in 2000 (above the 45-degree line). Among the 19 countries in the mean number of brackets was 4.11 in 2000 and 4.37 in 2018.

<sup>&</sup>lt;sup>112</sup> OECD reports show that while the number of tax brackets in PIT schedules certainly came down in the 1980s, where it was common for countries to have more than 10 brackets, the number was scaled back the most in those countries that to this

tax bracket as an exogenous component in theoretical framework. Given the remarkable stability in country scores, essentially from the 1990s onwards (OECD 2011b: 30), I believe this decision is justified.

The second factor, progressivity, requires perhaps a little more explanation than the mere number of tax brackets. The term refers to the profile of income taxes payments – how large a share of taxes is paid by different income groups. For example, to what extent do the rich pay relatively more taxes than the poor? One common way to compute this measure is analog to the Gini coefficient of household incomes, as one can use cross-national income distribution surveys to create a metric indicator of the distribution of tax contributions (according to incomes). Here, a score of zero means that all income groups in society pay an equal share of income taxes, while a score of one implies that one individual at the top pays all income taxes in society, i.e. the most progressive system possible<sup>113</sup> Due to extensive sampling and data that go into this computation, data on tax progressivity are typically not available on a year-by-year basis. However, the OECD's (2008a) report Growing Unequal? holds progressivity measures for most member states, which time-wise refer to surveys conducted in the mid-2000's.<sup>114</sup> When they calculate these concentration coefficients for tax progressivity, the United States comes out as the country with the most progressively distributed household taxes,<sup>115</sup> in part reflecting the greater role played by refundable tax credits, such as the Earned Income Tax Credit (ibid.: 104). The United States is followed in terms of progressivity by the other English-speaking countries together with Italy. In turn, taxes tend to be least progressive in the Nordic countries, France and Switzerland, where income tax burdens are more proportionally spread. It seems counterintuitive and is a redistributive puzzle that the literature as noted has studied meticulously, but as Kenworthy (2009) and others have

day the highest numbers (OECD 2011b: 30). Consequently, the order of countries, if ranked according their bracket number, has not changed much since the early 1980s. <sup>113</sup> In theory, we could imagine negative scores as well if income taxes were regressively distributed, i.e. lower income groups pay relatively more than top income groups. The different data sources on tax progressivity show, however, income taxes are virtually always progressive to some degree.

<sup>&</sup>lt;sup>114</sup> Another available source is the LIS 'Budget Incidence Fiscal Redistribution Dataset on Income Inequality' (Caminada, et al. 2017) that contains multi-year measurements of Gini coefficients and progressivity measures on both transfers and income taxes.

<sup>&</sup>lt;sup>115</sup> Household taxes here contain both income taxes and employee social security contributions.

shown, it is via social transfers, not taxes, that is the locus of inequality reduction in OECD countries.<sup>116</sup>

Before turning to the question of how each set of institutions shapes the mode of politics, let us first establish the relationship between them to make sure they are not merely picking up the same underlying variation. One could posit that it is a strong correlation, as having more brackets would allow one to create a tax schedule with a progressively steeper marginal rate that will ensure that tax burdens are skewed towards the top. The data reveal that there is something to this story, but it is clearly not a perfect relationship. This is evident from Figure 8 which shows the relationship between tax progressivity and the average number of income tax brackets from 2000 to 2010 for the sampled countries.<sup>117</sup> While countries with more progressive systems generally tend to have more income tax brackets, there are plenty of country cases that distort this trend.<sup>118</sup> For one, countries like Belgium and France have a much less progressive distribution of household taxes than their tax bracket numbers suggest. Conversely, neighbors Ireland and the United Kingdom combine relatively high progressivity with a modest number of tax brackets. It therefore makes sense to talk about the two as if not orthogonal, then separate institutional dimensions.

Another question to consider is what characterizes tax systems that are low and high on progressivity, respectively, besides the number of tax brackets. Can we derive anything on their policy structures? This is a good thought experiment, because, in theory, a system can be progressive or non-progressive in several ways. What matters in terms of progressivity is (mainly) the *difference* between tax shares for incomes at top and at the bottom. A system can thus exhibit low progressivity in each of the following: if tax rates are low on both the poor and the rich, or if tax rates are relatively high on both groups. But which one are we, empirically, looking at here? The tax literature is quite clear on this issue. Countries with the lowest progressivity generate the largest tax revenues. To ensure this, marginal tax rates must generally be higher in these countries. It is also what we find when we inspect correlations between

<sup>&</sup>lt;sup>116</sup> From this, we cannot conclude that taxes are unimportant for inequality reduction. Because they are. But what matters most in this respect is their quantity, in terms how much revenue they raise, rather than their progressivity (Kenworthy 2009).

<sup>&</sup>lt;sup>117</sup> I choose to average the latter so this period's midpoint roughly corresponds with the measurement of progressivity, which builds on income sampling done in 2004 or 2005 for most countries (OECD 2008a: 43-46).

 $<sup>^{118}</sup>$  The bivariate correlation is 0.33 (p-value = 0.19) for the 17 countries in which we can track progressivity.

tax progressivity on one side and different indices for marginal tax rates on the other. If we take one of the most obvious indicators, the top statutory tax rate on income, we find a strong negative relationship between progressivity and marginal tax rates across 17 countries (corr = -0.51; p-value < 0.05).<sup>119</sup> A figure of the bivariate relationship can be found in Annex A.I. So we are generally looking at two things: (1) a group of countries with low progressivity in which marginal tax rates are relatively high on both low- and high-income groups; and (2) a group with high progressivity where taxes on the rich are actually lower than the average of other countries, but where taxes on the poor are *much* lower relatively speaking.

**Figure 8** Income tax institutions – progressivity and the number of tax brackets – across the OECD



Source: Own visualization based on OECD (2008a, 2019b).

Notes: Data on progressivity refers to the progressivity of household taxes in the mid-2000s for the working age population. Data for Portugal and Spain are not collected in the study and are therefore excluded from the figure. Iceland has the lowest score of 0.257, while the United States has the highest one of 0.549. Switzerland and Luxembourg are excluded due to extreme thresholds scores.

<sup>&</sup>lt;sup>119</sup> The analyses draw on OECD data on countries' top statutory tax rates from 2000 and the aforementioned tax progressivity measures. Iceland is a stark outlier here, combining low progressivity with low tax rates. If Iceland is excluded, the correlation augments to -0.66 (p-value < 0.01).

## 4.5 Optimal Right strategies in different tax configurations

Having identified relevant tax institutions, the next question emerges: what are the politically optimal settings for reform-driven Right actors who prefer lower taxes compared to the status quo (due to the *positive* incentive effects), and who prefer cutting rates rather than raising threshold limits (due to the *stronger* incentive effects). In which contexts are they most likely to get away with pursuing such policy?

My view is, as stated in the introduction, that the two sets of institutions shape the policy process surrounding income taxation in distinct ways that augment or constrict the political room to maneuver. To explain how, let us first dwell on what the number of tax brackets does. I posit that this parameter defines the slate of feasible instruments available to policymakers, including those on the Right. The extreme case is again the simplest tax system one can imagine, one flat-rate tax for all taxpayers regardless of their incomes.<sup>120</sup> In this system, the Right will struggle to find fiscally sound ways to cut tax rates on whichever targeted groups of taxpayers, as the prime instrument at their disposal is *the* rate, visible to everyone. If one wishes to cut the marginal tax rate, one needs to do it across the board, and even meager cuts for the individual involve enormous revenue losses for the state. We can, of course, say that if the Right had succeeded with implementing a proportional tax model instead of a progressive one, they would already have won the war and have little left to fight for policy-wise. The argument has its merits, but it does not change what we can expect in terms of the future policy dynamics; the Right will find it quite tricky to cut taxes further.<sup>121</sup>

In the second-simplest system – one with two tax tiers – the Right may target the basic rate, which applies to all taxpayers, the top rate paid by those at the top end, or alter the threshold limit between the bottom and the top bracket. The latter two seem like the natural policy targets of the Right.

<sup>&</sup>lt;sup>120</sup> Among the OECD countries surveyed, only Iceland has a flat-rate income tax policy in place for a few years during the run-up to the Financial Crisis (from 2006 to 2009). It then re-introduced two additional rates from the fiscal year 2010. Flat-rate systems have been tried elsewhere in the OECD, in particular in the Central and Eastern European post-Communist countries. As of today, countries like the Czech Republic, Estonia, Hungary, and Latvia all employ a flat-rate income tax system (OECD 2019b).

<sup>&</sup>lt;sup>121</sup> Accordingly, the Right may look to different options for cutting taxes in this scenario, for example by introducing group-specific tax allowances or tax credits that disproportionately benefit those they wish to target.

Though their likely first choice is to cut the top rate, we have made the general argument that it is a policy move that attracts significant risk of blame attribution and thus is less attractive. Cuts to the higher rate in this two-tier schedule quite visibly move the system visibly closer to a proportional one, which goes against the widespread electoral support for (more) progressive income taxation in virtually all OECD countries (Barnes 2015: 72). With few tax brackets, I therefore expect the politics of income taxation to switch to less visible forms of taxes such as the threshold limits, and the struggle should be more over *when* the top tax bracket(s) should set in.<sup>122</sup> Policy changes centered on the top marginal rate should be rarer.

Contrast these simpler systems to those that hold four, five, or more tax brackets. Let us just denote them as 'high B' systems. Here, the policy space for the Right is much less constricted, as they are left with many more instruments to 'work with' in terms of policy design. Since the brackets are, by definition, more narrowly defined, reforming a specific bracket's rate or threshold limit is generally less costly to cut from a revenue standpoint. The choice of which instrument to choose should also be less confined to thresholds only, because it is now possible for policymakers to fine-tune the rate of a single tax bracket without compromising the entire redistributive profile of the whole tax schedule.<sup>123</sup> Due to the wider policy space, I expect that the strategies of policy elites, including the Right, would feature a more balanced mix of policy changes in terms of rates and thresholds<sup>124</sup>. Further, it provides them with much better opportunities for designing tax reforms with multiple moving pieces that reward several key constituencies at once, increasing the odds that a broader political coalition will get behind them. A curious extension of this line of reasoning is that while a tax system with many brackets may serve the

<sup>&</sup>lt;sup>122</sup> For the Right, especially, the discussion on whether the top rate in the current tax schedule targets the 'right' segments of taxpayers should be less tough politically than discussions on whether the richest should pay a reduced marginal tax on all incomes. The location of T should also be key. If it is much closer to – or even below – the median wage earner, raising it becomes much easier to justify politically than if the top rate kicked in at very high wage levels.

<sup>&</sup>lt;sup>123</sup> The lower fiscal costs to cutting tax rates are perhaps what tip the balance for the Right elite to make it worthwhile to pursue this policy strategy, even though it is expected to yield political backlash (due to the higher visibility).

<sup>&</sup>lt;sup>124</sup> It is difficult to generally predict what the specific tipping point *is* in terms the bracket number that generates this switch from the 'threshold only' to the mixed policy strategy. Instead, I will express the mechanism in probability terms: each additional tax bracket in a given country's tax schedule augments the likelihood of observing this 'mix strategy'.

Right's political cause in one way, giving them the legislative flexibility to reform, it certainly clashes with another common stated taxation goal of the Right: to make systems so simple that virtually everyone understands them.

Turning to tax progressivity, I argue that this factor influences not so much instrument choice as it shapes policy attention that is paid to the tax burdens on respective income groups. To prove this point, it is once again instructive to contrast the cases defined by high/low progressivity, respectively. In highly progressive tax systems (e.g. the United States and Ireland, see Figure 8), where household taxes fall disproportionally on the highest income groups, the Right should muster a strong push for cutting income taxes on these particular income brackets. Due to the steep tax schedules found here, Right elites are better positioned to *sell* rhetoric framing the high marginal taxes at the top end (compared to the bottom rate policy baseline) as the chief structural problem of the income tax code. The plead can, for example, take the form of cutting taxes on 'job creators' or on 'the most productive' members of the labor market, perhaps accompanied by arguments that such cuts would end up 'paying for themselves' when the secondary effects on increased economic activities and additional revenue are factored in. To iterate, tax cuts at the top end should generally have a stronger political pleasing here.

In countries with low tax progressivity (e.g. the Scandinavian countries) and a more equal distribution of household taxes, the Right is not only preoccupied with how the tax slope affects work incentives among the highest earners. Easing tax burdens on low-to-middle income groups should be given more equal priority due to their relatively high marginal tax rates, the result of the much flatter tax schedule. There are, in other words, pressing issues at either end of the income distribution. For example, whether taxes discourage labor market entry for fringe groups<sup>125</sup> has become a major bone of political contention that often takes the form of a 'work versus welfare' trade-off. We should therefore expect the Right's tax focus to be broader, as I, more specifically, expect them to fight for widespread tax cuts for both low- and high-income groups. Introducing a tax allowance on earned income is one obvious strategy to strengthen work incentives towards 'the bottom' of the income scale. Further, because incomes taxes are more skewed towards low-to-middle incomes in the first place, I expect the Right's reform strategies to be more 'defensive' or politically cautious in these settings, since their opponent, the Left, has a more valid claim of forcing the rich to pay a higher share of the tax burdens. What may be the true token of success is if the Right can function as the political safeguard against raising income taxation.

<sup>&</sup>lt;sup>125</sup> Here, I refer to low income wage earners, the unemployed, or other groups receiving social assistance.

**Table 6** sums up my theoretical expectations on the Right's tax strategies in each of the four case archetypes we can derive from combining the two institutional dimensions. As revealed by how countries align empirically in **Figure 8**, each cell does not contain the same number of country cases, and plenty of them seem to be spaced just on the middle of one, if not on both institutional axes. But in terms of building a comparative theory, which is the pursuit here, it makes a lot of sense to start from the cases that are placed at the scale ends to expose what truly distinguishes them.

		Progressivity of the tax schedule			
		Low	High		
Number of brackets	Low	Thresholds cuts at the bottom and at the top	Threshold cuts at the top		
	High	Mix of cuts at the bottom and at the top	Mix of cuts at the top		

Table 6 Theoretical expectations of the Right's strategies in different tax regimes

If we start in the upper left cell of **Table 6**, we find the case configuration low on the number of tax brackets and low on progressivity (low B/low P), in which we find the Scandinavian countries as well as Austria. Here, I expect the Right's tax-cutting efforts to be centered on a strategy that mainly aims at raising threshold limits on tax brackets at both the bottom and the top of the income distribution. For example, by pushing the amount for when the top marginal rates kicks in but also expanding the 'tax-free' brackets at lower levels of income, whether in the form of a personal allowance, a work allowance, or general tax credits that are independent of income size. We should observe roughly similar strategies pursued if we turn to the upper right cell where we find the low B/high P configuration (Ireland and the United Kingdom). The low number of bracket still leaves Right politicians with a more limited policy space to operate within, so cutting taxes via thresholds is expected to be the norm. The efforts to cut should be more concentrated 'towards the top', that can take the form of strategies that minimize the amount of income subject to steep marginal tax rates, or that introduce specific tax allowances that disproportionally benefit the higher income groups.

In the lower right cell, the high B/high P combination features countries like the United States, the remaining English-speaking countries as well as Italy. Here, we should expect the Right's room for tuning the specific parameters of the income tax schedule to be much wider. It is therefore difficult to predict that the Right would target just one type of instrument, e.g. the marginal rates to which they are naturally drawn. We should expect a broader mix of tax cuts targeted at the relatively well-to-do groups, in the form of marginal rate cuts and policies that minimize the tax bases of the rich that face high tax rates. Finally, in the lower left cell in **Table 6**, we find the high B/low P mix that includes France and Belgium as the countries that clearly fit this profile. These are, generally, the hardest cases to predict in terms of policy strategies. The Right has many type of instruments at their disposal when seeking to reform, and they wish to do something about the high marginal tax rates on rich and poor alike. One could therefore expect a broad tax-cutting effort that takes many forms.<sup>126</sup>

Though the ideological core is the same, I expect the Right to operate in quite distinct ways across institutional contexts. Hence, the general theory on the Right and income taxation is not wrong, just because it manifests itself in different ways. This claim is backed by the empirical findings of the comparative analyses which I will unfold in the next two chapters. Further, the various strategies are perhaps most clearly distilled in the reform case studies (in **Chapter 7**) that allow a much deeper dive into the reform process. Let us dive into the data then.

<sup>&</sup>lt;sup>126</sup> As laid out earlier, we should therefore expect the tax strategies of the Right to be the 'cleanest' in settings with many brackets and high progressivity where they should be less constrained politically and motivated at the same time to pursue tax cuts for high-income earners. In turn, I expect strategies to be the most confined in few-bracket settings with low progressivity, as the Right needs to split the policy focus across different income groups and cut taxation via threshold limits rather than rates.

## Chapter 5. Using aggregated policy effects to study the impact of tax institutions

I proceed now to the empirical chapters of the dissertation. The next four chapters look at the Right's politics of income taxation and test my theoretical propositions from different levels of analysis. The **Chapter 5** and **Chapter 6** look at it from the comparative macro perspective; **Chapter 7** dives into tax reforms conducted by the Right in Denmark, the United Kingdom, and the United States; **Chapter 8** examines voters' perceptions of the two main tax instruments.

As told in the review of the empirical tax literature in **Chapter 3**, there is a deficiency when it comes to output indicators that tell informative stories about the income tax policy trends of recent years. To reiterate, we need indicators that do not merely reduce policy to a single catch-all metric, i.e. average tax rates but pick up the subtle but crucial distinction between rates and thresholds, and at the same time allow us to evaluate how policy changes affect taxpayers across income groups, whether unevenly or the same. Since no such measures are readily available from existing comparative sources, I construct novel ones that fit this exact purpose. Relying on raw data from OECD's Tax Database, I show how we can compute policy measures that decompose changes in income tax liabilities into what can be attributed to the legislative changes in rates and thresholds, respectively. The intent is to leverage all the information we can possibly obtain from studying year-to-year changes in countries' formal tax laws. I end up with two key policy indicators: the *rate effect* of policy change and the *threshold effect*. I provide a detail step-by-step guide of the many computation steps.

Next, I provide descriptive evidence and discuss the face validity of these measures. I find that they are best suited to be studied either by looking at the dependent variable as yearly reform events (is policy changed or not?), or by looking at the aggregated policy trends over a longer period of analysis. Each provides informative answers to the tax question, and the next chapters are therefore split between them: this chapter looks at the aggregated changes and what they can tell us about how institutional configurations 'steer' the policy trajectory over the long haul. **Chapter 6** is then devoted to reform events and investigates to what extent we can observe something systematic about what characterizes them, not least whether the presence of Right cabinets affects tax reform activities.

In this chapter, I derive a 'backdrop of facts' that tax students must be cognizant of when trying a comparative story of what has happened in recent years within this policy domain. In continuation of the introduction puzzle, I find that countries have taken guite different policy paths over the last twenty years when it comes to following a predominantly rate- or threshold-based reform track. This variation extents to the general reform scope as well, i.e. how much they have reformed income taxes altogether. Whereas there is little variation in the extent to which they have cut taxes by raising threshold limits, there is considerable variation in what they have done with tax rates. Countries such as Spain and the United States, for example, have severely reduced tax rates, especially in the top end of the income scale, while countries like Ireland and Portugal have raised them. I demonstrate that institutions to a large extent explain these varying patterns. A common trait for countries in the low B group, i.e. tax schedules with relatively few tax brackets, is that they do not experience any long-term cuts in income tax rates, while there is much larger variation, and hence more policy paths to take, within the high B cluster. On the other hand, the results of this chapter indicate no systematic link between countries' level of tax progressivity and the long-term distribution of tax cuts across income groups over this period.

#### 5.1 A new class of income tax measures

To test my logic of two cruxes of policy, the rate and the thresholds, I need dependent variables that pick up the subtle distinction. Yet as the current state of the partisan tax literature suggests, such are not easy to find.<sup>127</sup> The most commonly employed tax indicators fall, as shown in **Table 4** into categories of either aggregated revenue shares (such as the OECD summaries),<sup>128</sup> data on top statutory tax rates (e.g. on income or capital gains taxes), or effective (average) tax rates on some reference taxpayer. Each of them has their obvious shortcomings in terms of measurement validity. The measures study either policy outcomes instead of those legislative outputs policymakers can affect

<sup>&</sup>lt;sup>127</sup> The better part of my first PhD year was spent meticulously searching existing policy databases for suitable measures, resulting mostly in frustration and disappointment on my part.

<sup>&</sup>lt;sup>128</sup> Most notably, the share of income tax revenue, or total tax revenue, as percentage of GDP.
meaningfully and directly via the legislative process.<sup>129</sup> Or they focus on a single parameter (e.g. the marginal rate) within the complex income tax code with a multitude of instruments to target.

We cannot blame this 'issue' on a lack of multidimensional datasets either. In recent years, we have witnessed a great influx of novel comprehensive databases on comparative tax policies, indicative of the growing interest towards understanding their policy drivers. None of these, however, target the crucial variety at the instrument level. Laura Seelkopf and her many collaborators (2019) introduce their *Tax Introduction Dataset* covering the historic introduction of six major tax types in 220 countries, covering the period from 1750 to 2018. While the scope of their data collection efforts is highly impressive, the level of detail behind their income tax measure does not allow us to go into any policy dynamics that go beyond its mere introduction.<sup>130</sup> Andersson and Brambor's (2020) *Financing the State* database looks at more detailed tax data, i.e. revenue figures, for a smaller subset of 31 countries, spanning 1800 to 2012. Yet, it lacks too policy indicators fit for my analytical purposes.

The IMF's *Tax Policy Reform Database* (TPRD) (2018) is perhaps closest to what I seek. It contains detailed event information on new tax policy measures adopted in 23 advanced and emerging market economies over the last four decades, covering six tax types, including the income tax. In terms of data generation, the individual tax reform measures were found through a process of text-mining historic OECD Surveys and thousands of tax-related news stories in combination with manual verification and subsequent content coding.<sup>131</sup> The final dataset contains information on key variables such as (1) the exact announcement and implementation dates of tax measures; (2) type of change (to a rate or a tax base); (3) the direction of change (tax cut or hike); (4) whether the measures represented a major tax change (e.g. enacted via tax reforms); and (5) whether they were phased in over multiple years (measuring the longevity of timing). The TPRD's main advantage is that it allows us to gauge the precise nature of reform measures, also for parameters for which no

<sup>&</sup>lt;sup>129</sup> The distinction between politically defined tax rules as an *output* phenomenon and revenue as a policy *outcome* is warranted, given the long complex causal chains between them. It echoes the longstanding discussion about social rights versus spending outcomes in welfare state studies (see e.g. Siegel 2007, Jensen 2011). Accordingly, the rules governing rates and thresholds constitute two (albeit important) dimensions affecting revenue intake and may only have a more subtle, delayed and therefore obfuscated impact on revenue figures.

<sup>&</sup>lt;sup>130</sup> Their database is, however, ideally suited to uncovering the historic drivers of states' fiscal developments.

<sup>&</sup>lt;sup>131</sup> Amaglobeli, et al. 2018 contains the full details on how the dataset is constructed.

time-varying policy indicators currently exist (e.g. changes in thresholds, tax exemptions, etc.). With these data in hand, the IMF authors convincingly show us that policy changes to the tax bases/thresholds are the most frequent during the time span of their dataset, and that such measures are typically enacted in combination with changes to tax rates. Their findings reinforce a main contention of the dissertation: look beyond marginal tax rates.

However, the TPRD is plagued by both measurement and substance issues. The data quality of the policy information gathered varies greatly across countries and periods, as explained by the authors. In some countries, OECD Economic Surveys were collected on a biannual rather than an annual cycle, reducing coverage.<sup>132</sup> Further, the temporal coverage of the database is clearly affected by the decision to phase out the so-called OECD *Calendar* of *Chronology* of countries' main economic events, a stable annex of OECD Surveys until around 2003 to 2005. To provide a sense of this bias, **Figure 9** shows the number of policy change events counted by the TPRD for income taxation from 1970 to 2014. It points to a clear decline in the reform activity coinciding with the changing format of the reports. The number falls from 31 measures in 2000 to around 16 in 2010. There is, of course, the possibility that this decline merely reflects the true underlying tendency. Yet, the decline looks suspicious enough that I do not wish to base my empirical conclusions on what is perhaps caused by inadequate source materials.

There are, secondly, further problems related to its coding scheme. The definition of what constitutes a 'tax base' change in TPRD terminology is at times so broad that it almost turns into a residual category. A base change is identified when the policy measures affect 'a large group of taxpayers or has the potential to mobilize significant resources' (ibid.: 11). Hence, it includes both the introduction and removal of tax measures, as well as changes in the number of income tax brackets. The authors seem to miss the key point that the former group of changes inevitably concern decisions on thresholds and rates at the same time: one cannot introduce a new tax without specifying both the 'who' and the 'how much' components. Their coding choice risks inflating the relative scope of base changes in my view.

<sup>&</sup>lt;sup>132</sup> Whereas the biannual surveys may tend to focus on a few hallmark tax policy changes, countries with annual surveys may also cover less macro-critical tax measures. Variations in measures counted may thus be an artifact of the varying quality in source materials rather than reflect actual policy differences.

**Figure 9** Number of new tax policy measures (personal income tax) as counted by IMF



Source: Own calculations based on IMF (2018).

**Notes:** The figure features 963 policy changes in total. The countries included are restricted to those in TPRD which overlap with this dissertation: Australia, Austria, Canada, Denmark, France, Germany, Ireland, Italy, Japan, Luxembourg, Portugal, Spain, the United Kingdom, and the United States.

Third, the TPRD leaves no way of evaluating and comparing the sizes of policy changes. While the database does try to distinguish between 'major' and 'non-major' policy measures, this variable is rendered close to redundant, as most changes meet these relatively vague criteria. Of the 963 income tax measures listed in **Figure 9**, 87% are counted as major reforms. It means, for example, that rate reductions of 1 *or* 10 percentage points are the same on paper, although they are hardly perceived as such by any political actor. We need a more valid measurement of size than simply counting the number of measures *per se*, to assess properly the relationship between reforms of threshold limits and rates. In practice, a tax reform may include many small compensatory tax increases to fund one major tax cut, yet they are counted unevenly in the way the TPRD data is structured.

I was hence left unsatisfied with the menu of tax indicators available. Upon plenty of head scratching, I decided to take a swing at this proposition myself by constructing a set of novel dependent variables, more suited for answering these puzzles on 21<sup>st</sup>-century income tax politics. I began by turning to the source of the policy data. The OECD is the obvious starting point for this endeavor, as it collects annual details on the taxes paid on wage income in its member states for its *Taxing Wages* publications. Their data collections cover both personal income taxes, SSCs paid by employees, and contributions and payroll taxes paid by employers. These data enable quantitative cross-national comparisons of tax burdens for different types of wage earners, often calculated as the average and marginal effective tax rates on labor costs. However, their approach, crucial as it may be for other tax comparisons, ignores the structure of policy designs.

Fortunately, one can easily dive right into the nitty-gritty, if one desires. The OECD publishes its separate *Tax Database*, which gives access to these rich and comparable, but also raw, legislative tax data. It holds specific information on personal income tax rates *and* thresholds limits from 2000<sup>133</sup> to 2018<sup>134</sup>. It is worth mentioning that OECD's Tax Database only looks at central government taxation and does not factor in any sub-central income taxes such as state, regional, or local in its main tables. It is not a huge concern here, as I, consistent with the theory, study the policies authorized by the national government, not decisions made at lower levels of government. In addition, I am mainly interested in the year-to-year policy dynamics rather than differences in absolute tax burdens across countries, whereby it becomes less problematic to use the central government policies as the baseline.<sup>135</sup>

The Tax Database contains information on five policy instruments in total. For each country, there is a positive record of the indicators in question, if it is featured in the country's income tax code; otherwise the indicator is set to 'missing'. Let us mention each one. The database lists whether a country has a basic *personal allowance* (PA) available to all taxpayers and/or a general *tax credit* (TC). In 2018, six of the 21 countries<sup>136</sup> investigated had a standard allowance, while seven countries had a universal income tax credit, as defined

<sup>&</sup>lt;sup>133</sup> The database goes all the way back to 1981 for a smaller subset of countries, but the OECD have yet to verify these policy data. As the older data have repeated issues with missing or incorrect legislative data and a variable structure that is inconsistent compared to the later data, I rely on observations from 2000 onwards. It is consistent with the theoretical focus of the dissertation.

<sup>&</sup>lt;sup>134</sup> Policy data were available up until 2018 at the time of my data extraction (26 April 2019). Since then, country data for 2019 and 2020 have also been released.

<sup>&</sup>lt;sup>135</sup> The focus on central government taxation does become an issue if the authority of a specific income tax policy is transferred from one level of government to another. It then registers as a policy change 'on paper' but is likely not experienced as such by the taxpayer nor policymakers. Such transfer of a tax across governmental levels is, however, a rare phenomenon in the period of the analysis.

<sup>&</sup>lt;sup>136</sup> The full list countries includes: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Iceland, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

by the OECD. Third, it lists whether countries' tax codes feature a *surtax* (S) or *surcharge* that de facto acts as an additional tax rate on income. These may include payments that are identified by governments as separate taxes but levied on a similar tax base as the regular income tax.<sup>137</sup> If the surtax rate varies with income, OECD reports the maximum rate. Eight countries had a separate surtax on income in 2018, ranging from 2% (Australia) to 9.7% (France). Finally, the database lists the two policy components we have discussed at length, the *marginal rates* (R) and the bracket *thresholds* (T). In line with the mathematical definition of the tax schedule (**Chapter 2**), OECD list +1 the number of rate variable(s) for each tax bracket a country has.<sup>138</sup>

My prime interest is the within-country policy variation, i.e. the type of reform. While policymakers do not re-design the entire income tax system from scratch at the start of each fiscal year, OECD's policy data still leave the impression that the changes we see from year to year do accumulate noticeably over time. The UK case is fine illustration of this, as seen in **Figure 10**.<sup>139</sup> It presents the visual plot of the income tax schedule by the parameters recorded by the OECD, with the level of taxable income shown on the *x*-axis and the corresponding marginal rates on the *y*-axis. Not surprisingly, its schedule in 2000 and 2018 are pretty similar. Yet all key parameters have changed to some extent. The basic income tax rate rose from 10% to 20% during this period,<sup>140</sup> and the top marginal rate rose from 40% to 45%. **Figure 10** shows that the number of tax brackets was three in the start and the final year (count the number of schedule 'steps' as a rule of thumb). For a short period, though, there were only two brackets in the fiscal years 2008 and 2009, where UK citizens only had to pay the 'basic rate' and the 'higher rate'. The positions on

<sup>137</sup> A prime example is Germany's 'solidarity surcharge' (*Solidaritätszuschlag*) introduced in 1991 as a 12-month measure to help cover the costs of the German re-unification. As of 2018, it was still levied at a 5.5 percent rate for the highest incomes.

<sup>138</sup> The quality of the raw data is probably as good as it can get, since data are drawn from the *Taxing Wages* project, which builds on thorough examinations of the formal tax rules in the member states. The data are scrutinized by economists, fiscal analysts and political observers who are likely to point out any major mistakes for correction. In my experience, the data stand the test compared to what can be found in legislative documents and secondary sources at the case level. In two instances, I spotted evident mistakes in the data (Austria, 2000 to 2001, and Germany, 2000 to 2002) and manually corrected those values to what I found in the actual tax codes. <sup>139</sup> To illustrate what OECD's data structure looks like in practice, **Table 12** in **An**-

**nex A.II** provides a full overview of the policy data available for the United Kingdom.

<sup>&</sup>lt;sup>140</sup> The rise reflects mainly the abolishment of the former so-called 'starting rate' of 10 percent, which was scrapped by the Labour government in the 2007 budget.

the income scale for the three thresholds are markedly different. In 2000, the lowest rate was paid on a relatively tiny proportion of the taxable income (£1,520), but the equivalent threshold has been expanded significantly over the period (£34,500). Conversely, the top rate now kicks in at a much higher income level (£150,000) than it used to (£28,400). Another key change was that the personal allowance on earned income not subject to income taxation nearly tripled (!) from 2000 to 2018 (from £4,385 to £11,850), though it is not evident from **Figure 10** which only portrays the taxable income (after such allowances are subtracted).<sup>141</sup>





**Notes:** The grey line represents the 2000 income tax schedule, while the dashed, black line is the 2018 schedule. Values for 2000:  $R_1 = 10$  %,  $R_2 = 22$  %,  $R_3 = 40$  %,  $T_1 = \pounds 1.520$ ,  $T_2 = \pounds 28.400$ . Values for 2018:  $R_1 = 20$  %,  $R_2 = 40$  %,  $R_3 = 45$  %,  $T_1 = \pounds 34.500$ ,  $T_2 = \pounds 150.000$ . The UK average annual wages were  $\pounds 22.512$  in 2000 and  $\pounds 35.163$  in 2017 (last year of available data).

The many moving parts make it difficult to draw any sharp conclusions on the policy direction of these measures, as some (e.g. higher rates) have the direct effects of increasing income tax burdens *ceteris paribus*, while others (e.g. higher thresholds limits) decrease them. It is also clear that the individual policy changes do not affect all taxpayers equally; the change in the top marginal rate is the obvious parameter to emphasize in this regard, as it per design targets the highest incomes. The income distribution among taxpayers is not constant over time either, which too needs to be factored into the comparison of

<sup>&</sup>lt;sup>141</sup> How this sizable change in personal allowance came about politically is one of the main stories of **Chapter 7**, which examines the reform process during the recent Conservative reign in the United Kingdom.

tax schedules from year to year. The UK average earnings rose from £22,512 in 2000 to £35,163 in 2017 in current prices (OECD 2019a). From this perspective, it makes sense that bracket thresholds have risen as well, but they have certainly increased at a different pace than earnings.

### 5.2 Separating the effects of rates and thresholds

One way to isolate the impact of multiple year-to-year changes in policy is to consider them separately. This is my approach to decomposing the effects of legislative changes in rates and thresholds. For example, if rates have been lowered from one year to the next in a given country – and all other parameters are kept at fixed values – it translates into a reduction in the overall tax liability. I denote this a *negative rate effect*, i.e. a tax cut via the marginal rate(s).

My approach to measurement construction has two steps. First, I calculate the tax liability (TL) imposed by the current income tax rules in each country year using the same **Formula (2)** introduced in **Chapter 2**:

 $TL = R_1 * TI + (R_2 - R_1) * (TI - T_1) * I(TI > T_1) + ... + (R_k - R_{k-1}) * (TI - T_j) * I(TI > T_j)$  (5)

where R and T are the marginal rates and thresholds. To reiterate, k specifies the number of marginal rates in the income tax schedule in a given country year, while j is the number of thresholds. TI is the taxable income defined as the income stemming from wages and salaries subtracted the standard personal allowance. The symbol I is indicator functions, which designate whether the taxable income is above the upper limit value of a particular threshold. In more intuitive terms, I derive the tax liability by first calculating the amount of taxes stemming from the basic rate (R<sub>1</sub>), which applies to all of the taxable income.<sup>142</sup> Then, I multiply the marginal, additional tax rate ( $R_k - R_{k-1}$ ) for each bracket on the income tax schedule for that specific subset of the income (TI – T<sub>j</sub>), as long the taxable income still exceeds the tax liability for that particular taxpayer (and the indicator function takes value o).

The taxable income can be set, of course, at any value to apply the formula for a taxpayer of theoretical interest, for example, an average or a low- or highincome earner. In my analysis, I rely on three types of references to capture the variety of tax conditions across the income scale: (1) a taxpayer earning average wages (AW) in a given country year, (2) one earning 50 percent of average wages, and (3) one earning three times average wages. All three are

 $<sup>^{142}</sup>$  To make things relatively simple, I add the standard surtax rate to the basic rate (R<sub>1</sub>) in countries where it exists.

necessary to include to test whether policymakers target specific classes of taxpayers with their reforms. The choice of 50 percent is to capture individuals squarely situated in the lowest quantile of incomes,<sup>143</sup> while the 300 percent comparison is set at a high enough number to capture policy measures aimed at the richest taxpayers.<sup>144</sup> Country data on average earnings are drawn from OECD's *Taxing Wages* comparative tables, which list total gross earnings before taxes in national currencies. As the OECD only lists the standard allowance for every taxpayer, I use this by default and do not incorporate changes to any group-specific allowances or deductions in my two measures. These instruments are, of course, at the hands of policymakers in practice, and omitting them may induce some bias in my overall conclusions on the scope of policy change, if the way such group-specific exemptions are used differs from how rates and thresholds generally develop. Yet, there are no valid cross-national policy data are available on these exemptions to my knowledge.

The second step is to calculate the decomposed rate and threshold effects. I do this by fixing all other tax parameters at last year's country values (t-1) and then calculate the simulated change in tax liability when setting rates and thresholds to the current year's values, respectively. For the rate effects, the formula is as follows:

Rate effect =  $TL_R - TL_{t-1}$  (6)

where  $TL_R$  refers to **Formula (5)** with all parameters lagged one year (TI and T) except the rates (R). By subtracting this calculated tax liability from last year's liability ( $TL_{t-1}$ ), I obtain the 'clean' net effect of what can be attributed only to legislative changes in rates. It implies that the rate effect is zero, if rates are constant from one year to the next.<sup>145</sup> The unit of the effect needs some

<sup>&</sup>lt;sup>143</sup> The OECD use different references to evaluate the impact of tax policies, typically the 67, 100, 133, and 167 percentage of the average wage. One could easily justify relying on this split. Yet to me, it was pressing to make the reference points to the left and right on the average extreme enough to capture the differences in policy intervention across the whole scale, or at least most of it. Further, I wanted to go higher than 167 percent of income due to the shape of the income distribution, typically skewed to the right with a long tail.

<sup>&</sup>lt;sup>144</sup> One could argue that the even richer taxpayers have been the prime beneficiaries of many contemporary tax reforms, at least in the United States (see Bartels 2005, Hacker and Pierson 2005) and therefore the ones to study. However, 300 percent still represent taxpayers many standard deviations above average wages.

<sup>&</sup>lt;sup>145</sup> The formula for calculating the threshold effect follows the exact same logic: Threshold effect =  $TL_T - TL_{t-1}$ , where  $TL_T$  lags TI and R but keeps T at the current year's values. A *negative threshold effect* means that thresholds were raised in comparison to last year's income tax schedule, reducing the tax liability.

work too, as the changes in TL are expressed in national currencies, which complicates any comparisons across space and time. To skirt the issue, I standardize the calculated rate and threshold effect by dividing it with the wage income of the reference taxpayer, whether at 50, 100, or 300 percent of average wages, to express my dependent variables in percentage changes. A positive rate effect of 0.5 thus implies that higher tax rates caused a rise in net tax liability that corresponds to 0.5% of the taxpayer's gross earnings.

## 5.3 An illustration of the rate and threshold effect

I realize that it is perhaps difficult to form a visual interpretation of the effects at this point, and a concrete example is warranted. Let us start simple. **Figure 11** depicts the rate and threshold effect starting with a simple, fictitious income tax schedule that features two rates and one threshold limit separating the two brackets: the bottom rate ( $R_1$ ) at 10%, the top rate ( $R_2$ ) at 30%, and the threshold ( $T_1$ ) at 50 for an unspecified currency. The taxable income (TI) for the taxpayer is 100 in this example. The area bounded below the tax schedule in **Figure 11** (the grey reference line) thus represents the total tax liability, which is 20 in this example.<sup>146</sup>

We now consider two different policy scenarios that involve tax cuts: (1) one where  $T_1$  is raised to 75 instead of 50 (the upper panel), and (2) one where  $R_2$  is lowered to 20% (the middle panel). The black dashed lines represent the corresponding shifts in the tax schedule. The threshold change in the upper panel corresponds to the horizontal, rightwards shift in the schedule, and the shaded blue area gives the monetary value of the tax cut (i.e. the threshold effect). Similarly, the top rate cut from 30 to 20% in the middle panel shifts the second horizontal line downwards, and the area highlighted with red gives the reduction in tax liability (the rate effect). The parameter values are not set randomly in this example, as it is evident that the tax cuts are of equal size in both scenarios (a reduction in TL from 20 to 15, with a net effect of -5). If we disregard other political and economic logics for now, they are different means of achieving the same target amount.

<sup>&</sup>lt;sup>146</sup> Using **Equation (5)**, the calculation is as follows: TL = 0.1 \* 100 + (0.3 - 0.1) \* (100 - 50) = 20



Figure 11 Stylized example of the rates and threshold effects

**Notes:** The grey line represents baseline example. Values for Year 0 are:  $M_1 = 10 \%$ ,  $M_2 = 30 \%$ ,  $T_1 = 50$ . The figure depicts three policy scenarios. In the upper panel,  $T_1$  is raised to 75 (blue shaded area is the base effect). In the middle panel,  $M_2$  is lowered to 20 % (red shaded area is the rate effect). In the lower panel, both policies are implemented at once.

What happens if both policies are implemented at once? The lower panel in **Figure 11** considers this scenario. It shows that simply summing the separate threshold and rate effects from the two upper figures will overstate the true reduction in tax liability, which is -7.5 in this example, lower than its sums (-10). It is because one area – the shaded greyish square – is counted twice when both parameters change. To avoid this pitfall, we need to take the changing tax bases into account. Raising T<sub>1</sub> thus expands the tax base for which the basic rate of 10% applies, while it reduces the base liable to the higher rate.

We therefore need to add a correction to the generic formula when R and T are adjusted within the same fiscal year, what is, of course, a highly relevant scenario in the real world. I correct the effects by (a) subtracting the 'gained' base multiplied by any change in the basic rate (which is zero in this example) from the calculated threshold effect, and by (b) adding the 'lost' base times the reduction in the top rate to the rate effect.<sup>147</sup> Intuitively, the shaded area can be understood as a tax cut never realized by the taxpayer, and we need to factor in that they do not receive the benefit of the lower top rate any longer (20% compared to 30%) on taxable income that falls between 50 and 75. The corrected rate effect amounts to -2.5, and if we subtract this from the initial net effect, we get the true rate effect of -2.5. The sums of the effects now correspond to the actual cut in tax liability. **Annex A.III.I** goes into much more details on how to calculate the corrected effects and formalizes it for more complex policy scenarios (e.g. for j > 1).

I next apply the approach to actual policy data, once again using the UK income tax rules as my example. I zoom in on the fiscal years 2007 and 2008 since they are illustrative of some of the main computational issues. The 2007 budget was the last of Chancellor of the Exchequer Gordon Brown, before he advanced to the premiership, and it contained multiple adjustments of the income tax code. For example, it abolished the starting rate of 10% ( $R_1$ ), which was formerly applied on the first £2,230 of taxable income, and cut the basic rate ( $R_2$ ) from 22% to 20% beginning from the fiscal year 2008 (HM-Treasury 2007). This altered the UK policy from a three-tier to a two-tier tax system. The threshold limits for the higher rate also rose from £34,600 to £34,800 due to standard indexation practices (ibid.). The average earnings of UK citizens was £29,413 in 2007.

Say we now wish to calculate the rate and threshold effects stemming from these policy changes for a taxpayer with average earnings. For them, only the starting rate and the basic rate would apply, since the threshold for the higher rate lies well above their earnings, especially since the standard UK personal

<sup>&</sup>lt;sup>147</sup> The correction of the threshold is:  $-\Delta T_1 * \Delta R_1 = -25 * 0.0 = 0$ . The correction of the rate effect is:  $\Delta T_1 * \Delta R_2 = 25 * -0.1 = -2.5$ .

allowance was £5,225 in 2007. Hence, their immediate taxable income was £24,188. If we assume a constant income over the two years, their tax liability would be £5,054 in  $2007^{148}$  compared to £4,838 in 2008,<sup>149</sup> a tax cut of -£216.

To calculate the separate effects, we treat the 2008 schedule (the 'after reform' policy) as a de facto two-rate system, even though it is not for the average taxpayer, where both  $R_1$  and  $R_2$  take the flat-rate percentage (20%). It ensures that we avoid a 'missing data problem', since the year 2007 features two marginal rates of relevance, while the year 2008 only has one. Similarly, we need to replace the missing value for  $T_1$  in 2008 with the value equivalent to the taxpayer's taxable income. We can do this because removing the particular threshold limit simply parallels expanding the size of the tax base to extend the entire income of relevance. The technical Annex A.III.II goes into more detail on the justification for and the consequences of this data replacement strategy. Premised on these assumptions, the direct net rate effect is a -£216 change,<sup>150</sup> while the threshold effect is a -£2,635 change.<sup>151</sup> However, the sum of the direct effects is, obviously, too large before they are corrected to the actual new tax bases. The true rate effect is thus a £223 tax hike, while the true threshold effect is a -£439 tax cut.<sup>152</sup> These sum to the correct joint amount (-£216).

In terms of policy substance, the measures suggest opposing reform effects. On the one hand, the taxpayer receives a higher tax bill because they now pay a 20% rate on the first £2,230 earned instead of the former 10% rate. On the other hand comes a tax cut in the form of the de facto expansion of this new 20% rate bracket from its previous threshold limit at £2,230 to its new position, which is way beyond the level of their current taxable income. In effect, they now have to pay the 20% rate on income earned between £2,231 to

<sup>&</sup>lt;sup>148</sup> The calculation is as follows: TL(2007, UK, 100p) = 0.10 \* £24,188 + (0.22-0.10) \* (£24,188-£2,230) = £5,054.

<sup>&</sup>lt;sup>149</sup> The calculation is as follows: TL(2008, UK, 100p) =  $0.20 \times \pounds 24,188 = \pounds 4,838$ . <sup>150</sup> The calculation of the rate effect is as follows: TL(R) =  $0.20 \times \pounds 24,188 + (0.20 - 0.20) \times (\pounds 24,188 - \pounds 2,230) = \pounds 4,838$ . Then the Rate effect becomes:  $\pounds 4,838 - \pounds 5,054 = -\pounds 216$ .

<sup>&</sup>lt;sup>151</sup> The calculation of the threshold effect is as follows:  $TL(T) = 0.10 * \pounds 24,188 + (0.22 - 0.10) * (\pounds 24,188 - \pounds 24,188) = \pounds 2,419$ . Then the Threshold effect becomes:  $\pounds 2,419 - \pounds 5,054 = -\pounds 2,635$ .

<sup>&</sup>lt;sup>152</sup> The correction of the threshold effect is:  $-\Delta T_1 * \Delta M_1 = -\pounds 21,958 * 0.1 = -\pounds 2,196$ . The true, corrected threshold effect is therefore:  $-\pounds 2,635 - (-\pounds 2,196) = -\pounds 439$ . The correction of the rate effect is:  $\Delta T_1 * \Delta R_2 = \pounds 21,958 * -0.02 = \pounds 439$ . The true, corrected rate effect is therefore;  $-\pounds 216 - (-\pounds 439) = \pounds 223$ .

£24,188 rather than the former 22%, resulting in a tax reduction. To standardize the effects, I divide them with the earnings of the reference taxpayer in the baseline year (£29,413). The results yield a rate effect of 0.76% and a threshold effect of -1.49%. The joint policy effect from 2007 to 2008 is therefore -0.73%. I compiled the calculated effects for all observations in the UK time series for illustrative purposes in **Annex A.IV.** 

# 5.4 Descriptive evidence and two approaches to study macro policy trends

Overall, the two measures tick a lot of boxes in terms of the theoretical requirements we have set. They are based on objective policy data that hold high quality standards across the OECD countries; they deconstruct the two instrument types into separate entities, meaning we can analyze their similarities and differences; and they take into account the relative size of reform, not just whether policy in a given country year was changed or not. I calculate next these effects for all countries featured in my analysis and for the three reference taxpayers over the period 2001 to 2018.<sup>153</sup>,<sup>154</sup> The process from the raw policy data to having tangible and meaningful dependent variables ready for analysis was time-consuming and required both careful methodological considerations, as spelled out over the previous pages, of how to transform the data as well as sharp attention to each step of the computation process.

Let us not wait no further and inspect what the descriptive evidence on my dependent variables can tells us. **Figure 12** shows histograms of the year-toyear changes in tax liabilities as a function of the legislative changes in rates (dark grey) and threshold (hollow), in total 378 county year observations (21 countries over 18 years). Here, I have chosen to show the results for the taxpayer earning 300 percent of average wages, though the main tendencies would be virtually similar had I chosen one of the two other references. The figures thus tell a number of informative stories that can be unpacked. What probably strikes the reader first are the distribution shapes for the two

<sup>&</sup>lt;sup>153</sup> I chose 2001 as my base year (instead of 2000), as it neatly evades the issue with transition to the Euro for a larger subset of the OECD countries. The currency switch naturally affected the legislative rules on threshold limits in direct ways, and it coerced legislators to re-calculate new threshold values for the income tax schedule, a conversion process not handled uniformly across countries. The decision limits the generalizability of the results, accordingly.

<sup>&</sup>lt;sup>154</sup> Germany is excluded, as its progressive formula for calculating the income tax differs sharply from the computation based on **Formula (5)** (OECD 2011b: 30-31). Hence, the country is missing in all of the macro analyses.

measures, as they are certainly not normal but rather leptokurtic.<sup>155</sup> This should not surprise trained students working with data on policy reforms and budgetary processes (see Baumgartner, et al. 2009, Chaqués-Bonafont, et al. 2020). The high peaks for both refer to the many country year observations with no or little policy change, while the weak 'shoulders' refer to the relatively few cases of moderate change. Finally, we see evidence of 'fat tails', the extreme policy changes many standard deviations away from the center of the distribution. In other words, changes to tax rates and thresholds are minor at the tall center of the distributions, and there are a lot of them – the long periods of policy stability – or the changes are rare but sizable in the tails – the episodic burst of reform (or 'punctuations' to use the agenda-setting term).

**Figure 12** Histograms of the yearly change in tax liabilities stemming from rates and thresholds



Source: Own calculations based on OECD (2019b).

**Notes:** N = 378. The reference taxpayer is the taxpayer earning 300 percent of average wages. The bandwidth is the histogram bars is 0.25 percentage points. Rate effects (dark grey): Mean = -0.05, St.d. = 1.23. Thresholds (hollow): Mean = -0.23, St.d. = 1.02.

<sup>&</sup>lt;sup>155</sup> Normal distributions have a kurtosis score of 3.0, and leptokurtic distributions have scores greater than that. The kurtosis score for rates changes is 19.9, and the score for threshold changes is 50.5.

There are, as **Figure 12** reveals, subtle differences between them. For the rates distribution, 61% of the country observations are zeros (230 of 378).<sup>156</sup> The best predictor of the countries' income tax rates in this period are, hence, last year's rates, which meshes with the argument made in the theory on the reform nature of rates: they require political intervention to change. Further, the rates distribution has plenty of instances of both negative tax-cutting reform years (89 observations, or 24%) and positive tax-hiking ones (59 observations, or 16%), though they do not balance perfectly.

The threshold distribution has slightly different features. For one, it has a lot less zeros, i.e. reform years with no policy change (122 or 378, or 32%). Status quo is not the norm. Instead, the most usual mode of politics, reflecting the tallest of the hollow bars, is to raise threshold limits (slightly) from last year's values, cutting income taxes, all things equal. It is, of course, indicative of the aforementioned mode of indexing tax brackets to whichever growth parameter set by policymakers to make sure that threshold limits, fully or partially, keep up with rising income levels. Because many of the countries studied have such practice in place, it is not surprising that more than half of the country observations have negative policy scores (232 observations, or 61%).<sup>157</sup> Figure 12 shows relatively few records of positive changes (24 observations, or 6%), which demonstrates that lowering threshold limits, thereby increasing tax liabilities, is a seldom-used political practice in the OECD. The obvious explanation revolves around politics; if policymakers actually wish to raise income taxes via thresholds, it attracts a lot less political attention doing so by inducing bracket creep by default (i.e. by doing nothing) than actively seeking to lower the same thresholds, even though the effects on liabilities, and hence revenue, may not be as immediate. So looking from the helicopter, the shapes of distributions and the differences between them seem to have a lot of face validity based on what we already know about the two instruments.

Of course, the global distributions do not paint an accurate picture of the more diverse policy stories at the country level. **Figure 13** shows the count of

<sup>&</sup>lt;sup>156</sup> Zeros, here, do not necessarily imply that nothing happened in terms of tax reform, as two equally sized policy changes in opposite directions in theory could cancel each other out. For example, if marginal rates were lowered for the basic rate of income taxation, while rates on higher tax brackets were raised accordingly. However, qualitative inspection of the data reveals that it is hardly the case in practice, at least not to the point where the changes cancel each other perfectly for the specific taxpayer. But one could certainly imagine policymakers using hikes at one end of the tax schedule to finance cuts at the other end, so the moves were revenue-neutral when calculated across the entire population of taxpayers.

<sup>&</sup>lt;sup>157</sup> The figure reveals that not all negative scores are merely minor policy adjustment; there are also major reform instances in the figure's left tail.

policy changes (again for the 300 percent AW taxpayer), both positive and negative ones, for all countries broken down for rates and thresholds, respectively. The figure shows whether policymakers in certain countries are more prone to use either instrument as a vehicle for policy change. As the figure spans 18 years of analysis, one can easily deduce that if Country A records the same number of instrument changes, for example as we see with threshold changes in Canada, the policy parameter in question was changed in every fiscal year.

Figure 13 reveals stark differences in how often rates and threshold limits are reformed across countries. Compare, for example, the contrasting experiences of the Netherlands and Switzerland. The created measures record Dutch policy changes on both instruments in all years of investigation (most are not major but mere fine-tuning of the existing parameters), while the federal income tax rules stay relatively constant in Switzerland, as marginal rates were not reformed once in the period of analysis, and thresholds only modified in four of the 18 observation years.<sup>158</sup> In other countries, instrument choices seem more selective, in the sense that politics is confined to altering one of the two types, typically threshold limits. Sweden and the United Kingdom, the clearest examples, have recorded nominal changes to thresholds in (almost) all country years, while the rates measure picks up only one policy change in the British case<sup>159</sup> and none in the Swedish. By extension, the global trend in the figure is that countries feature more frequent threshold than rate changes,<sup>160</sup> though the frequency varies considerably. We can easily explain why. Countries with income tax indexation schemes (OECD 2007: 53) also stand out regarding the count of yearly changes, e.g. countries like Belgium, Finland, and the United States.

<sup>&</sup>lt;sup>158</sup> Bear in mind, these counts do not (necessarily) reveal anything about the size or direction of the individual tax changes, only about their divergence from the status quo.

<sup>&</sup>lt;sup>159</sup> As evident from the raw data found in **Table 12** in **Annex A.II**, the UK marginal rates were actually reformed in three case years (2008, 2010, 2013). However, the policy changes in the latter two targeted only taxpayers with incomes higher than 300 percent of average wages, which is why it is not picked up by the rates measure. <sup>160</sup> Reversed in the cases of Austria, Italy, Japan, and New Zealand.



### Figure 13 Counts of policy changes in tax rates and thresholds across the OECD

#### Source: Own calculations based on OECD (2019b).

**Notes:** The reference taxpayer is the taxpayer earning 300 percent of average wages. The figure number refers to years where tax rates and/or threshold limits differed from values at  $t_{-1}$  – in other words diverged from policy status quo. The period covers 18 years in total (2001 to 2018).

In Austria and New Zealand, which do not have a similar automatic scheme, threshold limits are altered much more infrequently. If we split countries according to OECD's categorization on this topic, countries with a scheme to prevent fiscal drag<sup>161</sup> record 15.4 threshold changes on average, as per **Figure** 

<sup>&</sup>lt;sup>161</sup> I pool countries with adjustment schemes based on inflation and countries with schemes based on real earnings growth. The list includes Belgium, Canada, Denmark, Finland, Iceland, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

**13**, while those without<sup>162</sup> score only 5.7. We like, again, the face validity of these data as to how their behavior matches the preexisting sources of policy information.

After these initial descriptives, the next issue is to find out how we can study the dependent variables (DV) optimally to draw meaningful inferences from them. This discussion is guided by the question of the proper unit of analysis. It should be clear, from the theory sections, that my framework stresses the importance of both actors and institutions. Right elites are expected to those policy strategies that best serve them according to the logic of the institutional context. Therefore, we need to cut the DVs in ways that allow us, first, to examine how such institutions confine the direction tax policy can generally take. Is there, for example, evidence that they take away certain policy spaces? Yet at the same time, we also need output measures that are a lot closer to the specific reform results that derive from the political process, and which allow us to attribute proper responsibility to those political actors that deserve it. Because the two analytical goals are tough to maximize at once, we need more than one way of studying these variables.

One method to unlocking this discussion is to take one more look at what qualities define the reform data and then cut the measures accordingly for analysis. If we dwell on the histograms in Figure 12, it becomes evident quickly that they have tricky properties, statistically as well as conceptually. First, the measures as constructed do not represent proper linear scales. What I mean by this is that negative and positive output values cannot be treated as meaningful metric scores of the same underlying distribution. As laid out in the previous chapter, we must expect that policy measures to cut and raise taxes are governed by entirely distinct political logics, and therefore we cannot say that instances of cuts and hikes of equal numerical sizes simply cancel each other out; that they are the same phenomenon with reverse sign. In fact, we have every reasons to believe that the two kinds of reforms bode vastly different politico-economic drivers, and for these reasons, we cannot expect the potential effects of explanatory variables to be continuous across all types of outputs. On top of this schism between the positive and negative cases comes, of course, the real issue how to treat the 'in-between' observations, i.e. the political non-events. The zeros, here, do not constitute absolute zero points of standard ratio scales, as holding on to the policy status quo shows be regarded a third meaningfully distinct form of output. Finally, and adding to the challenge, we must consider the potential impact of policy outliers, those located in the tails on the distribution on our analytical conclusions. It is especially warranted if we seek to leverage insights at the level of the individual reform

<sup>&</sup>lt;sup>162</sup> Australia, Austria, Ireland, Italy, Luxembourg, and New Zealand.

cases, where few critical observations have the potential to distort the (average) effects of the many 'normally behaved' ones.

As I see it, there are two obvious ways to treat the dependent variables that enable us to take both analytical perspectives seriously and that dodge these measurement concerns. The first is to take a broader look at whatever policy trend not just by looking at the individual country years, but rather by gauging how policies *aggregate* over time.<sup>163</sup> What if we did not study, for example, individual tax cuts or hikes in one reform year, but look at what transpires within countries over, say, 20 years? The country, instead of the country year, then becomes the unit of analysis. The idea is that it cuts through the 'noise' and paints a clearer picture of the long-term trend. Studying the aggregates seems a more suited way to test institutional propositions – of the number of tax brackets and progressivity – that are expected to 'steer' the direction of policy slowly but steadily.

The second approach is to keep the country year as the unit of analysis but discard the notion of treating the DVs as meaningful metric indices. The alternative is to treat them as *events* of reform. Are rates, for example, cut in a given country year? Are threshold limits raised? In effect, it transforms the dependent variables into binary response measures and data series of zeros and ones. The obvious advantage is that it enables us to study the characteristics of the events; what defines them, not least with respect to their partisan traits. Is it actually true that cabinets populated by Right parties are more prone to cutting income taxes and do so in certain ways? The immediate drawback of relying on the dummy variables, which are more sound conceptually, over the metric alternatives is that the former eliminate valuable information on the scope of policy changes, pooling all cuts into one. To accommodate this concern, I narrow the categories of the types of events I examine by imposing a threshold for the size of reform. It implies that I do not necessarily wish to study all nominal tax cuts, for example, but only substantial reforms.

I wish to do justice to the insights of both perspectives and therefore treat each in subsequent analyses. I finish this chapter by diving into the aggregated

<sup>&</sup>lt;sup>163</sup> I do not think it is a stretch to say that the classic public policy literature has been more preoccupied with explaining individual instances of policy change, e.g. why did actors X change their Y policy at time Z, where the major unit of analysis becomes the individual policy in a country or set of countries. What one risks missing, when focusing on individual instances of policy changes, are the aggregated effects of the individual changes, which are arguably as important. Of course, there are plenty of good examples of public policy theories focusing on the long term, for instance Christian Adam and collaborators' (2019) recent work on the concept of *policy accumulation*.

policy results and their institutional prints, and then work my way to statistical tests in **Chapter 6** of whether Right partisanship predicts certain reform outputs and under what conditions.

# 5.5 Countries that lower rates lower income taxes the most

To generate scores on the aggregated policy effects, I simply take the calculated rates and threshold values and sum them for each country over the 18year period. Based on the UK effects, **Table 16** in **Annex A.IV** shows the aggregated scores for the three reference taxpayers. For the higher income earner (the 300 percent AW taxpayer), the scores are 0.21 and -2.24 for the rates and thresholds measures, respectively, indicating that UK policies combined to raise tax rates on this particular taxpayer corresponding to 0.21% of their wage earnings, but cut tax liabilities by raising threshold limits to the tune of -2.24%. The joint (total) effect of two aggregates sum to a cut in tax liabilities of -2.03%.

The easiest way to provide an overview of each country's scores is simply to plot them, as it is done in **Figure 14**. It displays the aggregated rates effects (on the *y*-axis) and thresholds effects (on the *x*-axis). It is not clear from the theory what we should expect of the exact nature of their relationship; whether cuts or hikes should generally come in coordinated effects over time (i.e. a strong positive correlation); whether cuts to one set of instruments is prioritized at the cost of lowering taxes on the other (an inverse relationship); or if tax hikes on rates, for example, are used to directly finance tax cuts to the threshold limits, and vice versa (a negative correlation). In any event, **Figure 14** does not settle this debate definitively. The linear fit is somewhat negative, perhaps indicative of a long-term policy trade-off between them, but the correlation is still insignificant (corr = -0.29; p-value = 0.19).<sup>164</sup> Even if we allow non-linear trends, it is still tough to identify a firm pattern.

<sup>&</sup>lt;sup>164</sup> As evident from the figure, the observation of Iceland has high leverage and 'pulls' the negative relationship. If it is excluded, the correlation is close to halved (corr = -0.17; p-value = 0.46). The reverse applies to the French observation at the negative end of the threshold spectrum. If excluded, the correlation soars and becomes statistically significant (corr = -0.39; p-value < 0.10).

# **Figure 14** Aggregated scores on rates and thresholds changes in tax liabilities from 2001 to 2018



**Source:** Own calculations based on OECD (2019b). **Notes:** N = 21. The reference taxpayer is the taxpayer earning 300 percent of average wages. The thick dotted line represents the best linear fit between the measures. Aggregated rate effects: Mean = -0.81, St.d. = 5.10. Aggregated thresholds effects: Mean = -4.06, St.d. = 3.64.

What can be concluded with more certainty is that the investigated countries generally fall into two of the four quadrants (demarcated by the zero lines on both axes). They align to the left of the vertical reference line, revealing more substantially that all countries (expect Iceland) cut taxes by raising thresholds limits during this period. Of course, the figures display great variation in this regard, ranging from Italy (-0.34) and Switzerland (-0.62) with the smallest cuts<sup>165</sup> to France (-13.05) at the opposite end of the spectrum. Further, ten of the twenty countries with negative accumulated thresholds scores combined it with negative scores on the rates measure as well, while eight had positive scores on the *y*-axis, reflecting that tax rates were raised for the high earners during this time span.<sup>166</sup> The UK falls (barely) into this category. Finally, Sweden and Switzerland had aggregated rates scores of zero.<sup>167</sup>

<sup>&</sup>lt;sup>165</sup> Bear in mind, these are only the accumulated negative effects in the absence of any change/growth in the wage level of the reference taxpayer. The latter needs to be factored in to draw any conclusions on whether taxes were effectively cut.

 $<sup>^{166}</sup>$  The fact that we observe a large number of countries both above and below the rates zero line is reflected in the mean score across countries of -0.81 (st.d. = 5.10), fairly close to zero.

<sup>&</sup>lt;sup>167</sup> It is hardly surprising, since we already knew from the cross-national counts of policy changes in **Figure 13** that both countries had zero rates changes from 2000 to 2018, reflecting policy standstill.

The next thing we would look for is whether the scatterplot reveals any tentative clustering of countries when it comes to our two institutional pillars or familiar geographic classifications such the Nordic/Scandinavian and/or the English-speaking group. Again, it seems difficult to draw sharp conclusions. One thing we may notice at this point is the positions of countries with a relatively low number of tax brackets (see discussion on tax institutions in **Chapter 4**). The three Scandinavian countries, Ireland, and the United Kingdom, all countries with three or fewer income tax brackets (on average), did *not* cut taxes via the rate-based route over the long term, placing them either at or above the horizontal reference line. It is perhaps indicative of a general trend, and I examine this relationship between tax brackets and accumulated rates changes more explicitly in the next section.

We can also look at the two separate aggregated policy effects in concert to study which countries generally have reformed income taxes most, or least, over the long term, when we sum the rates and thresholds effects. This allows us to gauge whether such joint effects are driven by the changes in either of the two constitutive measures; i.e. if a country's propensity to reform is explained by how much it has reformed its tax rates or its threshold limits. To test this, I first compute a joint aggregated measure (mean = -4.88, st.d. = 5.32), and again, France has the lowest score (-14.88) and Denmark the highest (3.75). I then plot the joint measure against either of the constitutive measure, as done in **Figure 15**, with the *upper* panel showing the joint score (on the x-axis) plotted against the aggregated thresholds scores (y-axis), and the *lower* panel the former against the rates scores (y-axis). We would, of course, expect relatively strong correlations between them, since the constitutive measures each comprise half of the joint one, so we are mainly turning our attention to the difference in correlation strength between the upper and the lower panel. It is rather pronounced in this case.

Starting from the thresholds plot (upper panel), the countries are, first of all, well spread across the *x*-axis according to their total scores; there is meaningful variation in how much they reformed during this period. Yet, the covariation with the aggregated thresholds effects (on the *y*-axis) is not *that* strong. The linear fit does predict a positive relationship, so that larger cuts in threshold limits are associated with larger cuts in total income tax liabilities for our reference taxpayer.<sup>168</sup>

<sup>&</sup>lt;sup>168</sup> The bivariate linear regression predicts a -6.79 percentage cut in threshold effects for the minimum case (based on the joint score) and a -1.69 percentage change for the maximum. If the minimum case with high leverage, France, is excluded from the calculation, the positive correlation drops to 0.21 (p-value = 0.37).



Figure 15 Aggregated joint effect plotted against rates and thresholds scores

Source: Own calculations based on OECD (2019b).

**Notes:** N = 21. The reference taxpayer is the taxpayer earning 300 percent of average wages. The thick dotted line represents the best linear fit between the measures. Correlation between joint effects and thresholds effect is 0.40 (p-value < 0.10). Correlation between joint and rates effects is 0.76 (p-value < 0.001).

It yields a bivariate correlation of 0.40 (p-value < 0.10).<sup>169</sup> It is relatively easy to explain why; most country scores align fairly close to the mean of the thresholds distribution, leaving the observations on the *y*-axis rather 'squeezed'. Nine of the 21 countries score within 2 percentage points of the cross-country mean (-4.06), and If we expand the inclusion criteria to 3 per-

 $<sup>^{169}</sup>$  If the minimum case with high leverage, France, is excluded from the calculation, the positive correlation drops to 0.21 (p-value = 0.37).

centage points, eight more countries join the category. In other words, if country scores on the thresholds dimension are similar, it is difficult to explain the large variation observed in the joint effects (*x*-axis).

In the lower panel, we observe a much stronger relationship between the joint scores and the aggregated rates measure, with the vast majority of countries aligning very close to the linear trend line. The correlation of 0.76 (p-value < 0.001) supports this notion,<sup>170</sup> as it is almost twice the size of the correlation with the aggregated thresholds. The figure seems to settle this issue unequivocally; if we wish to know which countries have generally lowered income taxes the most, we must first look at how successfully they have cut their tax rates. This is where the bulk of the variation lies.

# 5.6 Few tax brackets inhibit long-term rate-based cuts

The next question is what the main cause of this rates variation is. What factor locks a country's policy into this long-term trajectory? It is obvious to study this issue in relation to the aforementioned institutional traits, as my theoretical framework provides the theoretical answers to what constrains the use of the rate as a main vehicle of policy change. To reiterate, I regard the number of brackets that are featured in countries' tax schedule as key. The condensed argument is: with relatively few tax brackets to work with, politicians' reform efforts should switch from the rate(s) to less visible tax instruments, among them the threshold limits. In contrast, policy options should augment considerably once the number of brackets reaches a certain level, as it now becomes more politically feasible to cut tax rates along with other instruments. If we carry these proportions to the aggregate level, we should expect the countries with the relatively higher number of tax brackets to be most successful in cutting tax rates over time.

The most straightforward way to test this hypothesis is to plot the aggregate rates measures against the number of income tax brackets across all countries.<sup>171</sup> **Figure 16** displays this bivariate relationship, with aggregated rates on the *y*-axis and brackets on the *x*-axis. Its clear-cut results are among the most important of the dissertation. The clustering is evident, as we can draw two 'help squares' on top of the figure to ease the interpretation. The first can be drawn around five of the six left-most countries on the bracket dimension, i.e. those with relatively fewest tax brackets on average, consisting of the

<sup>&</sup>lt;sup>170</sup> Excluding France, the positive correlation increases to 0.82 (p-value < 0.001).</li>
<sup>171</sup> I rely again on the average number of income tax brackets between 2000 and 2010, as I did in Figure 8.

very group of countries we referenced in the former section: the Scandinavian countries, Ireland, and the United Kingdom. They are situated in the corner on their own. What is striking here is the absence of cases that feature large, or even moderate, aggregated cuts to tax rates. In fact, all five involve either no policy change when it comes to rates (Sweden), tiny hikes (United Kingdom) or sizable tax increases (Ireland, Denmark and Norway). What disturbs the picture a little is the deviant position of the sixth and final low B case, Iceland, where we have witnessed pronounced rate-based cuts over the past twenty years.<sup>172</sup> For the remaining countries in the configuration, we do not observe long-term cuts to tax rates when the number of income tax brackets is sufficient low.

**Figure 16** The number of tax brackets plotted against the aggregated effects rates across countries



Source: Own calculations based on OECD (2019b).

**Notes:** N = 19. The reference taxpayer is the taxpayer earning 300 percent of average wages. Switzerland and Luxembourg are excluded due to extreme thresholds scores.

Notice the 'long-term' label I attach to these cuts, as it is imperative to stress what I am *not* claiming. I do not conclude that income tax politics in low B

<sup>&</sup>lt;sup>172</sup> Iceland is a peculiar case. The bulk of the aggregated rates effects was accumulated when policymakers, before the Financial Crisis, introduced a flat-rate income tax policy by scrapping the 7 percent additional top rate after gradually phasing it out from 2003 to 2006. When a new top rate was introduced in 2010, it kicked in at a much higher threshold (the lower limit for the top rate was 1.01 percent of AW in 2006 and 1.48 percent in 2010). Much of the lasting rate-based effect actually came with the decision to reduce the basic income tax rate from 26.08% in 2000 to 22.5% in 2018, a 3.58% cut that benefited the richer groups alike.

settings is so tightly locked that we may never observe individual reform instances of tax rates being cut. In the in-depth case studies in **Chapter 7**, I will show one such 'exception' where the Danish Right coalition government in 2009 succeeded in reducing the top marginal tax rate with a bit of reform trickery, as they eliminated the so-called 'middle tax', the middle bracket of a three-tier income tax system, which had become a redundant tax bracket for calculating the effective tax liabilities.<sup>173</sup> My claim is, instead, on the long-term direction and how this institutional feature, the count of tax brackets, shapes the general mode of politics and what the political Right, and the Left for that matter, can reasonably (not) accomplish. The empirical pattern as established can, of course, be interpreted differently. While I reckon that the lack of aggregated rate-based cuts is caused by this lock-in mechanism of few brackets, another mode of politics that would generate the same results is a seesaw in which policymakers from either ideological corners take turns cutting income tax rates and raising them again. If we assign the specific roles, we would assume based on theory that the political Right would enact cuts while the Left would raise tax rates. However, the empirical material does not support this claim, not when we look at the raw underlying policy data that go into these aggregated measures, and not when we study tax reforms on a case-by-case basis, as done in **Chapter 7**.

Returning to **Figure 16** the second help square is demarcated by the Austrian and US cases on the *x*-axis and between the Australian and Spanish cases on the *y*-axis. Within, we find 11 of the 19 country observations represented in the figure. The contrast to the left-most cases is staggering, as ten hold negative aggregated rates scores, with Australia (0.60) as the slight exception. We observe the largest cutters 'at the bottom' in the form of Spain, Canada, and Finland, and as well the moderate and weaker ones closer to the zero point reference line. We know earlier from **Figure 14** that France, Australia, and the Netherlands cut income taxes significantly via the threshold-based route. Yet, the choice of policy mix is not the main point. The key is that only when the number of tax brackets becomes sufficiently high<sup>174</sup> are tax rates used in systematic, long-term ways to cut tax liabilities. It is not the only mean and

<sup>&</sup>lt;sup>173</sup> A main substantial finding is that this was a stealthier way to cut tax rates compared to lowering the top tax rate, and it made all the difference when it came to the move's political feasibility.

<sup>&</sup>lt;sup>174</sup> **Figure 16** suggests that this effect sets in empirically at around four tax brackets on average.

probably not the less politically contested method, but the path seems much more open than in the low B setting.<sup>175</sup>

# 5.7 The lacking long-term policy impact of progressivity

So what few tax brackets at hand do to politics, in terms of limiting the scope for rate-based cuts, seems clear enough. We have yet to look at how the second institutional parameter, the progressivity of the income tax distribution, affects policy. Of course, this can be studied from the aggregate level as well. Here, we have different expectations, not so much regarding the specific instrument choice but rather on how the pursuit of lower taxes is spread across the income scale. To recap from **Chapter 4**, I expect the Right's political fight to focus on the higher income groups in high progressivity countries, i.e. on countries that disproportionally carry the larger tax burdens. In contrast, their focus should be broader in low P cases where the rich and the poor alike face relatively high marginal tax rates on income. Note that whereas the claim on the impact of tax brackets is a general one that describes how politics is conducted regardless of who determines policy, the hypothesis on progressivity concentrates much more on how the Right as a collective actor should focus and behave. One pitfall of only looking at the aggregated country scores is that we do not get to witness how the Right, specifically, acts within this institutional frame. Both the events-based statistical approach followed in **Chapter** 6 and the country case studies in Chapter 7 are more suited to unlocking such insights. Nevertheless, I believe it is still informative for the broader tax question to consider whether politics that plays out in high and low progressivity settings, in general, follows a certain trajectory when it comes to outputs. More precisely, how the scope of policy changes might differ across income groups.

<sup>&</sup>lt;sup>175</sup> I refrained from commenting on the two obvious deviant cases in the high B universe, Japan and Portugal, which oversaw sizable increases in tax rates over time. They prove that it is not a deterministic theoretical proposition. Japan oversaw rates hikes on the higher income groups in 2007, when it switched from four to six tax brackets, and again in 2013, when it introduce a 2.1 percent surtax on earned income. In 2015, Japan added a new 7<sup>th</sup> tax bracket, a new 45 percent top rate (40 percent previously), yet it only targeted those earning 7.7 times of average wages. Portugal represents a case of two periods. Tax rates were reduced from the baseline up until 2009 when a series of post-crisis budgets increased rates both at the bottom and at the top of the income distribution. The latest hike came in 2018 with the introduction of two new tax brackets, going from 5 to 7.

One way to launch the discussion is to look closer at whether tax policies are reformed to the same extent if we fix on different spots on the income scale. Or whether altering the reference taxpayer changes the conclusion we can draw on countries' tendency to reform, to use the terminology of the novel measurement constructs. To proceed, it makes sense first to attack the issue descriptively, inspecting the correlations between the aggregated effects for the three different references. The joint measure for the 300 percent AW taxpayer thus shares a high degree of empirical overlap with that for the 50 percent AW taxpayer (corr = 0.54; p-value < 0.05), but even more with the 100 percent AW taxpayer (corr = 0.85; p-value < 0.001). The strong interrelations are not surprising considering the large commonality with the policy reforms that affect each of the taxpayers, as changes enacted at the bottom of the income scale inevitably impact individuals with higher incomes, albeit not to the same relative extent. Again, the obvious example is the decision to cut the basic rate on earned income, which results in lower taxes on both the poor and the rich, who pay a reduced rate on the subset of income that falls into this lowest tax bracket. Extending this logic, it is intuitive that the correlation between the 300 percent AW taxpayer and the one who earns the exact average wages is much higher, given there are many more potential policy changes that target the subset of income between half of the AW and the full AW, that would unite them.<sup>176</sup>

The correlation across countries between the 300 percent and the 50 percent AW taxpayer is pronounced, yet not perfect. This becomes even clearer if we compare the individual country scores directly. **Figure 17** (upper panel) displays the country variation in scores for the two aggregate measures, black circles for the 300 percent measure and grey squares for the 50 percent measure, aligned in ascending order by the 300 values. Once again, France is the steepest 'cutter', and Denmark is the largest 'raiser' looking at that particular taxpayer. A closer look at the figure reveals the relatively close relationship between them, as high scores on the one measure are generally accompanied by higher scores on the other, and vice versa. For several countries, we can observe a perfect or near congruence in policy tracks, most pronounced for Australia, Iceland, and Switzerland, where income taxes have been cut almost equally at the bottom and at the top, in relative terms. Yet, there are plenty of

 $<sup>^{176}</sup>$  Further, the correlation between the joint measures for the 100 percent and the 50 percent AW taxpayer is 0.64 (p-value < 0.01). Hence, there is statistical evidence of a larger policy overlap between what happens to, what we can deem, the average taxpayer and the relatively rich, than the same overlap between the average taxpayer and the relatively poor.

examples of non-congruent or diverging scores within the countries. The common pattern is that income taxes are cut relatively most (or not raised as much) for the richer reference taxpayer, as the cases of France and the Netherlands reveal. There are less frequent instances of the reverse, i.e. taxes on the poorer have been lowered most. Here, Austria is the clearest example.<sup>177</sup>

This difference in the size of policy change between income groups represents a variable of theoretical interest in itself. Why are some countries more prone to cut income taxes for the high than for the low income groups? And to what extent is this variable systematically linked to the progressivity of existing tax burdens, as the theory might hint at? To get a sense of this relationship, the lower panel of **Figure 17** shows what it looks like when these factors are plotted against each other. The difference in the joint effects is listed on the *y*axis, with negative values signifying that taxes, in the particular country case, were cut relatively more for the 300 percent AW taxpayer, and the other way round with the positive scores. As the mean aggregated scores across countries are -2.45% for the 50 percent and -4.88% for the 300 percent taxpayer, this explains why the values on the *y*-axis are predominantly negative. The progressivity measure on the *x*-axis is from the same OECD source as used in **Figure 8** in **Chapter 4**.

The lower panel of **Figure 17** reveals, however, that countries' tax progressivity and the long-term distribution of tax cuts across income groups are virtually uncorrelated (corr = -0.09; p-value = 0.74). The variance in especially pronounced within the group of low P countries, where we both find the countries with the steeper cuts at bottom (Austria and Japan) as well as those cases in which the relative benefits have been the most skewed towards the 300 percent AW taxpayer. As noted in **Chapter 4**, some of the latter countries are among those that held the highest statutory tax rates on top incomes at the start of this period, which may explain why policymakers and economists in these places have a more compelling case for reducing them than elsewhere.

<sup>&</sup>lt;sup>177</sup> Two major reform events, in particular, paved the way for this trend. First, when Austrian policymakers raised the bottom amount taxed at zero percent from €3,640 to €10,000 starting from the fiscal year 2006 while also introducing a relatively steep starting rate at 38.33% that replaced two prior marginal tax rates that were both well below the new rate. These changes predominantly benefited the lower income groups. Second, a reform of the tax schedule, commencing from 2016, reduced the marginal tax rates on the two lowest tax brackets significantly, from 36.5% to 20% and from 43.21% to 35%. The reform also introduced two brand-new tax brackets at the top of the income scale, now taxing incomes above €90,000 at a 50% rate and income above €1,000,000 at a 55% rate. The latter were obviously tax hikes that targeted the richest groups only.

But as evident from the figure, there is no strong evidence that implies an institutional steering of policy. However, as we will witness in the next chapter, this does not preclude progressivity from playing a key role in incentivizing the Right towards certain reform activity.



**Figure 17** Comparison of joint aggregated effects of low- and high-income taxpayers

Source: Own calculations based on OECD (2019b).

**Notes:** N = 21/18. '50 TP' is short for the taxpayer earning 50 percent of average wages. Ditto for '300 TP'. In the upper panel, countries are sorted (ascendingly) according to their joint scores on the 300 TP. The thick dotted line represents the best linear fit between the measures. Spain, Portugal and Switzerland er excluded from the latter panel due to missing values on the progressivity measure.

## 5.8 Conclusion

Summing up, this chapter has taught us a number of lessons on how income tax policies across the OECD have accumulated since 2000. The measures for the rate and threshold effects, which I have developed and presented in this chapter, represent an innovative bid as to how we can take the highest quality comparative policy data out there and compute it in way that captures this crucial instrument distinction. As demonstrated, the novel indicators exhibit good face validity, and it is my intention to make them soon available to all who have an interest in studying this subject.

I use the measures to derive this 'backdrop of facts' that we generally need to be aware of when we study (income) taxes comparatively during this period. Rates are threshold are not similar phenomena, as the 'aggregated' results display that if we neglect accounting for either of these parts we risk biased conclusions. Both when it comes to ranking countries' overall reform effects, but also when sizing up in what political ways they have been reformed. The chapter has further demonstrated that specific tax institutions are vital for setting the overall trajectory of policy and for limiting what can be achieved politically. A low number of tax brackets is strongly associated with the absence of long-term rate-based cuts. One of the reasons this finding is significant is that the low B starting point obviously also puts a limit on how much income taxes can be cut in the long-run within a given country, as those countries which have had success lowering tax rates are typically among those that have lowered income taxes the most. Finally, the findings in this chapter do not suggest a systematic link between tax progressivity and the long-term distribution of tax cuts across income groups. However, the coming chapter picks up this discussion when it sets out to test how low/high progressivity affects the reform tendencies of the Right, specifically.

## Chapter 6. The Right effect on major income tax reforms

While **Chapter 5** dwelled on possible conclusions from studying countries' aggregates, this chapter examines what goes on in-between; i.e. the year-toyear instances of policy reforms. This shift in analytical focus allows us to draw new types of inferences. Statistically, it takes us from looking at the results of N country observations to N by T, increasing the 'pool of data'. It enables us to rely on more sophisticated models of predictions to determine what increases the probability of reform events in a given country. On a more substantial note, it gives us an opportunity to study the role of the Right in terms of policy change. Can we, for example, find robust evidence that certain reform activities, such as tax-cutting reforms, are more pronounced in country years when rightist parties hold political power? Do the Right have an inclination to reform income taxes more (or less) in institutional settings of high or low progressivity and across a varying number of tax brackets?

I proceed as follows. First, I mark the playing field by describing the frequency of various reform types that exist in the data material, based on the novel rate and threshold measures derived in **Chapter 5**. I find that income tax policies were cut significantly (on the richer taxpayers) in about 13% of all country year observations, with a higher frequency in the years leading up to the Financial Crisis. Further, I demonstrate that was about twice as many major reforms (across the pool of countries) in which the lion's share of cuts were based on lower tax rates rather than higher-than-previous threshold limits. The data seem thus to confirm that when we have observed major instances of income tax cuts, it is much more common they have been rate-driven.

Next, I build my explanatory statistical models of income tax reform, first with a walkthrough of the arguments behind my choices of Right partisan indicator, control variables and model specifications. Using a series of logistic regression models, I find that the Right – on average – is a main driver of large tax-cutting reforms across the OECD, with the key asterisk that they mainly increase the likelihood of reforms that target relatively well-off groups, not low incomes. In line with the dissertation's theoretical claim, I find that this effect is more pronounced in settings of high tax progressivity and fading when progressivity is equally low. If we look at the reforms that intend to raise the level of taxation instead, i.e. the other side of the 'reform coin', I show that such reforms do not carry a specific partisan trace but are likely linked to circumstances where countries' fiscal balances are poor.

Finally, I look into whether Right partisanship predicts specific kinds of tax-cutting reforms. These dependent variables are even more fine-grained, or statistically 'thin' to use a different term, as we split the main category into their rate- and threshold-based components. The results are indicative of a 'selected' reform effect: the presence of Right parties in government can only explain event of tax-cutting reforms based on tax rates, not on thresholds. However, it is once again mainly driven the reform tendencies in high P countries.

### 6.1 The frequency of major income tax reforms

The measures for the rate and threshold effects, as presented in **Chapter 5**, possess tricky properties in terms of scale uniformity. To iterate, positive scores (hikes), negative ones (cuts) and zeros (status quo) are in my view distinct phenomena of politics that cannot be reduced to values on the same underlying

(linear) scale, if we wish to build more case-specific predictions as when taxes will be cut or raised.<sup>178</sup> I prefer to study each of them as separate species of reform events rather than to model them as a joint metric entity. This decision effectively transforms the measures into categorical indices.

To give an overview of how this 'events' approach affects the distribution of outputs, **Figure 18** is structured as a flowchart, inspired by set theory, that shows the subsets of different types of reform cases. To align the results with those in **Chapter 5**, I use again the 300 percent AW taxpayer as the reference in this example. All categories shown in the figure are provided with a corresponding number of observations and a percentage tally that indicates the category share of observations relative to the total number of cases. Starting from the top, we note that the number is 342 country year observations, spanning 19 countries<sup>179</sup> over 18 years (from 2001 to 2018). In 263 cases (or 77%), we

<sup>&</sup>lt;sup>178</sup> Another way of stating the same point is that model predictions of 'mean' values, as is what linear regression does, renders it difficult to say anything generalizable about the characteristics defining, for example, tax-cutting reforms, because the effects of covariates is assumed to be constant (i.e. linear) across negative values, zeros and positive values alike. Further, because there is a large proportion of zeros in the distributions for both the rate- and threshold-based policy measures, the linear model's effect estimates will be heavily skewed towards these cases, and not that much on the observations furthest away from the center, which arguably are of greater interest here.

<sup>&</sup>lt;sup>179</sup> Switzerland and Luxembourg are excluded in all **Chapter 6** analyses, as they are stark outliers on one of the key institutional variable of interest, the number of tax

can register at least one policy change when directly comparing this year's income tax rules to last year's – that is, the value of one policy parameter, rates or thresholds, must be increased or decreased, and however miniscule the change might be. Country policies were status quo in the remaining 79 cases.



Figure 18 A flow chart of income tax reform events across the OECD

Source: Own calculations based on OECD (2019b).

**Notes:** 342 country year observation for 19 countries. The reference taxpayer is the taxpayer earning 300 percent of average wages. The demarcation of 'major reform' is a policy change totaling 1 percent of total earnings in the given year, or if rate or threshold effects by themselves have an absolute value of more than 1 percent. The tax-cutting reforms are split according to the base ratio scores; if >0.5 then the reform is a threshold-based one; if <0.5 then it is a rate-based one.

Moving down the flowchart, we get to those cases that are perhaps of greater scholarly interest. The drawback of pooling all policy changes into one single

brackets. Including them severely biases the model estimates for the remaining countries. The generalizability of the results I present here is thus confined.

category is, as noted in **Chapter 5**, that it eliminates information on their relative size. One way to dodge this issue is to impose a benchmark for what would constitute only substantial reforms compared to the status quo. This is what has been done in Figure 18. Of course, any such demarcation must involve a relatively arbitrary judgement of what is 'sizable enough' to be counted and what is 'too small'. I chose to impose a rather simple threshold of '1 percent', implying that in order to be categorized as a *major* reform year, the tax liabilities must be cut or raised to an amount corresponding to at least 1 percent of the reference taxpayer's earnings.<sup>180</sup> For example, the tax liabilities of someone earning €50,000 has to be altered at least €500 in any direction within the given country year.<sup>181</sup> The figure reveals that 65 observation years (or 19% of all cases) meet this criterion. This number seems to strike a reasonable balance. On one hand, we have reduced the count of reform cases enough to make us confident that we are no longer grounding our potential empirical conclusions on the most trivial of changes. On the other, the pool of cases is still large enough for us to draw relatively precise statistical inferences on the drivers of major reform.

If we move down yet another level, the flowchart now splits the reform observations according to their policy direction based on whether income taxes are significantly cut or raised. The majority of these cases, 45, are taxcutting. It should be no surprise, based on what we have seen in the dissertation thus far, that cuts have been the primary mode of reform from 2000 and onwards with a ratio of more than 2:1 in favor of cuts over hikes, which was one of the prevailing reasons to focus on the role of the political Right instead of other families of parties. Going down to the final level, **Figure 18** splits according to instrument choice, showing that these tax-cutting reforms are also unequally split on this dimension. Twice as many reforms were predominantly based on lower tax rates (30 cases) than on higher-than-previous threshold limits (15 cases).<sup>182</sup> The data seem to confirm that when we witness

<sup>&</sup>lt;sup>180</sup> I also include cases where either the rate or the threshold effects by themselves are smaller than -1 percent or larger than 1 percent, even though their combined scores are not. Those are cases where cuts (hikes) to the one type of instrument were offset partially or fully by hikes (cuts) in the other. Hence, they do not register as large changes in the overall tax liability, but they do involve a noticeable restructuring of existing burdens, hence meeting a different criterion of 'major' reform.

<sup>&</sup>lt;sup>181</sup> I see it as a substantial change from the status quo, though other observers may disagree with this relative assessment. Obviously, there is an arbitrariness in that changes of, say, €501 are counted as a major reform while those totaling €499 are not, despite the trivial difference. But a cut-off has to be made somewhere.

<sup>&</sup>lt;sup>182</sup> These reforms were merely split according to a property I deem the *base ratio*. It simply captures the yearly (negative) score in the threshold effect and divides it with
*major* instances of income tax reform during this time period, it is much more common that they are rate-driven. Bear in mind that it does not equate that threshold limit are not changing significantly over time, as we clearly saw the opposite in the analysis of policy aggregates in **Chapter 5**. However, their mode of change is different; smaller, more frequent policy changes.

We see a rather similar pattern for the hikes reform. It is not explicitly listed in **Figure 18** but 17 of the 20 cases in this category are reforms where the higher tax liability was prompted by increases in the marginal tax rates. Only three were caused by significantly lowering the existing threshold limits – a rare empirical phenomenon. If policymakers enact tax reform aimed at raising the current income taxes, which by the way occurs in about one of every 17 country years, the overwhelming likelihood is that they do so by tuning the rates.

Another intriguing fact, which we cannot extract from the flowchart, concerns the periodization of these major reforms. There are clearly some ebbs and flows when it comes to timing. They become unmistakably evident in Fig**ure 19**, which displays the distribution of the major income tax reforms, as found using our novel policy measures, spread over the period 2001-2018. The timing of the events is recorded as follows: the year of reform is the enactment (or implementation) year, meaning that reforms dated to, say, 2008 refer to the recorded policy changes we can observe between 2007 and 2008. Hence, it contains no immediate information on the decision year, i.e. when these reforms were agreed upon politically, or whether multiple reform years within one country, by the method they are counted, can refer to the same political reform decision that causes tax rules to change over multiple years. The latter may be a potential source of error, since not everything we deem 'major reforms' necessarily refers to individual, independent decisions and should perhaps therefore not be treated as such. However, Annex A.V contains the full list and a graphical illustration of the major reform events, and it confirms that this phenomenon is not *that* common and hence not a source of concern: countries rather seldom record major revisions of the income tax code in two subsequent observation years.

the joint (negative) score of the threshold and rate effects combined. Scores of 0 indicate that all cuts came from lower tax rates and none from higher thresholds, while scores of 1 mean the opposite. Scores of 0.5 equate an equal split in attributed cuts. I divided the reform events according to this score, meaning that threshold-based reforms have base ratios above 0.5, while rate-based reforms have ratios below this value.

**Figure 19** The distribution of major income tax reforms (total reforms, cuts and hikes)



Source: Own calculations based on OECD (2019b).

**Notes:** The total number of major reforms shown in the figure is 65. The reference taxpayer is the taxpayer earning 300 percent of average wages. The black dashed line (cuts) and the greyish dotted line (hikes) are calculated as three year moving averages.

**Figure 19** breaks down the time distribution in two ways: as the total number of reforms that are recorded (grayish bars) measured as a year-to-year variable, and as reforms split into whether they involve tax cuts (black dashed line) and hikes (gray dotted line) calculated as a moving average of a three-year period, due to significant fluctuations in the individual reform years. The figure tells two complimentary stories. Looking at the bars first, we see clearly that the propensity to conduct major reform was much more pronounced in the first half of the period. Four of the five most prominent reform years, i.e. when the absolute number of reforms is six or higher,<sup>183</sup> were prior to 2010, and the last one in 2011. After that, the reform pace seems to have taken a bit of a dive, as the ensuing maximum lies at four reforms in a single year. This dip is also visible if we simply split reform years into two equally sized periods, from 2001 to 2009 and from 2010 to 2018. The averages for each period are 4.2 major reforms per year for the first and 3.0 for the latter.

<sup>&</sup>lt;sup>183</sup> Six reforms cases translate into about one third of the 19 OECD countries featured in this study experiencing major tax reform in that particular observation year, which seems like a lot.

What causes this levelling off in reform activity? It is, of course, tempting to link it to the Financial Crisis of the late 2000s, the timing of which corresponds roughly to our year split, i.e. the periods prior to and after the peak of the economic crisis. The explanation would then be one of fiscal leeway; taxcutting reforms come with a revenue cost, and it is easier, economically and likely politically, to fund steep cuts with the economy booming and the revenue streams flowing. In turn, it should be harder to justify when the same economy is in turmoil, and policymakers already face tough decisions on how to prioritize the available fiscal resources. It is an interpretation that meshes nicely with the trends we witness for the cuts/hikes split. The black line reveals that cuts were – on average – the norm in the boom years leading up to the Financial Crisis, whereas the gravish line shows that there were hardly any reforms in this period with the intent to raise tax liabilities. But, as Figure 19 shows, this script flipped from around 2010 to 2013 with a spike in the number of hikes reforms,<sup>184</sup> whereas the frequency of tax-cutting instances plummeted.<sup>185</sup> Again, it makes sense in relation to the Financial Crisis. In its aftermath, governments across the OECD were not only hindered from cutting taxes due to the poor fiscal realities; they were in many cases pressured to raise them, instead, to reduce deficits.<sup>186</sup> It is in any case telling that these trends reversed around 2015, when the dashed line overtook the dotted one once more. In the late 2010s, hikes virtually vanished once more, while cuts reforms rose, though not to the level prior to the Financial Crisis. One can speculate whether this rising trend simply continues, returning to the 'old normal', when the data series for the measures are extended with newer policy data. Similarly, it will be interesting to study the impact of the global pandemic and its economic ramifications for OECD governments, as it probably puts a fiscal bind on what they can reasonably do in terms of (lower) taxes, at least in the short term.

<sup>&</sup>lt;sup>184</sup> The value of the moving three-year averages peaked at 3.0 in 2012 for the hikes reforms.

<sup>&</sup>lt;sup>185</sup> The moving three-year averages were at the minimum value 0.33 in 2013 and 2014 for the cuts reforms.

<sup>&</sup>lt;sup>186</sup> Some obvious case examples include the countries that received bailout funds from the IMF (and the EU) during the Financial Crisis. To cut deficits, Iceland raised tax liabilities significantly in 2009 and in 2010; Ireland did it in 2009 and in 2011; Portugal in 2011 and in 2013; and Spain in 2012.

### 6.2 Issues on measuring the Right impact

After an in-depth examination of the political reforms we wish to explain, we turn to another key issue related to measurement; how best to capture the political strength of the Right in macro-statistical models. This topic, elsewhere referred to as the *independent variable problem* (Horn 2017), has been widely discussed in the partisan literature in recent years. Despite its obvious implications for the investigation of partisan effects, a small number of studies deliver any critical remarks on the gulf between the theoretical concept in guestion and the statistical indicator that is employed. The gold standard has been to use 'the share of social democratic cabinet seats' as *the* partisan measure, which usually takes one of two shapes – a year-by-year variable or cumulative cabinet shares over a longer time span.<sup>187</sup> At other times, a different party color of the incumbent - i.e. parties on the Right or Centrist or Christian Democratic parties – has been used to align more properly with the theoretical claim that is made. I also choose to rely on party labels for measuring the Right impact in this dissertation, following in many ways the literature convention. However, it is not a choice without concern. We know that these labels derive from the same types of expert scales and party categories<sup>188</sup> that are associated with a number of theoretical and operational issues. Especially if one tries to advance an argument on the importance of elite causal beliefs, as I do in this dissertation (see Chapter 3). Ideally, I would have preferred a partisan measure that came a little closer to tapping into the specific tax views we associate with the Right, the strength of which can, of course, vary across political elites in different countries. My ambition is not to play back this whole literature criticism of party labels point for point, as better overviews are certainly out there (see e.g. Döring and Scwander 2015, Horn 2017), but I will briefly reiterate the main arguments.

<sup>&</sup>lt;sup>187</sup> The former is based on the assumption that cabinets act quickly and independently from the institutional context when legislating, and a particular policy change is explained by the composition of incumbent parties at this point in time or in the immediate past. The latter is based on the premise that the effect of partisanship accumulates over time, essentially through mechanisms of ratchet effects, regime legacy, and ideological hegemony (Huber and Stephens 2001).

<sup>&</sup>lt;sup>188</sup> The classic reference point for the use of such measures is a study by Castles and Mair (1984) in which country experts were asked to place parties on a 5-point scale between *extreme left* and *extreme right* – giving us a measure that roughly captures a party's conceived spatial position within a given national party system. The number of categories is then usually reduced when the partisan effect is investigated statistically.

On the theoretical level, the most severe criticism is that cabinet shares derived from expert scales do not consider the ideological change of parties over time (or across space, for that matter); implying that partisan goals are *static*. Thus, both short-term and long-term adaptions of parties – moves invoked by a number of public policy and voter theories – are not captured properly. As the example of the alleged ideological transformation of left-wing parties demonstrates (Giddens 2000), classifications generated at one point in time many not be consistent with actual political ideas one or two decades later. It suggests that support to as well as rejections of partisan hypotheses could be an operational artefact of the ever-decreasing validity of party labels as valid proxies for Right parties' policy goals.<sup>189</sup>

Another validity concern with expert judgements is, of course, that they do not cover (*ex ante*) partisan positions but may rather reflect retrospective assessments of observed behavior or merely comprise a party's reputation of being Left or Right. On a general level, it is problematic if studies observe a relationship between partisan labels and policies while the ascription of labels is based on the very same policies and outcomes we are trying to present as our dependent variables. This is a circular argument and thus provides us with a potentially endogenous partisan measure. Applying this logic to taxation, it is to deem certain parties as belonging to the Right by virtue of their (historic) success in cutting income tax levels.

I am thus completely aware of the potential drawbacks of measuring partisan impact via cabinet shares. However, I do not regard the available alternatives as better, necessarily. For example, data from the Comparative Manifestoes Project (CMP) have become the preferred source for constructing positional partisan measures on the Left-Right scale and other ideological and policy dimensions. The project has collected information on policy emphasis for (almost) every party at each election over the entire post-war period for a large group of advanced democracies. The data are recorded as hand-coded counts of manifesto quasi-sentences related to a particular policy domain

<sup>&</sup>lt;sup>189</sup> To elaborate, it leaves us with a problem of empirical discrimination. If the nullhypothesis (no partisan effects) cannot be rejected, it is unclear whether ideological indifference or lack of political capacity to implement causal ideas is the cause of this non-finding. Here, the specific reading of the theory becomes paramount. The quintessence is that in order to do justice to the conflicting perspectives, those stressing the lacking maneuverability of politics and those highlighting the diluted political ideologies, we ideally need better indicators to test whether the assumption of ideological difference is accurate, *before* the partisan effect on policy-making is investigated.

(Volkens, et al. 2018).<sup>190</sup> Though manifestoes are not only written to inform voters about a party's goals on a given policy dimension but also to accommodate the strategic challenges in order to win an election,<sup>191</sup> the data have been used to derive positions for spatial modelling and to construct underlying Left-Right scales by adding several issues. The most famous such scale is certainly the Right-Left index (RILE) developed by Laver and Budge (1992), constructed rather inductively by qualifying statements as Left or Right by merit of their factor loadings. A far better attempt, in my view, was presented recently by Horn (2017), who relied on a more deductive, theory-driven approach to derive ideational measures for parties' welfare and market ideology, which he used to predict governments' propensity to enact risk privatization in the labor market domain.

These measures satisfy the condition of being temporally and spatially dynamic, which is obviously a desirable property that cabinet shares do not hold. But I do not regard the CMP data as a solid enough alternative for studying income tax dynamics due to at least two central caveats. The first is specific to the tax domain. While the CMP holds 56 different coding categories, none of these items are intended to capture party statements on taxes and tax policy, specifically. Which seems puzzling, because we know that such statements exist.<sup>192</sup> It is, hence, not an immediate option to distill all partisan mentions of tax goals and compute them into a single, conceptually validated dimension of the ideological divide between the Left and the Right within this domain. Let alone scales that would meaningfully capture the partisan struggle according to the central nodes of tax politics we have touched upon; e.g. levels and progressivity, rates and thresholds, cuts and hikes. Even if I had all the time and

<sup>&</sup>lt;sup>190</sup> They are, hence, based on the assumptions of *saliency theory* in that parties are thought to put their relative emphasis on favored issues and de-emphasize others rather than directly confront each other on the same issue (Jahn 2010). As Benoit and Laver (2006) correctly point out, the salience approach has been applied inconsequentially when the issue categories were designed. Around half of the items used are positional, which means that they consist of pro/con statements on the given topic.

<sup>&</sup>lt;sup>191</sup> While this is often the biggest demur to using manifesto data, it is evident that published party documents to a certain extent bind parties whose electoral success depends on their credibility.

<sup>&</sup>lt;sup>192</sup> A simple keyword search on the term 'tax' for the English-speaking manifestoes reveals that manifesto statements on tax matters are coded across a wide array of specific item codes and are not limited to those with the prefix '4', the main category that holds the economic domains. It reflects perhaps the tendency not to view taxation as a distinct mode of politics, a goal in itself, but rather as the (regulatory) means for achieving objectives across other policy areas.

resources in the world and chose to revisit the manifestoes, put considerable effort into identifying the sentences with relevance for taxation,<sup>193</sup> and finally recoded them appropriately, either by hand or using a sophisticated automated algorithm, I remain skeptical that it would improve the quality of measures much. My concern is tied to a second major challenge with the manifesto data, one that centers on document selection. As Gemenis (2017) notes, much of the CMP data are based on coding of documents other than national election manifestoes.<sup>194</sup> Hence, there is a large discrepancy when it comes to their authority, style, length and hence level of detail. The median length, counting the number of quasi-sentences coded, was just 605 sentences if we focus on the parties in the 19 OECD countries for elections after 2000, and even less in specific countries. They cannot be regarded as 'thick' sources of data to compute detailed tax 'ideology' considering these documents must cover a wide variety of political issues.<sup>195</sup>

I choose therefore to stick to cabinet shares to measure the Right impact, knowing that my argument hinges on the assumption that the right-wing party label is (still) a useful proxy for those causal belief systems we ascribe to Right party elites. Hereby, we accept the measurement errors as caused by natural variations in causal ideas across countries and over time. But the indicator should be good enough to capture what we are after; the claim that party labels have only weak or no relation to parties' ideologies is taking the argument too far, in my view. The measure of government partisanship is, as in **Chapter 3**, taken from the Comparative Political Dataset (Armingeon, et al. 2020).<sup>196</sup> It

<sup>&</sup>lt;sup>193</sup> The Comparative Agendas Project has managed this for party manifestoes spanning a small subset of the investigated countries, hereby coding the content according the CAP scheme with over 200 unique policy topics, including one for taxation (107).

<sup>&</sup>lt;sup>194</sup> Such examples include party leader speeches, draft manifestoes, local election manifestoes, newspaper ads, speeches by non-party leaders, party pamphlets, etc.

<sup>&</sup>lt;sup>195</sup> Benoit and his collaborators (2009) raised the problems related to document selection and considered the stochastic process of generating party manifestos, and they argue that manifesto-based policy estimates should come with associated measures of error reflecting the differences between documents. They rightly argued that longer documents are more authoritative and hence less prone to error but did not consider the differences between types of documents. Gemenis (2017: 8-9), however, convincingly illustrates the potential bias stemming from different party documents, in this case between manifestos and party leader speeches, as they yield entirely different estimates on its Left-Right position depending on which source is used.

<sup>&</sup>lt;sup>196</sup> I depart once from the dataset's party categorizations, as I have chosen, in the case of Spain, to recode the *Partido Popular* (Popular Party) as a Right party instead

ranges from zero to 100, with 100 indicating that all cabinet seats are occupied by members of Right parties in a given year. Most times, it is treated as a metric explanatory variable with the (implicit) assumption of linear effects across the scale, i.e. the same effect of an increase from a zero to a 20 percent share as from an 80 to a 100 percent share. It is too optimistic, in my view, as we should expect, theoretically, major shifts in effects either when Right parties gain representation in government (from zero to one), or when they gain the majority of cabinet seats and are the dominant political player in the cabinet (at least 50 percent of cabinet seats). The latter cutoff is the most suited for my analytical purposes. The statistical models feature a dummy version of the variable, with 0 representing country years when the Right held less than 50 percent of the seats, and 1 represents that they held at least 50 percent or more. The summary statistics (see

**Table 19** in **Annex A.VI**) shows that the variable mean is 0.51, meaning that Right parties held the majority of cabinet seats in 51 percent of the 342 country cases from 2001 to 2018. The variable holds the neat property of effectively splitting the observations into two groups of virtually equal size, allowing me to estimate the conditional means of each with relatively high statistical precession.

#### 6.3 Control variables

Having settled on the appropriate partisan indicator, we can move on to the control variables. A number of factors may affect both my Right dummy and the dependent variables in use, in the form of the various event measures, and are necessary to control for to avoid biased partisan estimates. Even if the rationale behind a potential effect of controls on the core explanatory variable may seem dubious, including the 'control' is still warranted as it predicts the propensity for major tax reforms (and is not determined by, hence a cause of, the measure of partisanship), since the inclusion in such cases helps increase the precision of other estimates.

The list of controls includes a number of variables commonly found in models of partisan impact on economic policy.<sup>197</sup> I control first for two factors that are crucial in determining the fiscal leeway of cabinets. The yearly percentage growth of real GDP is included with the expectation that higher levels

of a Center Party, as originally suggested by the authors. Its liberal-conservative traits bear stronger resemblance to traditional right-wing than to Christian Democratic parties.

<sup>&</sup>lt;sup>197</sup> **Table 18** in **Annex A.5** contains the full description of the variables included in the regression models.

of growth may increase the likelihood of tax-cutting policies by loosening budgetary constraints.<sup>198</sup> Related to the growth effect, my models also control for the cyclically adjusted annual government surplus as percentage of GDP – the so-called *primary balance*. The measure is scaled so that negative values equate periods of deficit and thus corresponds to a poorer fiscal state. Of course, the two are closely intertwined, if for no other reason that a booming economy breeds higher government revenue (the one half of the fiscal equation), but they do capture different aspects of fiscal pressure and are therefore both included.<sup>199</sup> GDP growth should also bear wider ramifications for income tax rules, in that a strong economy that raises wages and living standard across the board may inadvertently dampen pressure for tax cuts, as the net wages are already rising plentifully. On the other hand, the fiscal surplus is better suited for capturing the sum of already committed expenses to welfare causes (relatively to revenue), which is critical in determining the room for further tax cuts or the need to raise taxes. Regarding right-wing politics, weak economic performance at the level of society and government should cause electoral punishment and is thus expected to correlate with changes in cabinet composition. Data on GDP growth and government surpluses are drawn from the OECD databases on national accounts.

A related factor is the level of receipts, i.e. revenue, as a percentage of GDP, which is included as a third control. Whereas the primary balance expresses the balance between spending and revenue, referencing the fiscal equation from **Chapter 2**, this variable captures the absolute level of the latter. It conveys the logic that whether countries raise high and/or low levels of tax revenue can make a difference for the feasibility of reform. High revenue is generally associated with more extensive social policies, working as a proxy for the size of the welfare state.<sup>200</sup> More generous welfare provisions should increase

<sup>&</sup>lt;sup>198</sup> One can also make the reverse argument that low growth rates may potentially facilitate the need for income tax hikes, as the influx of new tax revenue dries up. <sup>199</sup> The bivariate correlation between them is 0.23 (p-value < 0.001) for my sample of observations. Not as high as one might suspect, but it reflects perhaps that most, if not all, of the cyclical component of the primary balance that is thought to work in accordance with economic growth rates is excluded from this version of the measure. I prefer the cyclically adjusted over the non-adjusted version of the primary balance, as policymakers arguably look more to the long-term status of public finances rather than dwell on year-to-year fluctuations caused by the business cycle when trying to decide on policies with an expected long-term fiscal impact such as tax reforms. <sup>200</sup> The bivariate correlation between total government revenue and total social spending, both as a percentage of GDP, is 0.70 (p-value < 0.001) for my sample (both

the size of the so-called 'welfare coalition', amplifying the pressure on policymakers to fortify existing social rights. In such a climate, it is tough overtly to choose tax-cutting reforms, and it may even require politicians of different cloths to find additional revenue within the tax system merely to maintain the existing quality of welfare. High levels of receipts should correlate negatively with the propensity to cut income taxes and positively towards hikes. For the same reasons, we may suspect that Right parties' tax messages do not resonate as clearly in such settings, making it slightly tougher for them to grab the executive power. The data on receipts come from the OECD, as well.

The next category of controls includes the three variables that describe the design of existing tax policies: the number of tax brackets, the progressivity of income taxation, and the presence of a threshold indexation scheme. As argued theoretically and shown empirically in the previous chapters, these are linked to the propensity of certain types of aggregated policy trends. They are included mainly because they are believed to be strong predictors of the dependent variables and key moderators of how the Right acts politically, but not so much because these institutional factors are correlated with the distribution of cabinet seats. My operationalization is line with the earlier chapters; the tax brackets are counted yearly as the number of 'non-zero' brackets, and tax progressivity is proxied via the top statutory tax rate on earned income due to missing data problems.<sup>201</sup> Further, the variable on indexation scheme is represented by a dummy that captures whether a country has such a scheme in place.<sup>202</sup> These data are also drawn from various OECD sources (see **Table 18** in **Annex A.VI** for details).

The final set of potentially confounding factors is institutional. Such factors are by definition near time-invariant, which has large consequences for any analysis interested in explaining reform dynamics. Though it is true that

measures taken from the Comparative Political Dataset). It underscores the proposition that governments generally spend (on social purposes) to the tune of what they raise in revenue.

<sup>&</sup>lt;sup>201</sup> Because we do not have good year-to-year measurements of tax progressivity, that cover all (or most of the) 19 OECD countries in the analyses, I turn to this proxy instead. As shown in **Chapter 4**, the top statutory tax rate on income captures a large chunk of the variation in tax progressivity measures, insofar as low levels of progressivity generally go together with high statutory tax rates, and vice versa. Equally important, the latter has yearly recorded data points and complete spatial coverage.

<sup>&</sup>lt;sup>202</sup> Here, I have chosen to disregard whether the adjustment yardstick differs, i.e. whether tax thresholds are linked to price or wage levels. The main effect on the propensity to reform should be whether such a scheme exists and to lesser extent on the specific adjustment rate.

national-level fixed institutions cannot *cause* qualitatively new policies within one country (Jensen 2014), it is a stretch, in my view, to assume that crossnational variation in such institutions is excluded from explaining why reforms on average happen at a higher or lower propensity.<sup>203</sup> The institutional measures used here - the degree of institutional fragmentation and the electoral system – correlate weakly with my dependent variables, but given their strong explanatory powers over cabinet formation patterns, excluding them may induce bias in the right-wing estimates. As the measure of institutional fragmentation, I employ the additive index developed by Huber and her collaborators (Huber, et al. 2004), which focuses on three nodes of policy systems: federalism (none, weak, strong), bicameralism (absent, weak, strong) and presidentialism (absent, present). The measures with scores scaling from zero to five capture the fragmentation of decision-making power in a country and is clearly distinguishable from the partisan makeup of the government at any point in time (Jensen and Mortensen 2014). Electoral systems are of key importance for cabinet composition, as proportional representation systems (PR) are well known for producing a much lower share of right-wing governments compared to majoritarian systems, at least historically (Iversen and Soskice 2008). Data on election systems are drawn from Liphart (1999/2012) and are simply measured via a dummy where majoritarian systems are coded as zero and PR as one.

**Table 19** in **Annex A.VI** reports the summary statistics on the variable in use, and **Table 20** just below it gives the correlation matrix.<sup>204</sup> Some findings are worth pointing out. First, the last column in the summary table displays the share of 'between variance' for each measure in proportion to total variance. It is an illuming property for data with a time-series cross-sectional (TSCS) structure, as it tells whether the measure varies mainly over time within the unit or primarily between units. The between shares, as reported in

**Table 19** seem to make a great deal of sense given the nature of each variable; the institutional variables, such as the threshold indexation, the degree

<sup>&</sup>lt;sup>203</sup> One of the most cited institutional claims in public policy is that an increasing number of *veto points* reduces 'room to maneuver' thereby causing policy stability (cf. Tsebelis 1995). Of course, I am not arguing that institutions *per se* carry certain preferences or policy goals, but they do provide the access points needed for actors to exert their opposition to a given policy change.

<sup>&</sup>lt;sup>204</sup> The correlation matrix contains lagged versions for five of the eight control variables, which is how they will be introduced in the regression models below. The logic behind the choice is the expectation that policymakers will predominantly be oriented towards last year's scores when deciding on tax reforms in given year. For example, they can only look at last year's GDP growth as their reference point, not the growth rate that exists while the political decisions are taken.

of institutional fragmentation, and the PR system, are all close to one, meaning they exclusively differ across countries and do not change over time. Conversely, the share is less than 0.5 for the two macro-economic controls, GDP growth (0.16) and the primary balance (0.43), implying that the main source of variation is within countries. More important, the table shows that the Right cabinet dummy, our main explanatory variable, is the one with lowest between share at just 0.11, meaning that difference in Right government participation as a political phenomenon is much more pronounced within than between. There is, in other words, a healthy dose of political turnover in most of the countries I study.<sup>205</sup> But it leads us to wonder; is it not problematic that we include controls that vary mainly across countries, when our partisan varies largely within? Yes, if we did not have more than one reason to include them in our models, as stated in the first paragraph. Though the correlations between the Right dummy and most controls are weak, as evident from the correlation matrix, I find plenty of examples when 'running my models', as I show below, where the decision to (not) include control variables makes a great difference in terms of the substantial findings.

#### 6.4 Model specifications

To examine the relationship between Right government and events of tax reforms, I estimate a series of logistical regression models. The choice reflects, of course, the dichotomous quality of the dependent variables. The basic logic is to estimate (changes) in the probability of observing the particular reform event as a function of the list of covariates. The model, specified for  $n = 1 \dots N$  countries and  $t = 1 \dots T$  years, has the generic form:

 $Pr(y_{nt}=1) = logit^{-1}(\alpha + \beta_v X)$  (7)

<sup>&</sup>lt;sup>205</sup> One could speculate whether this low between share was merely caused by the decision to use the dummy version of the Right cabinet seat share instead of the metric version. In terms of scaling, it forces artificial major shifts in the measure's scores, as it can only go back and forth between zeros and ones, instead of having the fine-grained nuances of the metric scale. If the cabinet composition measure could take all these in-between values, it would perhaps mean less within variance, because it does not have to travel the full scale in order to change. However, using the metric version of the Right measure yields a between share of 0.15, which does not alter the substantial conclusion.

where  $Pr(y_{nt} = 1)$  is the probability of observing a 'positive' outcome in country n in year t.<sup>206</sup> X describes the vector of the explanatory variables discussed above with the subscript v referring to the particular variable.  $\alpha$  is the global intercept across countries.<sup>207</sup> Besides the controls already described, the models add the lagged version of the given dependent variable. Often in TSCS analysis, it represents the best predictor of the dependent variable this year. Far from being a mere statistical fluke, it can been seen as reflecting the sluggishness of political processes.<sup>208</sup> As noted, I do not expect data on reform events to be as *sticky* as, say, spending data, but adding the lagged DV ensures that we pick up any 'persistency effects' in the individual models. It varies, if we look at particular DVs, but seems at a low level; the correlation between taxcutting reforms (300 percent AW taxpayer) at  $t_0$  and  $t_{-1}$  is 0.11 (p-value < 0.05), while it is just 0.05 (p-value = 0.37) for hikes reforms.

Because of the data's panel structure, one can discuss long and hard whether to include a battery of countries dummies that systematically control for time-invariant features that are unique to individual countries. From a statistical point of view, it means that we do not have to be concerned about omitted institutional variables, since all cross-national variation is captured this way. It also means that the only variance left to explain for the remaining variables is temporal or within-country. Given that most of the variance in my DVs takes this form, we seem to pay a small price for adding fixed effects.

<sup>206</sup> Equivalently, the equation can be written:

 $Pr(y_{nt}=1) = p_{nt}$ logit(p<sub>nt</sub>) =  $\alpha + \beta_j X$ 

where  $logit(x) = log(\frac{x}{1-x})$  is a function mapping the range (0, 1) to the range  $(-\infty, \infty)$ . It is preferable to work with  $logit^{-1}$  because it is natural to focus on the mapping from the linear predictor to the probabilities rather than the reverse (Gelman and Hill 2007: 79-80).

<sup>207</sup> In logistic regression, we do not apply an error term to the equation, as observations  $y \in \{0,1\}$  are assumed to follow a Bernoulli distribution with a mean parameter (a probability) conditional on the predictor values. So for any given predictor determining a mean  $\pi$  there are only two possible errors:  $1 - \pi$  occurring with probability  $\pi$ , and  $0 - \pi$  with probability  $1 - \pi$ . For other predictor values the errors will be  $1 - \pi'$ occurring with probability  $\pi'$ , and  $0 - \pi'$  with probability  $1 - \pi'$ . Hence, there is no common error distribution independent of the predictor values, which is why people sometimes say that 'no error terms exist' in logistical models.

<sup>208</sup> The prime example for public policy is, of course, budgetary processes and spending patterns that usually are deeply incremental, to the extent of being a law-like phenomenon (Jones, et al. 2009).

However, I refrain from doing so for two reasons. First, and this is the theoretical counter-argument, my models already include most of the deep institutional characteristics varying between countries – e.g. electoral system, size of the welfare state, etc. - which should control for the most important timeinvariant factors. Second and more importantly, the uneven distribution of the DVs when it comes the major reform events – characterized by a lot of zeros and few 1s – combined with the relatively modest sample size means that I risk dropping specific country time series from the model when I add the country dummies, if there is simply no within-variation to explain (i.e. no reform events within the given country).<sup>209</sup> It is a non-trivial issue, especially when I wish to explain the more peculiar reform instances, such as the type of tax-cutting reforms (rate-based versus threshold-based). Of course, I then allow for a potential (mild) bias stemming from unobserved heterogeneity, but it is a case, in my view, where 'the cure is worse than the disease'. I do handle, of course, the dependencies within the data structure when estimating the standard errors properly, as I apply clustered errors on the country variable, allowing for correlated error within each group.<sup>210</sup>

Dealing with TSCS data, one should almost always contemplate the 'true' lag structure of the main explanatory variable (Plümper, et al. 2005). Here, it translates into asking how quickly we should expect the effect of Right government to manifest itself in the DVs. Should it affect the propensity to reform only in the current observation year, or should a right-wing cabinet potentially have an impact on reform events down the line as well? The former claim is perhaps the easier to justify theoretically, building on the notion that the Right will enact, when passing tax reform packages, the bulk of the policy changes in the first coming implementation year. Also, if the Right, or others for that matter, hold the executive power, they are in a good position to block implementation of a tax reform adopted one or two years prior, if they did not consent to the content. Yet, it is difficult to rule out the hypothesis of a long-term effect without actual empirical tests. For this reason, I re-estimated all models with both a one-year and a two-year lag of the Right dummy, in addition to the current year's values. Yet, the parameters were always insignificant, and likelihood ratio tests suggest that adding the lagged version does not increase the explanatory power of the models. Hence, I stick with the one Right dummy

<sup>&</sup>lt;sup>209</sup> Had we had longer times series than 18 years, which is the result of both my theoretical focus and the data availability, the likelihood of observing at least one reform event per country would increase accordingly. Yet, given the conditions set by the data frame, excluding the country dummies is the more desirable option.

<sup>&</sup>lt;sup>210</sup> The models have been re-run with bootstrap standard errors, also, which do not alter the substantial conclusions one can draw from the results.

for the value at  $t_0$ . An important implication of this choice is that we must be sure that it is not reforms events *per se* (the DV's) that cause (change) in the partisan measure, as if this was the case, the empirics would be marred by problems of endogenity. Reassuringly, regressing the Right dummy on the various reform measures presented in **Figure 18**, using the same set-up as in **Equation (7)**, does not yield any significant partisan coefficients.

Finally, a word on the strategy of analysis. The reform events can be broken down in a multitude of ways, as we have seen, and with three reference taxpayers to cover also, this yields a large potential number of regression models to run and interpret. I have therefore chosen to focus the analysis mainly on the two indices of greatest theoretical interest, namely whether we can predict the occurrence of the major tax-cutting and the major hikes reforms (i.e. of major reform in either policy direction). If we study income tax reform at a higher level of aggregation here, for example *all* types of major reform (n = 65), we pool, in my view, two distinct political phenomena, insofar as we can reasonably argue that the effect signs of the covariates are not of the same size, perhaps not even in the same direction. The main explanatory variable, Right government, is a good example; it is expected positively to predict tax-cutting reforms, while we do not expect it to be positively associated with hikes.

To the extent I am able to find significant results for the Right dummy, I also wish to explore whether such effects are more or less pronounced in certain institutional settings, with reference to the number of tax brackets and tax progressivity, to test the theoretical propositions from **Chapter 4**. To do so, we simply add the interaction terms between the Right government and each of the tax institutions to test whether the latter moderates the effect size of the former. Equivalently, I wish to test whether the same significant effects can be found when the results are split into the type of reforms; can we say that the effect is mainly driven by a political pursuit to alter tax rates or threshold limits? I do this by including separate models for each output.

## 6.5 Does Right government predict major income tax reforms?

The short answer is 'yes'. The more elaborate version reveals, however, that it is a more 'selective' effect, settling one of the main puzzles of the dissertation. The results thus vary in coefficient sizes and statistical confidence. **Figure 20** reports the average marginal effect of Right government (with 90% confidence intervals) across six models; the left panel holds those for the models of tax-cutting reforms, while the right panel contains those for the hikes reforms.

The three models within each panel then refer to the three reference taxpayers; 50 percent of AW (black), 100 percent of AW (dark grey), and 300 percent of AW (light grey).<sup>211</sup>

**Figure 20** Effect size of the Right dummy for predictions of major tax reforms (cuts and hikes).



**Source:** Own calculations. See **Table 21** and **Table 22** n **Annex A.VII** for all model estimates. **Notes:** The estimated effects in the figure are the average marginal effects. Point estimates with 90 percent confidence intervals. The black circles represent the 50 percent AW taxpayer; the dark grey diamonds represent the 100 percent AW taxpayer; the light grey triangles represent the 300 percent AW taxpayer. The left-panel contains the major tax-cutting reforms; the right-panel the major tax-hiking instances.

If we describe the cut reforms, first, the coefficient of the right-wing dummy is positive across all three models; having a majority of Right cabinet seats seems, therefore, to increase the likelihood of observing major tax-cutting instances in a given country year. The congruence between the estimated coefficients should not be that surprising given the empirical overlap between what records as major reform events for each of the taxpayers. When rules are significantly altered at the bottom of the income scale, hence cutting the tax liabilities of the 50 percent AW taxpayer, the same policy changes will inevitably

<sup>&</sup>lt;sup>211</sup> Regression estimates for the full models, including controls, can be found in **Ta-ble 21** and **Table 22** n **Annex A.VII**.

touch those at the middle and towards the top of the scale too.<sup>212</sup> Yet, the populations of the reform events are different enough to produce varying statistical results, as shown by **Figure 20**. The coefficient size of the Right dummy (in the left panel) is progressively larger for the more affluent taxpayers, to the point where the effect is (only) significant for the 300 percent AW taxpayer ( $\beta$ = 0.59; p-value < 0.05). The coefficient is nearly as large for the 100 percent AW taxpayer, but the clustered standard error is noticeably higher ( $\beta = 0.53$ ; p-value = 0.147), while the coefficient is much lower for the 50 percent AW taxpayer ( $\beta = 0.31$ ; p-value = 0.333). When it comes to substance, this subtle variation reveals something crucial about how to understand partisan tax politics; we cannot say that some political actors are for or against lowering income taxes *per se*. The exact location where such cuts take place seems vital. The clearest right-wing imprint – in terms of average effects – is for the highest incomes,<sup>213</sup> not the middle or lower ones. It is important to note that the insignificant effects of Right government for the two other reference taxpayers do not imply that partisan politics does play a role for tax-cutting reforms. It only means that variation in reform propensity that cannot be attributed with statistical confidence to the partisan color of government. However, the insignificant estimates may imply a notion that it is generally easier for political actors across the spectrum to agree upon tax cuts for groups that fall below average earnings, since this policy accomplishes Left and Right goals at once. It creates efficiency gains from lowering the (marginal) tax burdens, and it entails an increase in the net incomes of these groups and (perhaps) a boost to economic redistribution at the societal level. Consequently, these 'non-findings' may be indicative of a separate, yet meaningful logic of politics. We can, at least, with certainty conclude that the Right has not been more prone to enact major tax-cutting reform in these parts of the income scale than their left-wing counterpart.

<sup>&</sup>lt;sup>212</sup> Especially if the cuts are rate-based, the richer taxpayers experience the same percentage cut as poorer taxpayers on the subset of income within the particular tax bracket.

<sup>&</sup>lt;sup>213</sup> According to model calculations, the predicted probability of observing a tax-cutting reform event is 12.9% under Right governments, when control variables are held at their means, and only 7.5% during non-Right cabinets. The absolute difference may not sound *that* impressive, but it is a sizable substantial effect. If one translates these numbers into reform frequencies, it entails that reforms occur, on average, once in every eight country years (7.7 to be exact) for Right governments, but only once in every 13 years (13.3) for non-Right ones.

The results in **Figure 20** are fairly robust to alternative specifications. I have run a set of models that feature a different delimitation of the DVs, replacing the '1 percent' threshold (measured as the change in tax liability) for deciding what constitutes a 'major' reform with one that looks only at the 10 percent most 'extreme' tax-cutting reform cases in terms of their joint effect scores (rate effect plus threshold effect). These are the observations furthest out in the left tail of the distribution.<sup>214</sup> As Table 23 in Annex A.VII shows, the only substantial difference from the main models is that the Right dummy for the 100 percent AW taxpayer is now significant at a 0.1 significance level  $(\beta = 0.68; p-value < 0.10)$ . It indicates that if we try to predict only those reforms that contain the steepest cuts, we distill a clearer effect of the Right; thus right-wing governments are, generally, more likely to enact the most extensive tax-cutting reforms for this particular taxpayer earning the average wages. Further, and with reference to Figure 19 and the temporal distribution of reforms, I have tried to include a 'crisis' dummy, before/after 2009, and the interaction term between this and the Right variable. The latter yields no significant results across the three models, indicating that the partisan effects, we have found, are consistent throughout the period of investigation.<sup>215</sup>

Finally, and turning briefly to the controls, only one of them exerts an impact of tax-cutting reforms that is statistically significant across the models.<sup>216</sup> Countries with a tax threshold indexation scheme are significantly less likely to conduct major tax-cutting reforms, and vice versa, though the effect is more pronounced when we study the lower end of the income distribution. The most straightforward interpretation of these findings is that the indexation scheme functions as a separate automated reform mechanism that likely softens the need for policymakers to pass major reform packages in order to curb fiscal drag over the long run. It meshes with the aggregated policy trends we studied

<sup>216</sup> We need to keep in mind that the estimated coefficients of the control variables are likely underestimated in the given model setup and should not be interpreted as their 'full effects', since any indirect impact that may be channeled through the measure of Right government is inherently attributed to the latter when the variables are included at once. Only the direct 'non-partisan' effects are left of the controls.

 $<sup>^{214}</sup>$  The specific cut-off values are -1.00 for the 50 percent AW, -1.21 for the 100 percent AW, and -1.24 for the 300 percent taxpayer.

<sup>&</sup>lt;sup>215</sup> A word of caution on the interaction models is, of course, that given our relatively modest samples of (positive) reform events, splitting these cases across the different levels of the interaction levels increases the probability of committing a Type II error (rejecting a true alternative hypothesis). To overcome this, the proposed interaction effects must be relatively large 'to register' as significant results. I am therefore not fully convinced that I can reject a hypothesis of a time-dependent partisan effect in this case.

in **Chapter 5**; countries without ongoing adjustment of threshold limits simply need to pass steeper single-event cuts to 'catch up' with the rest of the field.

If we turn to the right-panel in **Figure 20** with the major reforms that raise the level of income taxes as our DVs, we notice two things right away. The first is the positive coefficient signs in all three models; the presence of a right-wing government increases the likelihood of observing tax-hiking reforms all things equal. Second, we note that they are, once again, unequal effects in terms of statistical significance. Only the coefficient for the 50 percent AW taxpayer meets the 0.1 significance level ( $\beta = 0.70$ ; p-value < 0.10). In terms of probabilities, the estimated likelihood of observing a major reform instance is here 6.9% for right-wing cabinets (or about one in every 15 country years), while the same probability is 3.5% for non-Right ones (or about one in 29). The picture is seemingly reversed from the left panel; having the Right in government forms a political constellation that increases the chance of major tax cuts for the richer groups, especially, while concurrently boosting the odds of major tax hikes on the poor. This should lead to a non-trivial shift of income tax burdens between income groups, where the Right acts as the expedient. Since the incidence of tax-cutting reforms has a higher baseline probability than tax-hiking ones, we cannot reasonably conclude that the presence of Right governments, alone, is causing this pattern of relieving the high-income groups while further burdening the low-income ones. Yet, we can say that this pattern is reinforced when Right parties hold office. One is also tempted to think of the two types of reforms as conjoint in terms of timing; that these cuts and hikes happen in concert, for example to mitigate potential revenue losses. In order to 'give', the Right has to take the money elsewhere. Yet, the data disclose beyond doubt that these phenomena transpire at different time points. Of the 22 major tax-hiking instances on the 50 percent AW taxpayer, only one occurred in the same country year as a tax-cutting reform for the 300 percent AW taxpayer.<sup>217</sup>

What explains then the political decision to raise income taxes on the richer groups, if the partisan variable does not? According to **Table 22** in **Annex A.VII**, the most consistent predictor linked to such reform events is

<sup>&</sup>lt;sup>217</sup> The case is Spain in 2007. The government decided to abolish the former starting rate of 9.06% paid on taxable income up to €4,162. A new starting rate of 15.66% was introduced, and though the personal allowance was raised with €1,650 concurrently, these moves had the combined effect of raising tax liabilities on the 50 percent AW taxpayer, as judged by the available data. At the same time, the upper bracket thresholds were raised significantly along with a cut to the top bracket's rate from 29.16% to 27.13%, resulting in a sizable tax reduction for those at the top of the income scale.

countries' primary balance. The direct effect is negative and significant at 0.01, implying that a more positive primary balance, i.e. government surplus, is associated with a lower likelihood of tax-hiking reforms.<sup>218</sup> In other words, the better the state of the government's long-term fiscal sheets, the less likely it is that (any) government will raise income taxes significantly on the average wage earner and those above in the income distribution. Hence, it does not seem as an option that policymakers in charge resort to, unless they are forced to by poor public finances, which is when they need the additional revenue the most. Such interpretation is perhaps further propped up by the positive significant coefficients of another control in the same models, the total tax revenue variable (significant at the 0.05 level), which lends credence to the notion that countries with higher revenue levels, and hence more pronounced revenue needs, are generally more in the business of raising income taxes on high-income earners.

The conclusion for the Right regarding tax hikes can be summarized as follows: they choose to raise taxes predominantly towards the bottom of the income scale, and more so than the Left. It is probably a stretch to formulate this as a unilateral strategy of simply burdening the low-income groups as much as possible. The correct interpretation is rather that the Right prefer to impose higher taxes as broadly as possible, if political and economic circumstances dictate it. Yet, broad taxes , which can be understood as tuning the tax rules towards the bottom of the schedule, thereby 'hitting' as many taxpayers as possible, affect income groups disproportionally, if the higher income brackets are not adjusted accordingly. Yet, the latter seems mostly to materialize once the economy is in severe turmoil.<sup>219</sup>

If we go back to the left-panel results for the tax-cutting events, which is the phenomenon of higher theoretical interest for this dissertation, we should examine, for example, to what extent the Right has a higher propensity to enact such reforms in specific institutional settings. The obvious result to study

<sup>&</sup>lt;sup>218</sup> For the 300 AW taxpayer, the predicted probability of major tax-hiking reforms is 8.9 percent when the primary balance variable is fixed at the 10<sup>th</sup> percentile (-4.64% of GDP) with the other variables kept at their means, while it is as low as 1.7 percent at the 90<sup>th</sup> percentile (4.00% of GDP).

<sup>&</sup>lt;sup>219</sup> These unequal drivers across the models of cuts versus hikes only reinforce the point of treating them (statistically) as qualitatively different outputs in need of explanation, and not just as ends on a metric scale. Had we, for example, pooled all the major reform events (cuts and hikes) together as our model DVs, chances are that the Right dummy would never yield statistical results, because it does not predict cuts and hikes equally well across the different classes of taxpayers. Hence, the actual significant sub-effects would be biased towards null-findings, and we would not be able to establish, empirically, the different trends for the opposing policy directions.

in further detail is the significant Right effect we found for the 300 percent AW taxpayer.<sup>220</sup> In line with the theoretical framework, I test whether the Right effect is augmented or diminished when we can include an interaction term between the right-wing dummy and the number of tax brackets, and the same for our proxy variable for tax progressivity, in subsequent models. Here, it is important to keep in mind that these findings are not directly comparable to those in **Chapter 5**, which purely looked at long-term policy trajectories set by these institutions. The two chapters cover, hence, the main ways we can imagine institutions affect policies: how they pave the most likely long-run policy path for the broad group of political actors, and how they specifically affect the incentive structure of the Right as they govern on a year-to-year basis. The interaction models can be of use to say something of the latter mechanism. Referencing **Table 6** in **Chapter 4**, I mainly expect progressivity to moderate the reform strategies of the Right, specifically, resorting to more high-end cuts in high P settings.

**Figure 21** plots the average marginal effects of the right-wing dummy at various levels on the tax bracket variable (upper panel) and of the top statutory tax rate measure (lower panel).<sup>221</sup> The point estimates are represented as a full line, while the associated 90% confidence intervals are represented as dashed lines. The vertical axis is where we find the size of the average marginal effect. When the confidence intervals include zero on this axis, it means that the effect of the Right is statistically indistinct from zero, i.e. has no effect. The two plots cover the entire range of the respective interaction variable from minimum to maximum.

Certain results are worth commenting on. In the upper panel, the figure does not leave the impression of an immediate interaction between the presence of a Right-dominated government and the number of tax brackets; the estimate for the average marginal effect stays between 0.4 and 0.6 (on the *y*-axis) for the whole range of the moderating variable.<sup>222</sup>

<sup>&</sup>lt;sup>220</sup> In supplementary analyses, the following interaction models have been run for the 50 percent AW and the 100 percent AW taxpayer too, adhering to the notion that the conditional effects of a main explanatory variable may be significant, even though the main effect of the variable is not. However, I do not find any consistent conditional effects that are distinguishable from zero for either DV.

<sup>&</sup>lt;sup>221</sup> The full regression estimates for both interaction models is available in **Table 24** in **Annex A.VII**.

<sup>&</sup>lt;sup>222</sup> This interpretation is supported by the insignificant term between the variables ( $\beta$  = -0.10; p-value = 0.657).

**Figure 21** Effect size of the Right dummy at levels of tax brackets and tax progressivity (proxy)



**Source:** Own calculations. See **Table 24** in **Annex A.VII** for all model estimates. **Notes:** The estimated effects in the figure are the average marginal effects. Point estimates (full lines) with 90% confidence intervals (dashed lines). The upper-panel has the number of income tax brackets as the moderating variable; the lower-panel holds the top statutory income tax rate as the moderating variable.

Further, the Right effect is only statistically distinguishable from zero for the bracket values around 3 to 5. However, the fact that the coefficient estimate does not change noticeably within this range indicates that the different levels of statistical confidence are merely tokens of the uneven distribution on this

interaction variable, given that tax schedules in the majority of countries have 3 to 5 tax brackets.<sup>223</sup> The decision of Right governments to enact a major taxcutting reform on high-income individuals is thus, on average, not affected by this institutional measure. But as the theory predicted, we expect the number of tax brackets mainly to steer the instrument choice of policymakers, rather than the tendency to enact major reforms, and we expect them to affect the Right and the Left in a roughly equal manner. This lack of interaction aligns, hence, pretty well with what we would anticipate.

Interaction is, by contrast, clear in the lower panel of **Figure 21**. When the top statutory tax rate is at a sufficiently low level, associated with high tax progressivity as formerly noted, the Right effect is especially pronounced. Here, there is a strong statistical link between the main explanatory variable and the likelihood of introducing major tax-cutting reforms. However, this effect tends to decrease at higher rate levels, as the conditional average marginal effect becomes indistinguishable from zero, once the rate variables take values of 50 percent or above. This cut-off excludes all country years from the distinct 'high taxes, low progressivity' countries such as Denmark, Sweden and the Netherlands, yet almost 59% of all sample observations have statutory rates below this threshold. The interaction carries a substantial impact too. The predicted probability is 13.5% for right-wing governments when the top statutory rate is at the 10<sup>th</sup> percentile score (43.7%), while it is 11.2% for the similar prediction at the 90<sup>th</sup> percentile (55.9%).

Bear in mind that the interaction results in no way invalidate the main conclusion from this section: Right politicians in government *are* the key politico-economic factor to understanding the timing of major income tax cuts. However, by exploiting one of the two key tax institutions, we are able to define the scope of the Right effect further. The conclusion is thus straightforward; the Right is far more likely to pursue the major reforms when tax progressivity is high, i.e. when there is a large discrepancy from the outset between the tax burdens of the rich and the poor. The impression left by the results is that the Right is more often capable of imposing their ideological will onto politics in this context, with ensuing large-scale reductions in income taxes that are expected to generate tangible efficiency gains. As stated in my theory, it is simply better politics for them in high P contexts, because one can

<sup>&</sup>lt;sup>223</sup> In a supplementary analysis, I used a dichotomized version of the bracket measure (as interaction variable) to explore whether this would yield different results. Following what we learned from **Figure 16** in **Chapter 5**, I split the measure into two groups of '3 brackets or below' and '4 brackets or above' to maximize the statistical power. This did not alter the substantial interpretation of the results, and the new interaction term was insignificant ( $\beta$  = -0.51; p-value = 0.197).

make a more compelling case of selling the (relatively) higher marginal taxes at the top end as the chief structural problem of the income tax code. The effect vanishes as the relative tax burdens between the income groups are more offset. This conditional relationship naturally begs the question why Right governments are not, on average, more prone to enact such major reform than the reference, non-Right cabinets, in low P settings. It is again important to understand that this is a mean estimate, as it is evident from the full list of reform events (Table 17 in Annex A.V) that income taxes have been reduced steeply in plenty of countries where the Right has been the responsible political agent. One well-known case is the Danish tax reform of 2009 ('The Spring Package 2.0'), to which I return in **Chapter 7**, where the Right coalition cabinet carried out large cuts by eliminating, along with other policy initiatives, an entire tax bracket designated for the middle-income earners, from which the higher income groups profited tremendously. However, the large-scale evidence suggests that it is generally not the specific task of Right governments to slash income taxes for the rich when tax progressivity is high.

There may be various explanations for this pattern. We know from the findings in the previous chapter that it is not because income tax policies have stood still in the notorious low P countries during this period; income taxes were generally cut, and actually more so for relatively well-to-do than for lowincome taxpayers in many of these countries (revisit Figure 17). Yet, as the results above attest, we cannot attribute this long-term trend of cuts to specific major reform instances that are primarily initiated by the political Right. In my view, this leaves us with two alternatives. One possibility is, of course, that other partisan actors beyond the narrow Right have (also) made it their political priority to reduce the comparatively high tax burdens faced by high-income earners in low P systems, perhaps because it is easier to paint them as infeasible from an economic vantage point. Or that Right parties in opposition can perhaps exert significant leverage over the income tax policy in this context, pressuring the other parties in power to do what *they* would have done in this area. It is tricky to corroborate this interpretation with the results at hand. A second explanation revolves around the size of the individual reform events, as one could reasonably argue that it is more politically contentious to cut taxes on the rich as steeply, and thereby as visibly, if the (relative) tax burdens of the rich and the poor are closer to each other. The mode of reform that is then possible in low P settings may be to cut income taxes more moderately to avoid the worst political backlash. If this proposition holds, relaxing the cutoff of what constitutes a major reform (currently set at a 1 percent change in tax liabilities) and including a higher number of these moderately sized reforms might offset the strong interactive relationship between cabinet color and tax progressivity, which we see in **Figure 21**), as we feature a larger pool of potential reforms for which the Right can be the responsible agent.<sup>224</sup>

# 6.6 Does Right government predict the incidence of rate-based or threshold-based reforms?

The final wrinkle to this chapter is to split this category of major tax-cutting events into subgroups that align according to their policy designs, i.e. whether reforms were based predominantly on political decisions to lower tax rates or to raise threshold limits. The focus is, again, on the 300 percent AW taxpayer, where we have been able to locate the right-wing effect most consistently. To achieve this subgrouping, I simply rely on the same split of reforms according to the base ratio, as done in Figure 18 earlier in the chapter, and end up with two groups of unequal size; one with 30 rate-based reform cases and another with 15 threshold-based ones. The latter, especially, generates some obvious concerns about the count of reform cases, as it is not a lot to establish consistent partisan estimates with a high degree of statistical certainty. Yet, it says something about the true distribution in the population, and we cannot conjure additional reforms into one group simply because it is methodologically convenient.<sup>225</sup> To boost the samples, one could (again) attempt to relax the criteria for what counts as a major reform, lowering the 1 percent threshold to, say, 0.5 percent. This would yield 80 tax-cutting reforms instead of the 45 generated by the previous cut-off, split into 47 rate-based and 33 thresholdbased instances. Yet, the decision to increase the group sizes in this fashion, at the cost of diluting the concept of 'major' reform, does not alter any of the main substantial findings I present below according to supplementary analyses. Hence, I stick with the current computation of the data.

<sup>&</sup>lt;sup>224</sup> A third explanation concerns the measurement of the Right, referencing the prior discussion in this chapter. The analysis will be biased if the Right measure does not capture the same political orientation of the party elites that populate the Right cabinets we study. If these qualities are systematically linked to, for example, tax progressivity, that the Right generally thinks and acts more 'right-leaning' in countries with high progressivity systems (than in low P countries), then it becomes an explanation of political ideology rather than of the feasibility of certain reform strategies. <sup>225</sup> One could move the base ratio cut-off to a lower value, so we would include some of the rate-based reforms that contained a mix of rate and threshold measures, yet tilting to the former. For example, base ratios of 0.3 or 0.4. Yet, the concern for more balanced group sizes would violate the concern for conceptual stringency in that the line between what counts as a reform of either type would be blurred to the point that it is difficult to grasp what actually constitutes a threshold-based tax reform.

The next step is to re-estimate the base model from **Equation** (7) with these two new DVs.<sup>226</sup> Figure 22 presents the average marginal effect for the right-wing dummy for both models, with the black circle and its confidence intervals representing the rate-based model, and the navy square signifying the threshold-based one. The difference in the coefficient estimates is immediately telling. The Right effect is positive and statistically significant ( $\beta$  = 0.78; p-value < 0.05) in the rate-based model, indicating that right-wing cabinets, relative to non-Right ones, have a propensity to enact major tax-cutting reforms with cuts to the marginal tax rates as the main content. Given the Right's affinity for lowering tax rates, as derived by theory in **Chapter 4**, by virtue of the efficiency gains they are expected to produce, the findings make sense from the standpoint that such reforms have a higher likelihood of being introduced when policymakers from Right parties dominate the cabinet despite. The model yields a probability of 8.7% in this case, when control variables are kept at their means, versus 4.2% when a non-Right government holds executive power.227

We cannot find a similar positive effect when modelling the thresholdbased reform, as evident from **Figure 22**. The estimate coefficient is insignificant ( $\beta$  = 0.18; p-value = 0.707), implying that Right governments are not more prone to introduce major threshold-based reforms in a given country year. We do not need a set of regression models to arrive at this conclusion, perhaps. If we study these reforms in pure descriptive terms, we find that right-wing cabinets were in office during eight of the 15 reform instances, as close to half of them as possible, and hence with a distribution not skewed enough to establish a clear partisan pattern. Yet, we can observe that one institutional feature is strongly linked to the reform propensity of this type, the small-N notwithstanding, namely the existence of a threshold indexation scheme. Its negative significant direct effect reveals that countries with such a

<sup>&</sup>lt;sup>226</sup> The threshold-based reform model was estimated without the inclusion of a lagged DV, as its inclusion, not surprisingly, predicted the non-reform outcome (DV = 0) perfectly for a substantial share of the country time series. Here, I chose to keep the full sample over model stringency across the two DVs.

<sup>&</sup>lt;sup>227</sup> Further, supplementary analyses show that the interaction relationships from the non-split models (**Figure 21**) can be replicated virtually 1:1 when using the rate-based reform measure as the DV. It signals that the conclusion on the conditional Right effect extends to the introduction of rate-based reforms, specifically,

scheme are much less likely to experience major threshold-based reforms for the rich, for the same reasons we have already pondered.<sup>228</sup>

**Figure 22** Effect size of the Right dummy for predictions of rate- and thresholdbased reforms



**Source:** Own calculations. See in **Table 25** in **Annex A.VII** for all model estimates. **Notes:** The estimated effects in the figure are the average marginal effects. Point estimates with 90% confidence intervals. The reforms are split according to the base ratio scores; if >0.5 then the reform is a threshold-based one; if <0.5 then it is a rate-based one.

#### 6.7 Conclusion

The main takeaways from this chapter can be summarized as follows. The Right plays a vital role when we wish to explain the instances of major income tax reforms over the last twenty years. A vital, but selective role, as shown. On the theoretical level, the earlier chapters were at times relatively vague on answering the question as to how the Right would ideally prioritize between tax cuts at the different ends of the income scale. The results in this chapter seem to provide an unambiguous answer: Right presence in government increases the likelihood of tax-cutting reforms that target high-income groups, while their presence at the same time boosts the likelihood of major tax hikes on the poorest, if we focus our study to how the Right affects the main parameters of

<sup>&</sup>lt;sup>228</sup> These are therefore likely the similar observations that drove the negative coefficient for the same variable in the non-split models that included all major tax-cutting reform, which we dwelled upon in the prior section.

the income tax schedule. The results are pretty telling, but perhaps not too surprising. It is important to remember we are discussing 'average effects' that reflect varying circumstances across the individual country cases. The findings provide thus support for the one of the dissertation's institutional claims: the Right effect is stronger in high P configurations. Together with how **Chapter 5** demonstrated evidence for the tax bracket proposition, the macro results generally lend credence the suggested institutional mechanisms. Finally, the chapter shows this Right effect extends only to the rate-based major reforms, of which there are most. Given the listed pitfalls, the Right may face when slashing income tax rates overtly and in a major fashion, these results may push back a little bit on the many 'constraint arguments' presented in **Chapter 4**. Yet, I wish to stress the effect is especially in those settings where the Right has a stronger incentive and claim to cutting income taxes on the richer.

The last two chapters cover some of the most relevant ways we can 'cut' the policy question: how policies aggregate and the major instances of reform that are likely to receive public scrutiny. An empirical perspective we still wish to untangle is how the Right, more specifically, acts in institutional settings when there is less than ideal conditions for cutting rates. Some of the strate-gies which the Right employs here are perhaps too subtle to be captured in large-scale quantitative analyses. Oftentimes such reform processes underneath the macro trends are a lot more complex, partly because holding office does not always equal supreme power over policy formulation, whereby policy becomes the results of the interplay between a large variety of partisan actors and stakeholders. **Chapter 7** will dig into these more complex but vital political processes to get a fuller picture of the Right and income taxation.

### Chapter 7. Income tax reforms in Denmark, the United Kingdom and the United States

This chapter explores the income tax reform strategies of the Right in Denmark, the UK, and the US. The three countries represent very different political systems and tax configurations, as detailed in **Chapter 4** and later in this chapter. This allows me to study the commonalities of the Right across the Western world as well as how the distinct experiences of the countries influence the policies adopted.

The three countries fit my institutional ideal types. Denmark is a clear example of the low B, low P case – a country with relatively few tax brackets built into the tax schedule and with very little progressivity. The US case is the offdiagonal one, while the United Kingdom combines the B score with high tax progressivity. The theory predicts that this leads to different policy strategies, as per **Table 6**; a policy style tuned to thresholds when the number of tax bracket is low, and one tuned to top end cuts when progressivity is high. This picture was confirmed in the macro analyses in **Chapter 5** and **Chapter 6**, but we need to identify the evidence at the case level too to sustain a truly convincing theory of Right impact.

The chapter proceeds in the following way. I expand, first, on my case selection considerations, including the specific reform instances in each country chosen for further analysis; the 2009 Danish tax reform, the 2017 US reform (also known as the 'Trump tax cuts'), and the UK budget acts of 2012 and 2018. Each represents a 'typical' reform according their respective institutional logics. I dive into the reform processes by focusing on two types of observables: what the Right actors *do* in terms of policy, and how they *speak* of these proposed changes. To get an in-depth picture, I rely on an extensive list of legislative sources and reform documents as well as systemic reading of the media coverage in the run-up period before the adoption of reform.

Across all countries, I find that the Right generally pushes for income tax cuts due to strong ideological convictions of efficiency gains. In that way, we find a predictable Left-Right conflict pattern: Right parties are concerned with economic growth and work incentives, while the Left are preoccupied with inequality concerns. Policy-wise, this manifests itself in very different ways in the three countries, as the Right seem to 'flow' with the design of their tax systems. Thresholds, and setting the 'Right' limits, have been vital to the partisan tax strategies in Denmark and the UK, whereas the whole 'base discussion' in the US has only dealt with the broad issue of bracket simplification. The US reform case reveals that Republicans were aggressive in their pursuit of scaling back the top marginal tax rates. Further, the analysis demonstrates how the locus of tax cuts differs across the cases, as cuts have been relatively broadbased in Denmark, whereas the Right in the UK and the US have pursued a more open strategy of cuts skewed towards the top.

#### 7.1 Choosing specific reforms to study

Having established the broad trends of (Right) governments' income tax policies, I will now unpack the details in case studies. My theory posits, as noted, that the politics of the Right plays out differently in specific institutional configurations, which either augment or constrict the political room to maneuver. To reiterate, I expect the Right's strategy to be least constrained in settings with many tax brackets and high progressivity, because it gives them a tangible reason to pursue tax cuts for the middle-to-high income groups and a large set of policy instruments to work with. In comparison, few tax brackets and a simpler tax schedule cause them to pursue cuts to threshold instead of lower rates, and lower progressivity generates a pressure to cut taxes more evenly across the entire income scale. **Table 6** in **Chapter 4** gave the full overview of the expected strategies for each regime type.

Denmark, the United Kingdom, and United States fit three of these four ideal types and are chosen to maximize the variation on these institutional factors. When it comes the number of tax brackets, Denmark and the United Kingdom score well below the OECD mean, while the United States figure in the high end on the same variable.<sup>229</sup> In terms of tax progressivity, Denmark's is low, while the UK and the US both have highly progressive income tax systems. If we return to the descriptive split on the two dimensions (see **Figure 8** in **Chapter 4**), the three align clearly in their respective corners from the full pool of potential countries. What about the fourth corner – the high, low P case – one might ask? Countries like Belgium or France would be the obvious choices here. Yet, as I noticed in the theory, it is also were my expectations on policy strategies are weakest, or least specified. For this reason, I chose purposely to focus on the other three – in the first stage – where the larger political differences are expected to manifest themselves.<sup>230</sup> Further, because

<sup>&</sup>lt;sup>229</sup> The mean Danish and UK bracket number from 2000 to 2018 was 2.47 and 2.89, respectively, with an OECD average of 4.97 for the 21 countries studied. The US mean score was 6.26.

<sup>&</sup>lt;sup>230</sup> The combination of the three countries comes with high analytical leverage; if we are not able to find tangible strategic differences across the described dimensions, we are likely not going to find them elsewhere.

the Right's use of threshold instruments in low B settings is not sufficiently uncovered in this point, it is important to me to choose at least two such country cases. A natural avenue for future research is, of course, to explore the indepth reform mechanisms across a larger subgroup of Western countries.

The three countries share a neat quality with respect to the explanatory variable. All had longer stretches of right-wing rule over the last 20 years under different heads of government: Fogh Rasmussen (2001-2009) and Løkke Rasmussen (2009-2011, 2015-2019) in Denmark; Cameron (2010-2016), May (2016-2019 and Johnson (2019-) in the UK; and Bush (2001-2009) and Trump (2017-2021) in the US.<sup>231</sup>,<sup>232</sup> In addition, plenty of new income tax legislation was introduced during this period. It is, of course, a mammoth task to identify the hundreds (if not more) individual policy changes and tweaks made to the income tax codes. Finding the major reform instances, i.e. the most significant changes, is more manageable, as they tend to generate a lot of media and scholarly mentions. Using data collected on each country's parliament websites and governmental pages verified with references in the biannual OECD Surveys as well as other secondary sources, I first generated gross lists of income tax reforms in each of the three countries. Their timing is on display in **Figure 23**, which combines the overview of rightist rule with the specific reform events.

The figure reveals two things at least. First, it says something crucial about the way fiscal policy, or income tax reform more specifically, is decided upon politically. In Denmark and the US, major tax alterations are typically not set in relation to a yearly budget. Rather, they take the form of large one-shot reform events that typically end up defining income tax rules for a number of years going forward, until a need for new reform is established. In the UK, new tax legislation is decided exclusively in the annually. Finance Acts enacted by Parliament, often containing multiple provisions to all types of taxes and duties at once. In particular, it sets out the principal tax rates and thresholds for the ensuing fiscal years.<sup>233</sup> I flag the difference, as it is clear that it carries obvious implications for how we should study the political context. In Denmark

<sup>&</sup>lt;sup>231</sup> One further, and important, commonality is this writer understands the languages of the three countries, which is a requisite for grasping the content of primary sources.

<sup>&</sup>lt;sup>232</sup> We had a Republican-led Congress in most of these presidential periods too (2001-2007, 2011-2019).

<sup>&</sup>lt;sup>233</sup> These policy changes are announced together with the Chancellor of the Exchequer's speech on Budget Day. It is typically held in March, as the UK fiscal years go from 1 April to 31 March of the following year. Additional Finance Acts are common, however, and are often the result of a change in the governing party due to a general

and the US, we must expect the income tax instruments to be the focal point of these reform packages, while we should assume a stronger fusion of spending and tax measures in UK political discussions, since the budget is *the* prime legislative occasion for affecting both. Further, it entails a longer gross list in the UK case due to a higher frequency of 'natural' reform opportunities. At the same, the list requires critical sorting, since it is obvious that not all opportunities for major income tax reform are taken.

**Figure 23** Overview of periods with Right head of government in Denmark, the UK, and the US



**Notes:** The greyish areas represent times with a Right head of government, while the non-colored areas are times with non-Right cabinet leaders. The circles indicate major 'one-shot' instances of income tax reform, whereas the triangles – in the UK case – represent the yearly fiscal budgets, where income tax rules are usually set. The red figures are those chosen for further case analysis.

The second aspect of **Figure 23** worth commenting on is the number of major reforms conducted during the Right and non-Right government rule, at least in the Danish and American cases. It is a division that follows a familiar pattern. Four of the five major income tax packages in Denmark have been enacted by Right cabinets. While it is perhaps partially explained by their longer government duration during this period, the Right's relative frequency of reform instances, i.e. the number of cabinet year per reform, is still larger than for the non-Right. In the United States, the three most prominent tax acts – from the standpoint of how much they altered the policy status quo – have all

election, a pressing loophole or defect in tax laws, or rapid changes in macro-economic and/or fiscal conditions.

come during Republican presidencies.<sup>234</sup> These case level observations mesh with the macro findings of the previous chapter, i.e. that Right parties – in power – are the main partisan driver of large-scale income tax reforms.

The next issue is to decide which of the Right-led reform packages we should study – if we cannot study them all in detail. I let both a recently criterion, preferring newer reforms to older ones, and a size criterion, the reforms should substantial instead of minor policy changes, guide my reform choices. There are: the 2009 Danish tax reform, which contained the first reduction of the marginal tax rate since the introduction of the income tax in 1903; the 2017 US tax reform, which dwarfs the combined cuts of the 2001 and 2003 reforms; and the 2012 and the 2018 UK budgets, which introduced non-trivial top-end income cuts, albeit with different choices of reform instruments. The four are marked with red circles in **Figure 23**<sup>235</sup>.

#### 7.2 Strategy of analysis

How should we proceed with the analysis? It is, of course, very hard to find direct evidence to corroborate this story of a conditional Right politics as moderated by tax institutions, as the latter do not leave specific finger prints we can find as scholars. In each case, we cannot meaningfully observe what the Right's 'true' policy preferences were, independent of the contextual factors, and then follow how this institutional legacy affected them to pursue solutions that were ultimately not their first-choice but were expedient given the local rules of the game. Nor do we have direct access to what elite politicians were thinking and contemplating at the time of reform.<sup>236</sup> We can, however, observe

<sup>&</sup>lt;sup>234</sup> The larger tax acts under president Obamas – the 2010 Tax Relief Act and the American Taxpayer Relief Act of 2012 – were both prompted by the sunset provisions built into the Bush tax cuts of the early 2000s that were set to expire in 2010 (CNN 2010, The-National-Law-Review 2013). In the first act, Obama compromised with Congress Republicans to extend the tax cuts for an additional two years; in the second one, he agreed to make the tax cuts permanent for approximately 98 percent of taxpayers as a means to postpone the planned budget sequestration provisions (ibid.).

<sup>&</sup>lt;sup>235</sup> Of course, I will reference the other reforms in my case walkthrough when they carry direct political relevance for the reform under investigation.

<sup>&</sup>lt;sup>236</sup> One possibility to tap into politicians' mindsets is, of course, simply to ask them about their policy preferences, causal beliefs and strategic considerations. However, strategy is an issue that most political actors prefer to talk about behind closed doors. Interviews as a means of generating information may thus be problematic for multiple reasons. First, in terms of getting access to high-level political decision makers. Second, even if access is possible, it can be tough to differentiate between storytelling

the policymakers' specific actions and spoken words at the time and judge whether these actions and words generally match the expectations to the Right strategy for each corner in the institutional configuration. It requires, still, some thoughts on operationalization; what should we specifically look *for* along the two institutional dimensions.

At the core of the bracket dimension is the distinction between thresholds and rates, or really the distinction of Right politicians being limited to reforming threshold limits only in the low B setting, or having more policy choice between the different types of instruments in the high B one. As a minimum, the case studies must uncover the specific instrument choice and mix used in each reform package to gauge whether they broadly align with theory. Equally important, the studies must trace the origin of the policy solutions to disclose which agent was truly responsible for proposing and drafting these measures. Can we, for example, say with certainty that the reform was the result of the Right's political efforts, or should the responsibility be attributed to other agents? A related issue is, of course, to what degree the policymakers of the Right generally attempt to create distance between themselves and certain policy instruments – or blur this relationship – or whether they dare to claim credit for specific ones, e.g. lower marginal tax rates.

The second dimension related to progressivity concerns the distribution of tax cuts, or more generally the distribution of benefits and costs across the income scale. What we need to observe to confirm our theoretical expectations is not necessarily that the Right pursues an equal distribution of cuts for all (in absolute terms) in the low P case. Less will also do. Instead, we are looking for whether the Right's efforts are (almost) exclusively intended to benefit higher incomes or devote close-to-equal attention and efforts to below-average incomes too. It extends to how they construct their reform packages, obviously, but certainly also to the focus in their broader tax rhetoric, and how they attempt to sell their specific policies.

Trying to 'prove' such tax strategies and then attribute them to these institutional dimensions is a difficult endeavor given the many political, economic, and institutional contextual factors in the individual cases that may provide alternative explanations for the policy output and partisan rhetoric. This is a fair point of criticism, but I can push back a little. We must acknowledge first – which seems as an obvious realization – that the results of a political process can easily have more than one cause. In fact, the responsible thing as a social scientist is to assume that something like the content of a political reform package has multiple causes. It does not leave us with a blank check to dispel

<sup>(</sup>and *ex post* justifications of a certain decisions as 'strategies') and facts. Third, it requires that politicians have an exceptional memory of events and details.

all the potentially confounding factors that are better explanations of what we witness than the theoretical framework provided in this dissertation. The right thing to do – in my view – is to treat such case idiosyncrasies with openness; to shed light on them and discuss whether it strongly detracts from the theoretical claim I try to make.

So where should we look to form a systematic account of the cases in question. Overall, I turned to three main empirical sources to piece together the full timeline of what happened, and why. The first involved digging through the relevant legislative data. I focused, in particular, on the government's reform proposal and the finalized reform bill in order to document (1) the Right's initial reform bid and (2) what was politically feasible enough to make it through the political process.<sup>237</sup> To get a sense of the surrounding partisan conflict, I combed through the budget speeches in the respective parliaments, including the opposition speeches. Having nailed the legislative details, I then conducted an extensive review of mainstream media coverage.<sup>238</sup> The 'key word' search included articles published up to one full year before the adoption of the respective reforms and until one month after to ensure that it painted a full picture of vital events prior to reform, such as partisan statements on reform preferences, the origin of policy solutions, as well as postreform reactions. **Table 7** reveals the specific parameters of the article search, including the search term and the number of article hits. To ensure consistency in the way the article materials were treated, I logged political actions and statements related to five main categories: (1) the government, e.g. tax rhetoric, change in legislative strategy, or a revelation of policy content; (2) the opposition, e.g. political criticism or blame directed at the government; (3) displays of public opinion or opinion polls, e.g. indications that taxpayers are for or against the proposed reform or certain elements of it; (4) interest groups, e.g. which key organized interests support or reject the reform; and (5) a category for circumstantial evidence, e.g. other key events affected the reform process. Putting these on a timeline provided a clear picture of key ac-

<sup>&</sup>lt;sup>237</sup> The British case is again peculiar in this respect, as the government – due to its parliamentary majority – presents just one Finance Act that is written into law without many alterations.

<sup>&</sup>lt;sup>238</sup> In the Danish case, I relied on articles in two major news outlets, Politiken and Jyllands Posten. As they comment on current events from a Center-Left and Center-Right point of departure, respectively, it ensures a more balanced news coverage than if I relied on either one individually. For the United States, I relied on articles in USA Today, a moderate account that ranks first in circulation among all US news-paper. For the UK, I chose the Guardian and the Telegraph to cover both 'sides'.

tors involved in the reform package and their roles. Finally, to fortify the partisan angle, I studied the manifestoes of the respective Right cabinet parties to get a sense of their long-standing profiles in the income tax questions as well as insights into specific, pre-election pledges made in this domain.

Reform	DK-2009	US-2017	UK-2012	UK-2018
Reform date	May 28 2009	December 22 2017	March 21 2012	October 29 2018
Search period	May 28 2008– June 28 2008	December 22 2016– January 22 2018	July 1 2011– June 30 2012	January 1 2018– December 31 2018
Media outlets	Politiken and Jyllands Posten	USA Today	The Guardian and The Telegraph	The Guardian and The Telegraph
Article data- base	Infomedia	Factiva	Factiva	Factiva
Search term	"skattereform"	"tax reform"	"income tax" AND "budget"	"income tax" AND "budget"
Article hits	431	399	1,390	551

Table 7 Overview of the article search strategy for the individual case studies

**Notes:** The Danish search focused on a subset of medium-sized articles (from 125 to 700 words) due to a mere choice of constriction. These medium length articles seemed to strike the right balance by excluding very short article notes (less than 125 words), often not providing much background to the particular news story, as well as not engaging with those very long feature articles (more than 700 words), often too inclusive for this analytical purpose. The US and UK searches involved all articles under the search terms.

Using these sources, I will try to a give relatively detailed account of the background for reform, the political process as it played out, as well as a discussion of the reform content.

#### 7.3 Denmark

Denmark has been renowned for its high revenue levels, especially when it comes to income taxation (Ganghof 2006b, 2007). However, the policy structure is not overly progressive, as we have seen, as both low-income and high-income groups face high marginal tax rates.<sup>239</sup> Heading into the new millennium, the central Danish income tax system was a three-tier system; a bottom tax at 5.26% then a middle tax of another 6% (starting at a taxable income of 164,300 kr.), and an additional 15% top tax (starting at 267,600 kr.). The two

<sup>&</sup>lt;sup>239</sup> According to the OECD, the total tax wedge, i.e. the combined marginal tax rate of the personal income tax and social security contributions, was 49.6% for someone earning 67 percent of average wages and 62.1% for someone earning 167 percent of this reference in 2000.
higher tax brackets included 45 percent and 19 percent of all Danish taxpayers, respectively, in 2000 (Skatteministeriet 2018).

# 7.3.1 Background of reform

The minority Right cabinet, consisting of the Liberals and the Conservatives and headed by PM Anders Fogh Rasmussen, entered office in 2001, relying on stable parliamentary support from the populist Danish People's Party to form a majority. The Liberals, in particular, had toned down its former pursuit of income tax cuts at this point and now ran on a 'tax stop' pledge of not raising existing tax rates and freezing tax figures at their current levels (Venstre 2001, 2005). Though the Liberals were hesitant to campaign on the promise of lower taxes, the cabinet still delivered tax reforms (in 2003 and in 2007) that cut income taxation in its first two terms in government. Their fiscal impact was relatively modest, as they cut revenue by 9.6 billion and 3.9 billion kr. once fully implemented.<sup>240</sup> Their main policy intervention was two-pronged: introduce a new 'work allowance' for wage earners capped at 4.25% (but with a max of 13,100 kr.) designed to increase work incentives at the bottom of the income scale, and raise the middle tax threshold continuously each year to correspond to the top tax threshold (347,000 kr.) as of 2009 (Skatteministeriet 2019). Though the middle tax was still referred to as a tax of its own, these changes effectively converted the tax schedule into a two-tier system, as the thresholds for the two higher brackets were now similar.

Nonetheless, rightist observers remained disappointed with the lack of changes to the steep marginal tax rates in general and the top tax in particular. Yet, it was clear that the cabinet leadership did not consider the latter a feasible policy option. For example, PM Fogh Rasmussen, a known pragmatist, established in a famous 2005 interview that the most pressing need was to cut taxes for low-income groups due to the potential efficiency gains, also because of voter-strategic considerations (Børsen 2005). He was quoted as saying:

a clear message to those who always call for lowering taxation on the highest incomes: it is absolutely impossible to get public support for a tax-cutting policy if the impression arises that it is the goal to reduce taxes on a few wealthy incomes, and if the impression is that it is financed by cutting welfare services for those groups that do not have a lot of money. I need to say it loud and clear that is the situation. You have to acknowledge that painful political reality (own translation).

The transcript is as close to a smoking gun as one can imagine to substantiate a claim that the leadership of the Liberals went to great lengths to pursue a tax

<sup>&</sup>lt;sup>240</sup> The two reforms cut taxes corresponding to 0.7% and 0.2% of GDP.

policy that would not alienate the large group of voters at the political center. Despite frequent rumblings between the cabinet parties, Fogh Rasmussen kept clamping down on Conservative calls to reduce the top tax (DR 2004).

The cabinet secured its third term after the 2007 parliamentary election, yet still a minority government. The tax issue featured prominently in the runup campaign due to the recent tax reform, with the Liberals pledging to continue the 'tax stop' at least until 2015. Neither Right party campaigned on a commitment to new reform. However, when the cabinet released its official working program after the reformation of government (VK-Regeringen 2007), it pledged a major overhaul of the income tax system with the main goal to stimulate work and initiative by 'significantly' cutting taxes on work income.<sup>241</sup> The cabinet wished to form a Tax Commission whose task was to sketch designs for a complete reform proposal that met these criteria. On paper, they seemed to follow to same playbook as they had used for their major welfare and pension reform adopted in 2006, where a similar type of commission provided the expert blueprints for the following political negotiations. This new Tax Commission was established in early 2008 and was headed by former Minister of Taxation, Social Democrat Carsten Koch, with a February 1 2009 deadline for recommendations.

#### 7.3.2 The political process

From then, the discussion of tax reform subsided for a while. **Figure 24** displays the timing of the 431 articles covered in the Danish reform case, broken down according to week of publication, to illustrate how this debate featured on the media agenda. If nothing else, it provides a solid indication as to when the political discussions began to materialize.

During the summer of 2008, with the looming Financial Crisis still absent from the Danish political debate, the more pressing economic issue was how to combat the labor shortage. Unemployment rates had been below 3 percent in the first six months of 2008, causing concerns of rising inflation. In early July, Liberal spokesperson on taxation, Peter Christiansen, declared that he was willing to lower the top tax as a means to provide 'additional hands', yet failing to specify how to achieve this (Jyllands-Posten 2008d). The Conservative coalition partner welcomed this change in rhetoric, as they had been the lone advocate of this view for years. The mere fact that the Liberal leadership did not openly refute this statement marked a watershed moment, as they

<sup>&</sup>lt;sup>241</sup> The reform had multiple stated (and likely conflicting) intentions, among other things underscore the cabinet's climate ambitions, serve as 'distributively balanced' and fiscally sound, and continue the 'tax stop'.

were accustomed to discipline backbenchers arguing for tax cuts at the top end.



**Figure 24** Article count on 'tax reforms' – 2009 DK reform. Week 23 2008 through weak 26 2009

Source: Own calculations based on Infomedia.

**Notes:** N = 431. The search period ran from 28 May 2008 (1 year before the reform) to 28 June 2009 (1 month after the reform). The article count feature medium-size articles (from 125 to 700 words) in two Danish two news outlets, Politiken and Jyllands Posten.

By the fall of 2008, and with the onset of the global Financial Crisis, the media began to turn its attention to the Right cabinet's inability to handle the now slumping economy. What had been one of its major assets in year's past – the ability to secure stability and only moderate political change – now turned into weakness, as critics began to notice its inability to commit to radical reform when needed. Especially regarding another chief structural problem in the Danish economy: the forecast of low long-term growth rates. Further, negotiations over the government's planned – and much publicized – labor market reform crashed in early November, and Finance Minister Lars Løkke Rasmussen managed only to negotiate a 'status quo' budget for 2009 with the Danish People's Party, which did not attack these problems head on. The future tax reform was therefore seen by observers as key to solving the pressing economic issues.

The political discussions picked up steam from the start of the new parliamentary year in October (see **Figure 24**) while the Tax Commission was still working on its draft. The Conservatives were first to get specific about their goals as their spokesperson, Mike Legarth, wished to cut the top tax rate by 13 percentage points, capping it at 50% in 2010 (Jyllands-Posten 2008b). Peter Christiansen of the Liberals openly supported the idea of cuts but emphasized political realism and was still hesitant to commit to specific rate levels. Yet, the Liberal Minister of Taxation, Kristian Jensen, doubled down on November 16 and promised 'massive' tax cuts when negotiations over a new tax reform commenced (Jyllands-Posten 2008a). He indicated cautiously that their scope would be larger than the two prior reforms, more than 10 billion kr. in cuts. Jensen was flanked by Finance Minister Lars Løkke Rasmussen, who pledged 'significant' tax cuts to the about 1 million Danes paying top tax (Politiken 2008) but was not specific about which tax instruments should be tuned to achieve this goal. Observers noted that the announcement broke a longstanding taboo in the Liberal Party. The Danish People's Party expressed their intention to negotiate a future tax reform but rejected cuts to the top tax at the expense of low-income groups and generally wished to scale down the size of the cuts, as they did not see the need for a large-scale reform.

Hence, the Right had plenty of broad intentions early on about what a reform should do. A perfect storm of economic pressures seemed to generate fertile grounds for contemplating significant tax reform. However, what strikes a scholarly reader is that these lofty ambitions contained remarkably few concrete political signals on the content of reform. The cabinet parties were eager to play the waiting game regarding the Tax Commission's recommendations, and the Right elites seemed content to hand over policy development to these non-partisan experts. Some hints on what we can deem as the wider parameters of a potential reform did emerge, however, in late 2008. On December 9, Finance Minister Løkke Rasmussen publicly broke with the previous notion of a fully financed reform – one that aimed not to worsen the budget balance - and argued for the reform to be 'underfinanced' in the first years to boost economic growth (Jyllands-Posten 2008c). This was echoed by the Conservative leader, Lene Espersen, who wanted the tax reform to 'kickstart' the Danish economy. In early January, PM Fogh Rasmussen, who had been noticeably absent from the entire reform discussion to this point, wanted to tie the tax reform to a joint 'growth package' that included public investments in addition to tax cuts. On February 24 2009, shortly before the reform negotiations began, he elaborated on his demands to potential legislative partners. The Right cabinet expected them to (1) pledge to the tax stop (after the reform), (2) accept that the reform had to be underfinanced in its first years, and (3) negotiate and settle on the reform's content within a matter of days, once the government had put forward their reform bid (DR 2009). Swallowing all three seemed to write off the possibility of compromising with the left-wing opposition from the outset.

### 7.3.3 The content of reform

As seen in **Figure 24**, the media coverage spiked dramatically around the release of the Tax Commission's report on February 1 2009. The Commission's proposal intended to lower income taxes at an estimated 35 billion kr. (Skattekommissionen 2009), which were sizable cuts equaling 2 percent of GDP.

The tax-cutting elements of the report were detailed and sought to cut taxes at all income levels. At the top, the key cuts were the abolishment of the middle tax of 6%, a 1.5 percentage point lowering of the top tax rate (from 15% to 13.5%), and an increase of the top tax threshold by 36,000 kr. Further, the Commission proposed to lower the maximum tax ceiling to 50%.<sup>242</sup> At the bottom of the scale, there were measures to lower the bottom tax by 1.5 percentage points and raise the employment allowance to 7% (max. 22,300 kr.). The top cuts were estimated to cost 12 billion kr. to finance, while the cuts at the bottom were estimated at 20 billion kr. Finally, the Tax Commission proposed to 'spend' 3 billion kr. by raising the personal allowance by 1,000 kr. for all taxpayers and by introducing a new 'green check', essentially a compensation allowance to offset the impact of new environmental excises (ibid.).

**Table 8** provides an overview of the proposed changes to income tax rules from the Commission split according to instrument type. The third column shows the policy baselines at the time of the report release. The grouping of the measures into the binary rate versus threshold distinction is, of course, less clear-cut for the two cases where the instrument in question is either introduced as a new tax rule (the green check) or removed altogether (the middle tax), and they are put into a separate category. Creating the new allowance is a an obvious 'base' measure, as it detracts what is counted as taxable income, and it aligns, in my estimation, closer to the threshold camp than the opposite. The middle tax abolishment, in turn, involves a removal of the whole bracket that is defined by the rate as well as the threshold and must be considered something separate of the hard either-or proposition. In any event, it is evident that the Commission's policy mix features a blend of cuts to both rates and thresholds, and a conscious focus on the balanced distribution of gains.<sup>243</sup>

<sup>&</sup>lt;sup>242</sup> The "tax ceiling" thus defines the upper limit on a taxpayer's marginal tax rate, once local taxes and all central government taxes are added together.

<sup>&</sup>lt;sup>243</sup> The Commission recognized that their reform bid entailed the largest absolute tax cuts in absolute terms to the richest decile, but underline that their relative gains are in line with what the lower income deciles get. The relative distribution of income taxes would thus be the same in the before and after scenarios (Skattekommissionen 2009: 22).

Instruments	Recommendations from Tax Commission	Policy baseline	Cabinet proposal	Final reform bill
Income tax				
Thresholds	Raise top tax threshold by 36.000 kr.	347.200 kr.	>	÷ , 54.400 kr. (im. 2011)
	Raise employment allowance to 7 percent (max 22.300 kr.)	4 percent	>	÷ , 5.6 percent (im. 2019)
	Raise personal allowance by 1.000 kr.	42.900 kr.	>	÷, dropped
Rates	Top tax rate lowered by 1½ pp	15 percent	>	÷, dropped
	Tax ceiling lowered to 50 percent	59 percent	$\div$ , 51 percent	÷ , 51.5 percent
	Bottom tax rate lowered by 1½ pp	5.26 percent	÷ , 0.5 pp	`
Introduction /	Abolishment of the middle tax (6 pct.)*		>	>
abolishment	New 'Green check' (allowance) of 700 kr.		>	÷ , 1.300 kr.
Total costs	35 billion kr.		30 billion kr.	29 billion kr.
<b>Source:</b> Skattekomr <b>Notes:</b> 'pp' is an abb	aissionen (2009); Regeringen (2009b, a) reviation for percentage points. 'im' stands for implemented.			

**Table 8** Proposed changes to income taxation rules in connection to the 2009 tax reform

The financing side of the Commission's bid included green excises and a reduction of corporate grants as well as existing tax deductions. In total, 23 individual tax and spending measures. The initiative that attracted most attention was the proposal to lower the so-called interest allowance from 33% to 25% over multiple years. The intent of this allowance is to reduce tax payments of homeowners in particular, as it reduces the tax liability with an amount corresponding to the rate, defined by the tax, of the taxpayer's interest payments. The measure challenged the Liberals, especially, as they had for years championed the notion of protecting homeowners against rising taxes. Further, PM Fogh Rasmussen was attacked for potentially breaking a specific pledge made in letters to 400,000 Danish homeowners during the 2007 election campaign where he promised 'no tax surprises' during his premiership and warned that the Social Democrats in office might raise property taxes (Jyllands-Posten 2009b).

The Right coalition moved swiftly from the Commission report and presented their own reform bid, 'Spring Package 2.0', only three weeks later on February 24.244 The main outlines of the reform package were more or less copied from the Tax Commission. As Table 8 demonstrates, all measures to cut income taxes were copied one-to-one, with the slight exception that the government proposed to lower the bottom tax rate by 0.5% instead of 1.5%, which meant that the tax ceiling would reach 51% rather than 50% (the existing level was 59%). The cabinet thus opted away from the full, but revenuecostly, cuts at the bottom of the income scale. The move reduced the total estimated costs of the package to 30 billion kr. in lost revenue, 5 billion kr. less than the Commission's estimate. Further, many finance elements were dropped entirely from the cabinet's proposal, which was underfinanced by 12.7 billion kr. in the first year of the reform (2010) and by 1.3 billion kr. in its last year (2015). This meant that the government conveniently dodged many of the compensatory tax hikes for which the Commission faced criticism. Most prominently, the government diluted the negative impact on homeowners, as their proposal only affected a small minority of taxpayers with interest payments exceeding 50,000 kr. a year with a gradual phase-in from 2012.<sup>245</sup> The reform bid was received with pronounced skepticism by the left-wing opposition as well as the Danish People's Party. Their deputy leader and negotiator, Kristian Thulesen-Dahl, criticized 'the social profile' of the cabinet proposal as more unfavorable to pensioners than the Commission's original bid and

<sup>&</sup>lt;sup>244</sup> The first Spring Package refers to a 2004 parliamentary decision to implement the Right cabinet's first tax reform from 2003 faster than originally intended.
<sup>245</sup> Effectively postposing these costs from commencing until the next election cycle.

called, specifically, for the planned cut to the top tax rate to be dropped (Politiken 2009b).

In the following days, Finance Minister Løkke Rasmussen began fast pace negotiations with all opposition parties as warned. The swift pace was attributed to PM Fogh Rasmussen's desire to land the reform as quickly as possible to evade further talks of broken pledges.<sup>246</sup> In any case, Løkke Rasmussen excluded the left-wing and centrist parties from the negotiations in less than 24 hours, which left the Danish People's Party as the only and obvious coalition partner. The political spokesperson of the Social Democrats, Henrik Sass Larsen, criticized the process as 'pre-choreographed' and called the reform content 'skewed', backed by an opinion poll stating that 65 percent of Danes did not think they would benefit financially from the reform (Jyllands-Posten 2009a). On March 1, the cabinet and the Danish People's Party settled on a final reform version.

Though the structure of the reform remained intact,<sup>247</sup> many individual reform elements were fine-tuned once the parties engaged in negotiations. Of the eight proposed income tax cuts (see **Table 8**), only one instrument remained unchanged from the proposal phase: the decision to abolish the middle tax. What garnered the most media scrutiny was, without a doubt, the U-turn on the top tax rate. The narrative was that the Danish People's Party coerced the government to drop them from the package entirely, a clear political victory for the support party (Politiken 2009a) to the detriment of the large business associations. The top tax rate thus stayed at 15 percent. The parties chose to beef up the cuts to thresholds instead. As compensation for shielding the rate, they agreed to raise the top tax threshold to 54,400 kr. over two years (instead of the proposed 36,000 kr.). This would take an estimated 350,000 taxpayers out of the top bracket and cut their marginal tax rate with 22.5 percentage points (Regeringen 2009a: 10).<sup>248</sup>

<sup>&</sup>lt;sup>246</sup> Fogh Rasmussen seemed also to have different priorities on his mind at this time, as he was frequently mentioned as a candidate for NATO General Secretary later that spring.

<sup>&</sup>lt;sup>247</sup> The proposed cuts amounted to an estimated 29 billion kr., 1 billion kr. less than the government's bid. If Danish People's Party wanted to scale down the reform as much as possible, we would be hard pressed to say that they managed much.

<sup>&</sup>lt;sup>248</sup> A well-hidden fact in the package was that the legislative partners gave the top tax threshold a sizable (one-shot) spike and simultaneously chose to suspend the standard automatic adjustment for all thresholds in the personal tax code, including the top tax threshold, for the fiscal year 2010. So the real jump in that particular parameter was much lower than the announced one. This move escaped most observers but was thought to be bring in an extra 5 billion kr. in revenue each year (Berlingske 2009).

To a scholarly observer, the political semantics of instrument choice is striking. The urgency of the Danish People's Party to take the rate cuts off the table is illuming to the type of reform case we are discussing; the low B case where cuts at the top end are expected to be politically contentious. The case proves these specific rate cuts are third-rail in the Danish context. On the surface, the final reform package looked like a victory for those adverse to inequality, given that the cuts were concentrated on the earned income around the existing threshold rather than on income at the (far) right end of the tail. Yet, what seemed missing from this entire discussion was any focus on the middle tax abolishment. Since this tax as of 2009 shared the same bracket limit as with the top tax, the former was effectively just a sub component of the latter. Consequently, the much talk about the 1.5% cut, which was dropped, and the absence of talk about the 6% cut, which was upheld without further notice, cannot be understood properly if we do not account for the differences in their perceived feasibility. The middle tax targets, almost by definition, 'middle incomes', and lowering taxes on so-called middle incomes over the top ones proved a much easier sell politically, even though the policy impact may be the same. Hence, the finalized reform still made sure that the marginal tax rate for the highest incomes was cut by 7.5 percentage points – as is evident from the cut in the tax ceiling (see **Table 8**) – without having to touch the symbolically important top tax rate. Put into perspective, it is an astounding one-time cut.

We notice two additional stories in this regard. The first is the cabinet's obvious hesitation to draft and propose the specific framework for reform. The Right parties chose an initial strategy of commenting only on the overall direction of reform and its broader parameters, shelving any discussion on solutions until the Tax Commission's were known. This display was not exactly an offensive political tactic. However, placing themselves in the slipstream of these expert inputs – where they were the ones designing the principle guidelines for what should be proposed – likely provided the political shield the Right parties needed. If we consider the counterfactual – the absence of the Tax Commission – I have a hard time imagining the cabinet propose something close to those marginal rate cuts at the top-end that ended up in their bid. The congruence between the Commission's and the cabinet's proposal seems to substantiate this view.

Second comes a discussion of what truly caused the cabinet to change their policy mix regarding the top tax, since it has implications for how we should look at the role of the Right in an institutional setting mimicking the Danish. One is tempted to point to the unsuccessful attempt to cut the top tax rate as a restraint stemming from another partisan veto player – i.e. Danish People's Party – and not something deriving from the Right parties' own strategies.

Should we not have seen the Right cabinet succeed in enacting these particular cuts had they had a parliamentary majority to do so? It is a likely explanation, but it builds on the premise that we can reasonably trust that the cabinet's reform bid revealed their actual policy preferences on the top tax and was not predominantly based on strategy. This is where things become a bit speculative. But given the political prelude to reform, the Right government knew very well that the Danish People's Party would have a tough time swallowing any cuts to the top tax, and in particular the 1.5% rate cut. Including it provided the cabinet with a symbolic key measure that the legislative partner would have to use their political capital to eliminate, and that could be 'traded' for the further cuts in the threshold column, as described. We cannot truly settle this question, but the cabinet's noticeable resistance to taking this exact policy route in their prior tax reforms may lend some credence to this strategy argument. Further, they have not been successful in lowering the top marginal tax rate since and have never campaigned openly on this question.<sup>249</sup>

The final negotiated reform did little to change the distributive impact of the earlier bid, as the general tax cuts still accounted for more than half of the revenue costs (Regeringen 2009a). Slight alterations were made, as per Table 8. The 1.5% cut of the bottom tax rate re-emerged in the package along with a more generous version of the green check (1,300 kr.),<sup>250</sup> while the planned cuts to the personal allowance and the employment allowance were scrapped and dialed down, respectively. Nevertheless, the left-wing opposition persistently tried to press the government on what they saw as the reform's dire distributive consequences, often highlighting the vast differences in the size of the tax cuts; the 'typical' CEO would receive an immediate yearly cut of 49,224 kr., while the home helper would face a net gain of only 1,182 kr. (Jyllands-Posten 2009a).<sup>251</sup> It led critics to refer to it, condescendingly, as the 'red wine reform'. The Right parties maintained that the reform left the Danish income tax code with a distributive fairness intact, as it did not significantly alter the relative distribution of income tax burdens; the richest decile would still pay 10.7 times more taxes than the poorest decile (11.0 before the reform). The

<sup>&</sup>lt;sup>249</sup> By removing the middle tax bracket and turning the tax system into a two-tier one, the policymakers deprived themselves of these policy instruments to be used in future (tax-cutting) reforms.

<sup>&</sup>lt;sup>250</sup> This check was gradually phased out for incomes above 360,000 kr., essentially targeting low and middle incomes.

<sup>&</sup>lt;sup>251</sup> Curiously, all types of calculations of the reform's impact on the post-tax income distribution were left out of the final reform agreement that was presented to the public, although they featured in the earlier bids.

numbers used by both sides were, of course, correct. However, the cabinet appeared mostly on defense in subsequent debates and had troubles selling the reform as a 'balanced act' that benefited the many rather than the few. This focus on the redistributive consequences crowded out much of the discussion about the positive effects the reform would have on the (at that time) slumping Danish economy,

# 7.3.4 Summary

The Danish case shows how the Right devises a rather balanced effort to cut income taxes at both ends of the spectrum, and it demonstrates the sensitive politics of the top marginal tax rate. It was an issue that leading policymakers on the Right had been noticeably cautious to discuss since landing political power in 2001, and it took them until their third term in government seriously to combat it. Even then, the government never launched a 'head-on' political assault on the high marginal taxes, as they leaned heavily on the politically neutral experts of the Commission for political cover. Nevertheless, the cabinet employed a clever 'one-time' circumvention to cut the top marginal tax rate on income, using the opportunity to abolish the middle tax bracket, which was de facto the top bracket at that point. Yet, as the case clearly shows, the Right parties had to shelve any ambitions of touching the symbolically important top tax rate in order to land its reform. Here, altering the threshold limit proved the politically feasible alternative.

# 7.4 United States

The top marginal tax rate on income was retained at 39.6% – the level of the Clinton era – when the rate reduction of the Bush tax cuts expired after 2012. Afterwards, the US income tax schedule was a seven-tier system with starting rate of 10%. The structure is in the high end on progressivity comparatively speaking, thanks to the impact of the refundable credits for lower-income households, such as the Earned Income Tax Credit, the standard deduction, and the graduate rate structure. Generally, tax expenditure plays an enormous role in the US system, amounting to \$1.3 trillion in 2019 – more than the combined costs of Medicare and Medicaid (CBPP 2020). The values of these tax breaks tend to be sharply tilted towards the highest income households (Faricy 2016).

# 7.4.1 Background of reform

Republican presidential candidate, Donald Trump, released his official tax plan, 'Tax Reform That Will Make American Great Again' on September 14 2015, during the campaign. According to the Trump camp, the plan was founded on four main goals: (1) to provide tax relief for middle class and increase their post-tax incomes; (2) to simplify the tax code; (3) to boost economic growth, job creation, and competitiveness; (4) to avoid increasing the debt and the public deficit.

The main component of the Trump plan was to replace the current seven tax brackets with three, with rates on ordinary income of 12% (upper limit: \$37,500 for single filers), 25% (\$112,500) and 33%, while increasing the standard deduction from \$6,300 to \$15,000 (Tax-Foundation 2016a). The structure clearly resembled then House Speaker Paul Ryan's tax plan released in June 2016 that featured identical rates (Tax-Foundation 2016c). Further, the plan was a revision to Trump's first tax plan from 2015, which would have slashed the top income tax rate to 25 percent, but cost an estimated \$12 trillion in lost revenue over the next decade. This new plan dialed back much of these costs, yet was still estimated to reduce federal revenues between \$4.4 and \$5.9 trillion before factoring in any positive feedback effects. The Republican and Democratic tax positions thus differed sharply, as Hillary Clinton pledged to raise taxes on the top 1 percent earners, and key measures in her plan included a new 4 percent 'surcharge' on taxpayers above \$5 million and enacting the "Buffet rule", which would establish a 30% minimum tax on incomes above \$1 million that would be shielded from all exemptions (Tax-Foundation 2016b).

### 7.4.2 The political process

After Trump's surprise election victory, and with the Republicans carrying both the House and the Senate, the push for tax reform was considered a centerpiece in the party's legislative program together with the repeal of Obamacare for the coming session. Political observers expected them to move quickly on this question, and on February 24 Treasury Secretary Steven Mnuchin said the Trump administration aimed to pass 'significant' tax reform by August that year (USA-Today 2017c). Tax reform, he stated, was integral to achieving the administration's goal of at least 3 percent economic growth over the coming years; a growth target that was repeated throughout the reform process. On February 28, Trump repeated his commitment in his first address to Congress, promising "historic" tax reform that would provide massive tax relief for the middle class (USA-Today 2017g).

As evident from **Figure 25**, the media coverage picked up traction early on, especially around the congressional address, before starting to fade out in March and early April. During this time, Republicans concentrated the bulk of their reform efforts to repeal Obamacare but ultimately failed. Reports on April 10 indicated that the administration had begun work on their tax reform bid, but questions already began to emerge on the realism of the earlier August timeline. As the 100<sup>th</sup> day in office stared the president metaphorically in the face, the Trump administration finally pushed out a tax reform plan on 25 April that in large part mimicked Trump's campaign pledge but otherwise contained few details and no overall cost estimate. It fit on a single sheet of paper, and aides stressed that most of the plan was flexible – a starting point for negotiation. The plan intended to alter the income code in the following way:

- (1) reduce the seven tax brackets to three brackets of 10, 25, and 35 percent
- (2) double the standard deduction
- (3) tax relief for families with children and dependent care expenses
- (4) trim targeted tax breaks used by the wealthiest taxpayers
- (5) keep deductions for mortgage interest payments and charitable giving
- (6) repeal the alternative minimum  $\tan^{252}$
- (7) repeal the 'death tax'

Many reactions initially centered on the proposed rate structure, as there was, curiously, no mention from the political leaders presenting the plan or from media observers covering it of *when* such tax rates should set in. Hence, the threshold component of the legislative puzzle was kept in the dark. Otherwise, it was the plan's finance elements, or the lack thereof, that caught the main attention of the press. Besides eliminating certain unspecified deductions, it was vague on how it would pay for the lower corporate and personal tax rates, which led to speculations that the great bulk of the cuts would presumably be financed through borrowing.

Going into the summer, the failed bid to abolish Obamacare had clogged any momentum of getting tax reform rolling. Generally, the failure of the GOP majority to walk in line and get things done on the legislative agenda was criticized frequently, and tax reform was more often mentioned as the key issue that could unite the party and give it a needed legislative win. The Republican congress, however, was still waiting for a more comprehensive bid from the administration, and Speaker Ryan, though underlining the need for reform, expressed uncertainty of its chances of being worked out within that calendar year (USA-Today 2017i). Leading House Republicans had already voiced their desire to use the reconciliation rule to avoid a Democratic filibuster, once a

<sup>&</sup>lt;sup>252</sup> This tax as a device intended to curb tax avoidance among high-income earners by defining a broader tax base of regular income but also adding on disallowed items and credits such as stock options, foreign tax credits, home equity loan interest deductions, and so on. It broadens the base of taxable items.

reform proposal would be put to the House floor. Since it is a budget tool, it could not start until Trump would submit a full budget request to Congress for the new fiscal year beginning in October.





Source: Own calculations based on Factiva.

**Notes:** N = 399. The search period ran from 22 December 2017 (1 year before the reform) to 22 January 2009 (1 month after the reform). The article count feature all articles published in USA Today.

On August 29, President Trump kicked off the new political season with a tax address to a crowd of factory workers in Missouri, trying to breathe new life into the reform efforts. He reveled once more only broad bullet points for his agenda: simplification of the tax schedule, middle class relief, and slashing the corporate tax rate (USA-Today 2017j). New details would first emerge in a late September speech in Indianapolis, now outlining a proposal of a new 15 percent starting rate, along with a 25 and a 35 percent bracket – still without any hints of the income thresholds defining the new tax brackets (USA-Today 2017d). Trump persistently stated that the reform would not benefit the wealthiest, pointing to the lower personal tax rates and the proposed increase in child tax credits as measures that would mainly benefit the middle class. Yet, numerous sources, including the non-partisan Tax Policy Center, insisted that high-income households would benefit the most, since the plan, in addition to the lower top marginal tax rate, scrapped tax provisions that only affect the wealthy taxpayers: the AMT and the estate tax (USA-Today 2017h). At this point, the president expressed willingness to engage with the Democratic swing-voters in Congress after failing to repeal Obamacare with only Republican votes. Without dismissing the idea of working with Trump on tax reform,

leading Democrats blasted the initial reform bid due to its adverse effects on post-tax inequality.

Negotiations on tax reform finally picked up intensity in late October, accompanied by a spike in media coverage (see **Figure 25**). On October 26, Congress narrowly approved a Republican budget plan, using reconciliation language, that would allow tax changes to add as much as \$1.5 trillion to the long-term national debt. Media observers noted the paradox of the seemingly deficit-averse Republicans giving themselves fiscal leeway to add insult to injury. Yet, the legislative framework also capped the amount of revenue that could be cut. As earlier projections of the initial tax plan had shown ever higher debt numbers being added, president Trump and his Republicans needed to rein in some elements deliver a reform.

On November 2, the House Republicans released their initial tax plan that in large part stuck to the general outlines proposed by the President. With one clear change, as they suggested cutting the number of tax brackets to four with the following rate structure: 12, 25, 35, and 39.6 percent. The withholding of the 39.6 percent bracket – for single filers earning \$500,000 – was notable in light of Trump's repeated call to abolish it, but was seen as a tool to skew the cuts (a bit) more towards the middle class (USA-Today 2017e). The plan's other core elements featured cleaning up a cascade of individual-specific deductions but doubling the standard deduction, instead, as compensation. Further, the abolishment of the AMT and estate tax was still included in the House package. A few days later, the plan from Senate Republicans emerged, which kept all seven brackets in place but lowered the rate for most of them: 10, 12, 22.5, 25, 32.5, 35, and 38.5 percent<sup>253</sup> (Tax-Foundation 2017a). It was, thus, the first to address the possibility of retaining the current number of tax brackets. The Senate bill also featured two major additions, as it introduced sunset provisions to the personal tax cuts to expire after five years, and it targeted the Affordable Care Act as well by proposing to end the individual mandate.<sup>254</sup>

Over the course of November, the Republican leadership in Congress worked to round up support for the tax bill, aiming to prevent dissidence in Republican ranks rather than seeking bipartisan compromise. Meanwhile, the Congressional Budget Office (CBO) released a study breaking down the distributive profile of the Senate's plan, which was grim reading for those con-

 $<sup>^{253}</sup>$  Further, it suggested postponing the proposed corporate tax rate cuts – a centerpiece of the original Trump plan – by one year (to begin in 2019).

<sup>&</sup>lt;sup>254</sup> It is the provision that ensures tax penalties for individuals who do not obtain health insurance coverage. While the mandate would technically remain in place, the penalty falls to \$0 under the Senate's plan.

cerned about the unequal distribution of gains. The CBO estimated that everyone earning less than \$30,000 a year would experience a net loss from 2019 onwards due to the package, while everyone earning \$75,000 or less would lose by the time many of the reform measures expired in 2027. Conversely, people in every income group earning more than \$75,000 would pay less in taxes or receive bigger benefits such as credits over the coming decade. These conclusions matched a similar study conducted by the Joint Committee on Taxation released earlier in November (USA-Today 2017e).

The Senate Republicans passed a revised version of the tax bill on December 1 that stuck to the seven bracket rate structure (USA-Today 2017f). House Republicans remained most concerned about the sunsets to the individual tax cuts, now set to expire in 2025, the delayed reduction in corporate tax rates until 2019 and the plan to keep the estate tax intact, though at a \$10 million threshold. They settled on a joint agreement on December 13 (USA-Today 2017a). The bill was passed by the Senate (51 to 48) on December 20 with all Republican support and approved by the House later the same day (224 to 201) with 12 Republicans breaking party ranks.<sup>255</sup> The bill, "Tax Cuts and Jobs Act of 2017" (TJCA), was signed into law by President Trump two days later.

### 7.4.3 The content of reform

The size of the final package was immense<sup>256</sup>, but in line with the gist of the dissertation, I focus mainly on the reform's income tax components. Even here, it is hard to provide a crisp overview without getting lost in the details. Looking at the tax schedule first, the law keeps – as noted – the number of tax bracket intact: seven before the reform and seven after. Yet, the parameters changed considerably as shown in **Table 9**. The top rate fell from 39.6 percent to 37, the 33 percent bracket dropped to 32, the 28 percent bracket to 24, the 25 percent to 22, and the 15 percent to 12. The lowest 10 percent bracket and the 35 percent bracket remained unchanged. While it is easy to evaluate the direct effects of the rate cuts on tax liabilities, the effects of the threshold changes, which largely escaped political attention, are murkier. The upper limits on the previous 25, 28, and 33 percent brackets were all lowered, raising income taxes all things equal, yet most taxpayers would be pushed into a higher tax bracket, which due to the reduced rates was now taxed at a lower rate than the bracket they were originally placed in.

<sup>&</sup>lt;sup>255</sup> These were almost exclusively congressmen from high-taxing states like California, New Jersey, and New York, as taxpayers stood to gain less (or even lose) from the bill due to its new limit on deductions for state and local taxes up to \$10,000. <sup>256</sup> The full legislative changes took up a sizable 186 pages in total.

Under previous law			Under TCJA		
Rate	Income	bracket	Rate	Income	bracket
10 %	\$o	\$9,525	10 %	<b>\$</b> 0	\$9,525
15 %	\$9,526	\$38,700	12 %	\$9,526	\$38,700
25~%	\$38,701	\$93,700	22 %	\$38,701	\$82,500
28 %	\$93,701	\$195,450	24 %	\$82,501	\$157,500
33 %	\$195,451	\$424,950	32 %	\$157,501	\$200,000
35 %	\$424,951	\$426,700	35 %	\$200,001	\$500,000
39.6 %	\$426,701	and above	37~%	\$500,001	and above

**Table 9** Tax brackets in the Internal Revenue Code for single filers (2018)

Source: Public Law 115-97 115<sup>th</sup> Congress.

**Notes:** Brackets are for single filers, as separate brackets were per American custom designed for married filing jointly, for heads of households, and for married filling separate returns. The law also raised the standard deduction from \$6,350 to \$12,000 for single filers, yet at the same time suspended the personal exemption, which was \$4,135, through 2025.

The point becomes easier to see when the two schedules are plotted as in **Figure 26** The United States income tax schedule in 2017 and 2018. Even though the prior 28 and 33 percent brackets take effect earlier than in the pre-reform schedule, the marginal tax rates are still lower than before. Marginal rates were raised, however, for specific intervals of the schedule: from 28 to 32 percent for taxable income ranging from \$157,501 to \$195,450, and from 33 to 35 percent in the range from \$200,001 to \$424,950. Here, the black dashed post-reform schedule lies above the grey solid line for the pre-reform year.<sup>257</sup> It is important to bear in mind that the median US household income was \$61,822 in 2017, while the \$157,000 corresponded to about the 87<sup>th</sup> percentile or above,<sup>258</sup> affecting therefore only the very highest income groups. Further, the Republicans ended up raising the standard deduction from \$6,350 to \$12,000, effectively doubling the size of the de facto 'zero-rate' bracket.<sup>259</sup> Of course, this meant that the bracket thresholds were de facto adjusted accordingly and that taxpayers would pay less on the same income, all things equal.

<sup>&</sup>lt;sup>257</sup> Interestingly, such hikes in the marginal rate were almost avoided for the newly joint schedule for married filers in the way the specific threshold limits were determined. For this group, marginal rates were only raised on income ranging from \$400,001 to \$424,950 with a hike from 33 to 35 percent.

 $<sup>^{258}</sup>$  For single filers, the \$157,000 mark would therefore be in the even higher percentile.

 $<sup>^{259}</sup>$  At the same time, the personal exemption of \$4,050 in 2017 – which did have a phase-out for the richest taxpayers and hence an inequality-dampening effect – was scrapped.





**Notes:** The grey line represents the 2017 income tax schedule, while the dashed, black line is the 2018 schedule.

The sunset provisions to the personal income tax cuts, as originally proposed by the Senate Republicans, made it into the final reform bill. It meant that most of the personal tax measures would be only temporary until the end of 2025, as it would then reduce the cost of the changes over the 10-year budget window set by the reconciliations rules, as they would only be in effect for eight of the 10 years (Tax-Foundation 2017b). It also implied that the effective tax rates would rise on the poorest and middle-income groups, especially, once these reform provisions would fade. Another component, intriguing from a policy design standpoint, which escaped most observers, was that the law changed the measure of inflation used for indexing tax brackets going forward. With the TCJA, the consumer price index for all urban consumers (CPI-U) was replaced by the chain-weighted CPI-U as the indexation vardstick (ibid.). The latter takes account of changes in consumer spending habits as prices shift and is considered more rigorous than the standard CPI. It also tends to rise more slowly, so substituting it with the current formula is expected to accelerate bracket creep significantly over time. Curiously, this measure was not set to expire as the rest of the income tax measures, and at no point during the reform process was the change openly discussed.

When it came to the supplementary measures to affect the richest groups, the law ended up keeping both the AMT and estate tax in place, even though they were scrapped in the earliest reform sketches, but raised the threshold levels for each significantly. The TCJA – by raising the exemption line from

\$54,300 to \$70,300 (single filer) – reduced the fraction of taxpayers eligible for the AMT from 3 percent in 2017 to just 0.1 percent in 2018. Further, the estate tax remained at its current 40 percent but now applied only to estates exceeding \$11.2 million (\$5.2 million previously). The distribution of both of these cuts were, alas, heavily skewed towards the richest Americans.

The reform package would reduce federal revenues with an estimated \$1.47 trillion over its 10-year span, with the personal tax measures comprising the bulk of these cuts (ibid.). The adjustments of the individual tax rates and thresholds alone would cost about \$1.87 trillion, before any dynamic effects on revenue are factored in. The major finance initiatives pulling in the other direction were – besides the repeal of the personal exemptions and the change in how bracket thresholds would be indexed going forward – the cap on deductions for state and local taxes paid at \$10,000 as well as ending the individual mandate of Obamacare. The former so-called SALT deductions include property taxes, which tend to be higher in states with Democratic majorities i.e. New York, California, Connecticut and New Jersey – known for high concentrations of wealth and expensive real estate. The cap would therefore prevent many homeowners from deducting thousands of dollars that they previously could, beyond what they pay in property taxes to state, country, and local governments in these places. The individual mandate would save around \$300 billion, since an estimate of 13 to 15 million fewer people would have health insurance coverage, resulting in the government paying fewer tax subsidies. Table 26 in Annex A.VIII provides one full overview of the estimated 10-year revenue impacts of the TCJA.

The content of the final reform was therefore quite different from the tax cuts proposed by the Trump Administration early on, as the run-up to the reform shows how the goalposts for the bill moved. While the overall direction did not change, it underwent two general alterations: it was significantly reduced and it became far less regressive. At each step, the net tax cuts shrank, primarily by slimming down the gains for the highest income households. The Tax Policy Center estimates that households making more than \$730,000 (the top 1 percent) would have received an average tax cut of 11.5% in 2018 under the April outline (TPC 2017). It was curbed to 3.4% in the final reform bill, but it was still a post-tax income rise of \$51,000 on average for this group. Tax cuts for the low- and middle-income groups changed much less through the process. While the TCJA have many moving parts – rate cuts and increases in the standard deduction offset by the abolishment of personal exemptions the overall size of the cut for households making less than \$25,000 barely changed. The April plan would have cut their taxes by 0.3% of their after-tax income (about \$40 on average), while the final bill landed at 0.4% (or about \$60 on average).<sup>260</sup> Similarly, the plan did not develop much for middle-income households between \$49,000 and \$86,600. The April plan held an average cut of 1.3% in post-tax income, or \$760, while the final bill was a bit more generous, landing at an average of 1.6%, or \$930.

Notwithstanding what was originally proposed, the tax cuts were in the end heftily skewed towards the top incomes – both in absolute and relative terms. It seems to reveal a disconnection between this and the Republican rhetoric, as the party elites kept promoting the reform as one for the so-called 'middle class', though they were persistently vague on defining this group (USA-Today 2017b). It was likely by design, as a Gallup poll in June 2017 found that 62 percent of Americans identify themselves as middle or upper middle class – only two percent think they are upper class (ibid.). But the reform mainly served the interests of the latter. These effects would only be magnified over the reform's lifespan; as the personal tax cuts would be revoked, nearly 83 percent of all benefits under the TCJA would go to the top 1 percent of households (TPC 2017). As the Bush tax cuts of the early 2000s, it is likely a shrewd, if not fiscally costly, move, as we can reasonably predict that the pressure to extend income the tax cuts will be intense down the line, as it would otherwise generate a significant tax hike across the entire income spectrum once the cuts expire. Though it was a key move to get Republicans under the reconciliation ceiling, it provides them with enormous political leverage in future tax battles.

The unequal distributive impact, the sunsets along with the sizable debt increase induced by the reform were the elements that met most public resistance; not only from the Democrats, but also from high-profiled billionaires such as Bill Gates and Warren Buffet. They were backed by a choir of large American and international news outlets and journals such as The Economist, The Financial Times, The New York Times, USA Today, The Washington Post, The LA Times, etc. Among economists in academia, there was no clear consensus on whether the reform package would boost the economy to the degree that the Trump administration had predicted – in terms of its growth impact – but there was a broad consensus that it would increase public deficits and economic inequality.<sup>261</sup> Further, the reform was criticized for failing to meet

<sup>&</sup>lt;sup>260</sup> Bear in mind, this group pays very little income tax to begin with.

<sup>&</sup>lt;sup>261</sup> Several critics pondered whether the Republican tax plan was primarily a bill for the party's donors and contributors. In November 2017, Senator Lindsay Graham (SC) was quoted saying that 'financial contributions will stop' flowing to the Republican Party if the tax reform was not passed (The-Hill 2017). This echoed comments from Congressman Chris Collins (NY): 'My donors are basically saying "get it done or don't ever call me again" (Insider 2017b).

the Republican creed of increasing the simplicity and transparency of the tax code. The administration itself had cited the SALT deductions as an example of this, and the bill first proposed by the House would have eliminated those and many break-specific exemptions, including those for medical expenses, disaster losses, and moving expenses. But the final bill, which aligned more closely with the Senate's version, added a wave of new tax breaks to the bill, such as a tax reduction for craft brewers and special relief for certain citrus growers (NY-Times 2017), and seemed to make existing ones even more complicated.<sup>262</sup> One source claimed that Republican ambitions 'fell to powerful forces of lobbying and the status quo. Killed tax breaks returned to life. New ones sprung beside them. A plan for individual tax brackets become five, and finally eight' (ibid.)

If we return to the main distinction between rates and thresholds, the Republicans were – in contrast to the Right in the Danish case – unapologetic in their pursuit of lower marginal tax rates. As shown, they promoted the idea fiercely throughout the reform process and did not need outside agents to provide political cover. Even though the Senate-based reform package ended up closer to a status quo bracket structure – for various reasons – than the threetier structure originally planned, only the rate levels were up for discussion in the public discussions. It became the quick guide to judge whether one version of the reform plan would cut income taxes more or less than previous versions. And five of the seven bracket rates were ultimately cut. In my view, it is staggering how little debate there was on defining the corresponding bracket thresholds; they were never publicly discussed by any partisan actor and at best mentioned as an afterthought. Combing the reform materials, I come up short trying to answer why the threshold limits of the seven tax brackets were altered the way they were.

#### 7.4.4 Summary

The US case clearly reveals the relentlessness of the Right trying to reduce the level of income taxation. Their desire was openly transmitted – even before Trump's election – and so was their ambition to cut taxes drastically. Though shielding themselves using a rhetoric of 'middle class relief' and 'revenue neutrality', it was the limits set by the reconciliation rules in Congress that capped the size of the cuts and the policy structure they can choose. Though the top marginal tax rates on income were ultimately cut by 2.6 percentage points, lower than President Trump's original plan, it was the reductions in tax rates

<sup>&</sup>lt;sup>262</sup> For example, the deduction for moving expenses was retained for members of the armed forces only.

across the many tax brackets that provided the main gains of the reform. These changes – along with other targeted measures such as the higher exemption levels for the AMT and the estate tax – made the richest taxpayers the obvious beneficiaries.

# 7.5 United Kingdom

The UK income tax system of the last 40 years has generally been a tale of two stories. The headline changes were the steep cuts in the marginal tax rates during the Thatcher-reign – with the top rate falling from 83% to 40%, and the basic rate from 33% to 25% (Alt, et al. 2009), along with a major reduction in the number of tax brackets (from 11 in 1979 to 2 in 1990). At the same time, thresholds and allowances have tended to rise in line with inflation instead of earnings, leading to significant fiscal drag over time. As a result, the size of income taxes as a percentage of GDP has fluctuated between 8 and 10 percent since 1980, indicating a relatively stable burden.

By 2010, the schedule had evolved into a three-tier one. The personal allowance allowed the first £6,475 of earned income to be deducted. From here, the system dictated a 20% basic rate, a 40% higher rate (starting at £37,400<sup>263</sup>), and finally a 50% additional rate (starting at £150,000). The latter was introduced by the Labour government as a part of the 2009 Budget.

### 7.5.1 A budgetary overview

As noted, changes to the UK income tax code are linked to the individual yearly budgets. Therefore, we need to start our assessment of the Right political impact with a wider shot of the policy measures that have been enacted over a series of years, as it seems they would more likely accumulate from budget to budget rather than materialize more infrequently, as in Denmark and the United States.

As with any macro-fiscal budgeting process, there are a lot of moving parts. During the Conservative reign from 2010 to 2018 – the end point of my analyses – no less than 917 individual tax measures were passed through the budget, 239 alone within the income tax domain (OBR 2021) – changes that come in all sizes and in both directions.<sup>264</sup> We already know that the major

 $<sup>^{263}</sup>$  It corresponded to a de facto threshold at £43,875 when adding the elements (£6,475 + £37,400).

 $<sup>^{264}</sup>$  The 2018 Budget provides good examples. As one budget headline, the Conservative government decided to raise the tax-free personal allowance to £12,500, while also raising the higher rate threshold to £37,500, at a joint estimated cost of £3.3

parameters of the income tax schedule, too, underwent a noticeable transformation during this period (see **Table 12** in **Annex A.II**, for a display of the UK policy data as recorded by the OECD, which was used in our macro-level analyses). Of course, these changes in parameter values refer to specific policy decisions, and I dug up all of them by investigating the content of each budget as published by the Exchequer. **Table 10** gives the full overview of the Conservatives' major tax legislation and its gradual evolution. Glancing over the table, one must quickly arrive at the conclusion that UK income tax policies have largely centered on the changing thresholds of the personal allowance and the higher rate threshold. In contrast, three of these six items have not changed even once during the period – the basic and the higher rates themselves and the threshold for the additional rate, which has stood firm at £150,000. Finally, the additional rate was cut once (in 2012) under large public scrutiny, as I demonstrate below.

billion in the fiscal year 2019-20. Contrast this to another, more peculiar, tax measure undertaken in the same budget regarding small charitable donations. Before, UK taxpayers were able to claim 25% on cash donations of £20 or less, up to £2,000 in one tax year. The government raised this limit to £30 but did not expect this decision to yield any budgetary consequences (+£0).

	0		-				
<b>Prime Minister</b>							
(Chancellor)	Budget	PA	<b>Basic rate</b>	Higher rate		Addition	al rate
				Threshold	Rate	Threshold	Rate
Policy	baseline	£6,475	20%	£37,400	40%	£150,000	50%
Cameron	2010 (June)	£7,475		£34,900 <sup>1</sup>			
(Osborne)		(+ E1,000)		(-E2,500)			
Cameron	2011	£8,105		Freeze $\rightarrow$ £34.370			
(Osborne)		(+ £630)		(- £630)			
Cameron	2012	$E9,205^{2}$		$E32,245^{2}$			45%
(Osborne)		$(+ E_{1,100})$		(-E2, 125)			(-5%)
Cameron	2013	£10,000		£31,865			
(Osborne)		$(+ E_{560})$		$(-E_{145})$			
Cameron	2014	£10,500 <sup>3</sup>		£31,785			
(Osborne)		$(+ E_{500})$		(- £80)			
Cameron <sup>4</sup>	2015 (March)	£10,800		£31,900			
(Osborne)		(+ £200)		$(+ E_{115})$			
Cameron	2015 (July)	£11,000		£32,000			
(Osborne)		(+ £400)		(+ £215)			
Cameron	2016	£11,500		£33.500			
(Osborne)		(+ £500)		(+ E1,500)			
May (Hammond)	2017 (March)			No policy changes			
May	2017 (November)	£11,850		£34,500			
(Hammond)		(+ £350)		$(+ E_{1},000)$			
May	2018	£12,500		£37,500			
(Hammond)		(+£350)		(+£3,000)			
Source: UK Budgets 20	010 to 2018.						

Table 10 Overview of UK budget decisions with ain impact on the income tax schedule

Notes: <sup>1</sup> The reduction of  $\pounds 2,500$  was based on preliminary RPI forecasts, but was later revised to  $\pounds 2,400$  instead, giving a higher rate threshold of  $\pounds 35,000$ .<sup>2</sup> In the Autumn Statement 2012, the PA was increased by a further £235, pushing it to £9,440, while subtracting the similar amount from the higher rate threshold (£32.010, instead). <sup>3</sup> In the Autumn Statement 2014, the PA was bumped a further £100, pushing it to £10,600. <sup>4</sup> The measures from the March 2015 Budget was never enacted into law, as the later Budget from July 2015, now the single-party Tory cabinet, overwrote these decisions.

## 7.5.2 The Conservative-LibDem coalition

In 2010, the Conservatives ended their 13-year government drought. The General Election on May 6 resulted in a hung parliament for the first time since 1974. In less than one weak, however, the Conservatives, who won the most seats, agreed to form a coalition with the Liberal Democrats, with David Cameron as Prime Minister and Nick Clegg as Deputy Prime Minister. The parties published a joint coalition agreement specifying the terms of the coalition, including their tax aspirations (HM-Government 2010). The Conservatives' manifesto in 2010 had been vague in its tax language. They opposed Labour's proposed increase in National Insurance; they wanted to raise the inheritance tax threshold to £1 million (the baseline was £325,000); and they wished to reduce the 'very high' marginal tax rates faced by many people on low incomes who wanted to return to work or increase their after-tax earnings (Conservatives 2010). The coalition agreed to prioritize the personal allowance (PA), and their long-term objective of increasing the PA to £10,000 was taken straight from the LibDem manifesto. Further, the parties explicitly pledged to prioritize it over other tax cuts, including cuts to the inheritance tax. As they took over an economy severely impaired by the Financial Crisis, finding 'free' revenue to cut taxes in any major fashion was a politically tricky task.<sup>265</sup>

In June 2010, the coalition took the initial steps on this path by increasing the PA £7,475 (+£1,000) in its first 'emergency' budget. To help partly fund this measure and to ensure the cuts would focus on low and middle incomes, the government also lowered the threshold limit for the higher rate by a projected £2,500 to £34,900. In addition, the cabinet stuck to the Labour government's decision to freeze the higher rate threshold in nominal terms from the fiscal year 2012-13 to help pay for the future tax cuts for low-income groups. The coalition continued the trend in their 2011 Budget, as it increased the PA by a further £630 to reach £8,105 in 2012-13. Equivalently, the higher rate threshold was reduced by the same amount to leave it de facto unchanged. The cabinet adopted an under-the-radar, yet significant, decision on how to index threshold limits in the future. The UK norm had been to adjust them according to inflation. Yet, the coalition decided to switch the default indexation assumption from the RPI to the CPI starting from 2012-13.<sup>266</sup> As the RPI

<sup>&</sup>lt;sup>265</sup> The 2010 March Budget, which the coalition inherited from the Labour government, included an estimated deficit on the current budget of 8.4 percent of GDP (HM-Treasury 2010).

<sup>&</sup>lt;sup>266</sup> RPI, or the *Retail Price Index*, was the historic inflation measure of the two, and the logic of tracking price changes in goods and services over time mimics the more

tends to rise more rapidly than the CPI, the decision was expected to lead to even further bracket creep down the road. For example, the government estimated that this measure alone would yield an additional £1.1 billion in revenue by the 2015-16 fiscal year. Generally, the cabinet was criticized for convenient 'inflation shopping', as the majority of government transfers and benefits would be linked to the lower CPI, while certain revenue generators – such as car taxes and other excises – must follow the higher RPI.

The 2012 Budget was the most famous of the coalition term. The PA was raised by a further £1,100 to £9,205. At the same time, the higher rate threshold was lowered to £32,245 (-£2,125), enough to ensure that most higher rate taxpayers only received one fourth of the tax cut, a typical basic rate taxpayer would receive.<sup>267</sup> Yet, what stole much of the attention was the coalition's decision to cut the additional rate, the top marginal rate on income, from 50% to 45%.<sup>268</sup> Below, I dive deeper into the politics surrounding this budget.

Then, the 2013 and 2014 Budgets followed predictable patterns by now. The PA was raised with £560 and £500 in successive years, ending at £10,500 in 2015-16 and out-delivering on the coalition's initial long-term goal. The higher rate threshold was also allowed to grow by 1 percent in actual terms, a policy goal defined in Chancellor George Osbourne's 2012 Autumn Statement. The 'true' threshold thus increased from £41,450 to £41,865, but due to the growth in the PA, the statutory threshold had to be lowered by £145. In the coalition's 2015 Budget – the final one before re-election – the parties proposed to raise the PA a further £200 and the higher rate threshold by £115. However, none of them eventually took effect.

### 7.5.3 Conservative rule amidst Brexit turmoil

Entering the 2015 General Election, the Tory tax pledges were more handson, as the party committed to increasing the PA to £12,500 ad raising the (de facto) higher rate threshold to £50,000 over the next government term (Conservatives 2015).<sup>269</sup> Justifying the latter, the Conservatives repeated the argument that the 40% rate had initially been designed as a tax paid only by the

known CPI, used for international benchmarks. Their main difference is their computation method. The RPI uses the arithmetic mean, while the CPI uses the geometric mean.

 $<sup>^{267}</sup>$  The PA increase was expected to provide a gain (in real terms) of £170 to most basic rate taxpayers, but only £42.50 to most higher rate taxpayers in 2013-14.

 $<sup>^{268}</sup>$  Concurrently, the government cut the corporate tax rate as well from 26 to 22 percent in 2014-15.

 $<sup>^{269}</sup>$  In isolation, these moves involve a £380 cut (in nominal terms) to someone earning £12,500, and a £1,867 cut to someone earning £50,000 or above annually.

best-off taxpayers, yet far too many had been dragged into this bracket over the past couple of decades. Further, the party stated. in more defensive terms, that a Conservative government would pledge to not increase 'the rates of VAT, Income Tax or National Insurance in the next parliament' (ibid.).

It was widely predicted throughout the election campaign that no party would gain an overall majority, with expectations of another hung parliament. However, the Conservatives outperformed the polls and secured a narrow majority (330 seats of 650 possible), partly because the Liberal Democrats collapsed, going from 57 to a mere seven seats. It allowed the Conservatives to rule alone this time, and they used their position to propose a revised 2015 Budget in July, shortly after their formation. It boosted the policy changes from their March budget slightly, taking the PA from £10,600 to £11,000 and the higher rate threshold from £31,785 to £32,000. This trend continued the following March, delivering on their campaign commitments. The PA was raised to £11,500 (+£500) and the higher rate threshold received a substantial bump to £33,500 (+£500). The two first budgets thus seemed to divert from the course set by the coalition, as the higher rate threshold, targeting the higher percentiles of wage-earners, took center stage in the Tory tax-cutting efforts and was raised most in absolute terms.

Concurrent with their tax agenda, the Conservatives were preoccupied with the European question and the UK's future membership status. In June 2016, the Leave campaign won the Brexit vote, despite the advocacy to remain by the Conservative leadership. Prime Minister David Cameron, responsible for the Brexit referendum, resigned shortly after and was succeeded by then Home Secretary Theresa May as both Conservative leader and Prime Minister. Philip Hammond replaced George Osborne as Chancellor. May's first budget (the 2017 Spring Budget) was the first during the Conservative reign that did not feature new commitments to further income tax reductions (HM-Treasury 2017b). Shortly after, she called for a snap General Election to be held in June 2017, hoping to secure a larger majority to 'strengthen her hand' in the forthcoming Brexit negotiations. However, a 20-point lead at the start of the campaign had eroded close to Election Day. Though the Conservatives gained 5.5 percentage points, taking them to 42.4 percent – their highest mark since 1983 - they secured only a 2.4 point lead over Labour. In fact, they lost 13 seats, which resulted in a new hung parliament instead of Conservative consolidation. May remained Prime Minister with the support of the Unionist DUP's 19 seats, giving the Tories a razor-thin majority (327 seats out of 650). The tax issue did not feature promptly in the run-up campaign, with Brexit and terrorism dominating the election agenda. The Conservatives reinforced their promise to the £12,500/£50,000 pledge (Conservatives 2017), but their manifesto was noted for lacking commitment to new future tax cuts.

The Conservatives' Autumn Budget of 2017 continued a by now familiar path; it raised the PA to £11,850 (+£350) and the higher rate threshold to £34,500 (+£1,000). The former rise made sure that the PA would keep up with inflation, while the latter, once again, constituted a hike in real terms (HM-Treasury 2017a). Since November 2017, the budget was more permanently moved to the autumn to allow major tax changes to take effect well before the commencement of the new fiscal year. Ahead of the 2018 Budget, set in October to avoid what was thought to be the final stages of Brexit negations, Chancellor Hammond notoriously claimed that the era of austerity was 'finally coming to an end'. The government announced it would meet its commitment to raise the PA to £12,500 from April 2019, one year earlier than planned. Also, the higher rate threshold was raised to  $\pounds_{37,500}$ , a whopping  $\pounds_{3,000}$  singleyear rise, and took the de facto threshold to the promised £50,000. Curiously, the budgetary costs of the two measures, the PA and the higher rate hike, were estimated jointly in the official government budget reports, not as separate posts as one might have expected.

If we tally the score on the Conservative tax record, the decisions they took, first of all, align strongly with our case expectations on policy choice. Their version of the Right tax strategy has been almost exclusively about fine-tuning the bracket limits defining the PA and the higher rate threshold during the recent decade. With the exception of the 5 percent cut to the additional rate in 2012, there has been remarkably little discussion about rates coming from the Right side of the political aisle.<sup>270</sup>

The Tory reign can be divided into two distinct periods, as evident from both the walkthrough of the budgets and **Table 11**, which demonstrates the over-time value of the three key threshold parameters in the UK tax code – the PA, the higher rate threshold, and the additional rate limit – expressed as a percentage of UK average earnings in the given year. It provides a yardstick and allows us to judge to what extent the Conservative policies cut taxes in real terms, or whether a rising wage level has gradually chipped away at them. Here, the findings are clear-cut. During their first term – the coalition period with the Liberal Democrats – the PA increased in nominal as well as real terms, as the PA rose from comprising 21% of the gross average earnings to 32% in 2015, a sizable change. In contrast, the political decision to first lower and then freeze the higher rate threshold had a substantial real impact too, as it went from 141% of the baseline to 126%. This meant, among others things,

<sup>&</sup>lt;sup>270</sup> In 2015, Labour pledged specifically to reinstate the 50 percent top rate on the top one percent of taxpayers to reduce the budget deficit and to help lower and middle incomes by re-introducing a 10 percent starting rate of income tax. They did not specify the cut-off values for this bracket.

that the number of higher rate taxpayers rose steadily during the coalition term, from 3.02 million in 2010-11 to 4.51 million in 2015-16 – or from 10 to 15 percent of all income taxpayers (HM-Revenue&Customs 2021). But the trends shifted in the subsequent periods, as per **Table 11**. From 2015, the PA rose little in real terms – despite the political credit-claiming on the part of the Tories – up to 34% of average earnings in 2019. The higher rate threshold, meanwhile, rebounded to 135%, a 9 percentage point hike, thanks in large part to the grand push made in the 2018 Budget. As a result, the number of higher rate taxpayers dropped below 4 million (3.86 million) once again during the fiscal year 2019-20. Finally, the table keeps clear tally of the erosion of the politically neglected threshold for the additional rate. Political decisions not to intervene kept it constant at £150,000, causing its value to diminish from 503% of average earnings, before the Conservatives took office, to 439% in 2019.<sup>271</sup>

				Additional
Fiscal year	<b>Cabinet parties</b>	PA	Higher rate	rate
2010-2011	Labour	21%	141%	503%
2011-2012	Conservative-LibDem	24%	135%	500%
2012-2013	Conservative-LibDem	25%	133%	495%
2013-2014	Conservative-LibDem	29%	127%	487%
2014-2015	Conservative-LibDem	30%	127%	484%
2015-2016	Conservative-LibDem	32%	126%	478%
2016-2017	Conservative	32%	125%	467%
2017-2018	Conservative	33%	128%	459%
2018-2019	Conservative	33%	129%	450%
2019-2020	Conservative	34%	135%	439%

**Table 11** Income tax brackets in the UK expressed as a percentage of average earnings

Source: OECD (2019b).

Notes: The annual average earnings in the UK rose from £31,137 in 2010 to £37,003 in 2019.

It is tempting to explain the term difference with the Conservative majority status. The first term as part of the coalition was characterized by a much stronger emphasis on cutting income taxes 'at the bottom' and for the many, while we then witnessed a priority of the high-earnings taxpayers, once the Conservatives could rule alone. It is noteworthy that the Tory-led coalition, at the start of their term, faced dire fiscal circumstances and made it a secret to

 $<sup>^{271}</sup>$  It is reflected in the number of UK taxpayers liable to the additional rate; from 236,000 in 2010 (0.8% of UK taxpayers) to 440,000 in 2010 (1.4%) (HM-Revenue&Customs 2021).

no one that reducing the deficit was *the* overwriting goal of the government's economic policy. Still, the coalition, quite remarkably, found a way to cut income taxes for low and middle incomes in each of the yearly budgets.

With the Tories free of cooperation, and with the bulk of the crisis-induced deficit eliminated, the tax cuts began to tilt towards the highest incomes. Looking at **Table 11**, one could argue that the Conservative choice to disproportionally target the high-income segments was due given the restraint they were forced to maintain during the worst crisis years. The full span of the Conservative reign has certainly not been a net win for those in the higher rate bracket. But continuing to tune this specific instrument has become a stable for the Conservatives. The leadership has since flirted with the prospect of raising the higher rate threshold to £80,000, at an estimated cost of £8 billion in lost revenue, but a goal they have not pursued further due to the fiscal uncertainty spawned by Brexit (FT 2019).

### 7.5.4 The 2012 Budget – misjudging the unpopularity of topend rate cuts

To look more in depth at the politics surrounding the individual budgets, I next sketch a timeline for the 2012 and the 2018 budgets, which, as mentioned, capture significant variance in terms of policy change. The 2012 Budget oversaw the largest single increase in the PA, a large concurrent lowering of the higher rate threshold and a 5 percentage point reduction of the additional rate. How the latter was received, given the theoretical expectation of limited success pursuing marginal rate cuts in the UK setting, is intriguing to study. The 2018 Budget witnessed the largest single-year increase in the higher rate threshold of this period, dwarfing the hike to the PA made in the same budget. How the Conservatives framed this unequal distribution of tax cuts across income groups is equally interesting.

Let us begin with the process leading up to the 2012 Budget. The media coverage leaves the clear impression that the idea to raise the personal allowance came from the Liberal Democratic coalition partner, whereas the chief Conservative goal for the budget was to abolish the 50 percent income tax rate. In July 2011, the contours of conflict were already drawn, as the Conservative Chancellor George Osborne, backed by the Tory Right, came out hard against the 50 percent rate, pushing three main arguments: (1) it raised little revenue and could be scrapped at small fiscal costs; (2) it risked making the UK uncompetitive compared to other European and G20 countries; and (3) the rate was never meant to be permanent, but was a temporary tax introduced by Labour to cope with crisis deficit (Guardian 2011b). The LibDem leadership came out equally hard against its abolishment, insisting instead on easing burdens on low-paid families (Guardian 2011a). The general public seemed to side with the latter, as the 50 percent rate was popular even among Tory voters. Yet, Osborne seemed eager to fight it and instructed his Treasury to assess how little revenue the tax actually brought in.

The positions remained entrenched entering 2012. On January 26, Deputy Prime Minister Nick Clegg warned that the pressure on family finances, squeezed by the economy in turmoil, had reached a 'boiling point' voicing a call to speed up the coalition's goal of raising the PA £10,000 within this parliamentary term (Guardian 2012d). Chancellor Osborne reinforced his desire to scrap the 50 percent rate two days later, stressing once more that his Labour predecessor, Alistair Darling, had only considered it temporary. Right before the March budget, the LibDems publicly signaled willingness to compromise on the 50 percent rate, if the coalition could agree to accelerate efforts to meet the £10,000 PA limit a year ahead of target (Guardian 2012a).

Ultimately, the coalition compromised and agreed to reduce the 50 percent rate to 45 percent instead of abolishing it (FT 2012). In his budget speech, Osborne cited the its damaging effects on competiveness held up against its low revenue intake, as government calculations showed that the 50 percent rate only raised a third of the intended £3 billion. His Treasury estimated that the policy change would cost a mere £100 million in lost revenue. The Labour opposition predictably contested this tax cut. In his opposition speech, Labour leader Ed Miliband stressed that the Budget failed 'the fairness test', as the Government did not use 'every penny in the Budget' to relieve the squeezed middle-income families.

Media reactions to the budget were also dampened. The Guardian and the Independent both summed up the Chancellor's budget as 'a gamble', and the Financial Times his budgetary moves as 'an audacious roll of the dice'. Some pondered on the immense fiscal costs of raising the PA by a further £1,100 at an immediate estimated cost of £3.3 billion, though it would have been even more had the government not opted to bring down the higher rate threshold as compensation. Predictably, attention turned mainly to the cuts to the 50 percent rate with different touchpoints of criticism.<sup>272</sup> First, the government's

<sup>&</sup>lt;sup>272</sup> The Budget also received heavy criticism for two other decisions in particular. To raise sufficient revenue, the government decided to freeze the special PA for pensioners in 2013, which was higher than the standard PA for those aged 64 or below. In a second move, they decided that new pensioners reaching age 65 after April 2013 would be kept on the standard PA rather than move to the higher PA for pensioners. The value of the existing pensioners' PA would then be frozen until it aligns with the

estimate of the small revenue costs associated with reducing the rate was contested by multiple economists. Second, the media repeatedly used the millionaire as a reference of the skewed gains it would generate; a banker earning £1 million would get £42,500 in direct tax cuts. It was later leaked that the Prime Minister acted as a restraining policy influence on the Chancellor, as the former was concerned about the signals a dramatic slashing of the 50 percent rate would send to middle income earners (Guardian 2012c). The Conservatives suffered significantly in the ensuing polls, and it was clear that the 50 percent cut did not have the credit-claiming opportunity that Osborne had expected. Polls with the Conservatives and Labour neck-and-neck before the 2012 Budget clearly began to swing towards Labour as negative press mounted (Guardian 2012e) and remained there for at least two years after. Osborne's personal credibility took a dive too. In June 2012, even Prime Minister Cameron admitted mistakes in the budget that left the government 'ploughing into a brick wall' (Guardian 2012b). His comments generally reflected poorly on Osborne, whose stock according to many had taken a big hit, after being a feted as the key Conservative strategist for years.

The Conservative's main target in this budget was, quite obviously, the richest income earners and rewarding them with lower marginal tax rates. However, this case demonstrates that the Tories presumably underestimated just how unpopular such policy was in the political-institutional context. The backlash was significant, and the Conservatives likely overplayed their 'tax cards'. It represented, perhaps, a key learning experience for the party, which

standard PA and then abolished. The coalition claimed, perhaps rightly so, that introducing one single allowance instead of different age-related ones would represent a major simplification, that would save money, while no pensioners would lose cash in nominal terms. Yet, the move was met by public outcry, as especially those reaching the pension age on average would miss out on £285 compared to the baseline. The move was dubbed the 'granny tax'. Another political loss was the so-called 'pasty tax'. Under the VAT rules, sales of meals bought to eat or cook at home were zerorated for VAT, hence not taxed. By contrast, meals bought and consumed at restaurants were liable to the 20 percent standard VAT rate. There was a grey zone of foods baked for sale and sold while still hot, which was also not taxed under current rules, e.g. freshly baked bread, pies, pasties. The coalition proposed to close this loophole, so only bread would be exempt in the future, but this sparked immediate backlash. The discussion focused a lot on the Cornish pasties. Critics claimed the Conservatives were 'out of touch' with ordinary people, only confirmed that neither the Prime Minister nor the Chancellor could remember when they had last eaten a pasty. The Government later made a U-turn on this decision and reduced the intended 20 percent charge to 5 percent.

has since refrained from pushing new demands to scrape the additional rate or cut the higher rate.

# 7.5.5 The 2018 Budget – threshold cuts saved by unexpected windfall

The run-up agenda to the 2018 Budget was dominated by the dire state of the UK National Health Service, cross-pressured by years of low spending increases, growing waiting lists, and higher demands for care by an ageing population (Guardian 2018c). On the NHS's 70th birthday in June 2018, Prime Minister Theresa May promised an extra £20 billion a year funding by 2023-24, which meant that the then £114 health budget would rise an average of 3.4% above inflation annually (ibid.). The revenue to finance this spending hike was found partly in the so-called 'Brexit dividend', membership contributions saved from leaving the European Union, but she also made it clear that taxpayers should expect to contribute more (BBC 2018). It signaled, according to commentators, a noticeable shift in rhetoric compared to the former Tory leadership. Government sources even hinted that May was prepared to forego the Conservative tax pledges made in the last general election – increasing the PA to £12,500 and the higher rate threshold to  $\pm 50,000 - to pay$ for her NHS plan (Guardian 2018b). This would perhaps involve freezing the income tax thresholds over the coming years, which would stick in the throat of many Tories.

On October 3, less than a month prior to the budget, Prime Minister May delivered a publicized address to the Conservative Party conference, where she marked a new way forward for economic policy in the UK, promising that the era of 'austerity is over' (Guardian 2018a), though she did not give a specific timescale or plan for raising public services and welfare budgets to growth rates higher than inflation. However, this along with the previous NHS pledge raised expectations to the coming budget. But it also put her Chancellor Philip Hammond between a rock and a hard place. Asked about the Conservative tax pledges, senior Tory sources said it was 'up for grabs' (Telegraph 2018b).

The pains of Chancellor Hammond became easier in the weeks leading up to budget, however, as initial tax receipts for the fiscal year 2018-19 came in well over projections. The Office of Budget Responsibility (OBR), an independent economic watchdog, had overshot the predicted £25 billion deficit by about £13 billion, leaving the Conservatives with a little more room to maneuver in the upcoming budget, and at least for now shelving considerations of any major tax hikes, thought to be difficult to get through parliament without a stable Conservative majority.

The 2018 Budget announced on October 29 – pushed forward a month due to Brexit negotiations later that year – contained significant income tax cuts, much to the surprise of political observers. It committed to raising the PA to £12,500 and the higher rate threshold to £50,000, delivering on the Tory promise one year before expected, at a total estimated cost of £2.7 billion. Some of the gains would be clawed back by changes to national insurance, hidden in the Budget's small print. The upper limit for 12 percent NI band, previously aligned with £46,350 higher rate threshold, was raised to £50,000, meaning that higher rate earners would now pay 12 percent NI on the subset of income between £46,350 and £50,000, instead of the 2 percent rate now kicking in on earnings above £50,000 (Telegraph 2018c).<sup>273</sup> Yet, higher rate earners would be around £520 better off a year, once the NI hike was taken into account. Motivating these cuts, Chancellor Hammond directly cited the better-than-expected OBR estimates for the public finances and wished to claim credit for having lifted another 1.7 million taxpayers out of income tax altogether since 2015, and nearly 1 million out of the higher rate. However, experts described this as a 'gamble', deciding to use every means available on his NHS spending increase, while at the same time cutting incomes taxes - on the rich, predominantly – and making the Universal Credit more generous. With fiscal uncertainty looming from the Brexit fallout,<sup>274</sup> his strategy was regarded as reckless, as his budget would increase long-term borrowing rather than fulfill the Tories' long-term commitment to balance the budget (Telegraph 2018a).

Despite the political and fiscal binds put on the Tory government by May's NHS promise, the party used their political capital to cut income taxes in a way that has become customary: by raising threshold limits. They did so in a way that was disproportionally skewed – at least in absolute terms – towards the higher income groups without suffering immediate electoral backlash.

### 7.5.6 Summary

The politics surrounding the UK budgets during the Conservative reign reveals a party that did not shy away from carrying the low-tax mantle, despite leading the country through a time of poor fiscal outlooks. The political compromise with Liberal Democrats made them turn their focus on offering relief to the broadest group of taxpayers by raising the tax-free allowance in a number of

<sup>&</sup>lt;sup>273</sup> As a consequence, while the income tax rate to be paid on that slice will be reduced by 20 percent, national insurance contributions will go up by 10 percent, making the net cut only 10 percent.

<sup>&</sup>lt;sup>274</sup> The CBO's projections depended on a "smooth" departure from the EU, which a 'no-deal' Brexit could change.

subsequent budgets. Taught by the electoral fallout after targeting the additional rate, the Conservative efforts have since focused on altering threshold limits, specifically by raising the higher rate threshold to take 'hardworking people' out of this tax band (Conservatives 2015). A move that, despite the rhetoric, disproportionally benefits the higher income groups.

# 7.6 Conclusion

My studies of the Danish, US and UK reform cases support many of my theoretical expectations regarding the Right's income tax strategies in different regimes.

The Danish case – the few B/low P type – seems to back how politically tense discussions on the top tax rate are. The run-up to the 2009 reform shows that the Right coalition went to great lengths to divert potential blame, including giving the Tax Commission responsibility for proposing the entire legislative framework. Still, the idea of cutting the marginal tax rate on the top bracket stuck out like a sore thumb, and they only succeeded in lowering it by stealth, as they abolished the middle tax bracket. In turn, the Right government had much less trouble convincing the reform-averse Danish People's Party to convert the rate cuts at the top end into raising the top bracket threshold, instead. One can speculate whether it was the cabinet's accepted end goal from the start, as it was a much easier sell to lift 'ordinary' wage earners such as school teachers, nurses and carpenters out of the top income bracket instead of reducing the marginal tax rate on 'millionaires'.

The reform's cuts were fairly broad-based, as the bulk of foregone revenue was used to lower taxes at the bottom of the tax schedule. In rhetoric at least, the cabinet did a lot to stress that the reform would boost incentive effects at both ends by also increasing the net gain of taking a low-wage job compared to claiming benefits. Still, the unequal distributions of gains in absolute terms was the opposition's main entry of attack, persistently calling it a 'red wine reform'. Since, the Right parties – with no middle tax bracket to target – have found it increasingly difficult to find politically feasible ways to cut income taxes on middle and high incomes, and have turned their attention to improving work incentives for those at the fringe of the labor market (Venstre 2015).

The off-diagonal case, the 2017 US reform, reveals how scarce discussions on tax thresholds were in the American context. Not that my theory demands that thresholds cannot be a central part of the reform debate in high B settings, as the analysis of the country aggregates in **Chapter 5** showed. But this was not the case here. While the Right's reform plans were heavily debated and scrutinized, the main row between policymakers centered on the number of tax brackets, which the future tax schedule should include, and their respective rates. The stages in President Trump's tax plans were mainly evaluated on their rate levels. Further, the debate tended to zoom in on the top marginal rate, and to what extent highest income earners would see reductions from the current 39.6 percent rate. The final reform, which cut rates modestly across the entire income scale, was more incremental than Trump's initial proposals as a result of the fiscal constraint placed on the bill by the reconciliation rules. Still, major inequality-boosting initiatives, such as the de facto erosion of the AMT and the estate tax, remained in the package.

The political Right in the US – in the form of the Republican leadership – pushed the income tax agenda openly and aggressively, stressing the importance of boosting macro-economic growth and middle class relief, irrespective of the actual policy content of the reform package. They used increasingly colorful framing arguments; Trump claimed that his tax plan would be 'rocket fuel for the economy'. Democrats, instead, zoomed in on the vast accumulation of debt, by virtue of unfinanced tax cuts, and the unequal distribution of gains going to the 99<sup>th</sup> percentile, or the '1 percent'.

The UK cases – the few B/high P type – showed the Conservative commitment to cutting income taxes, even during the poor economic times of the early 2010s. During the first coalition years, the PA was raised significantly, mainly at the insistence of the Liberal Democratic coalition, though the Tories would later claim credit referencing the higher PA. The prime Conservative goal in the first term was to remove the 50 percent additional rate, contrary to what we should expect theoretically in this case configuration. Yet, the politics surrounding the 2012 Budget shows that the Conservatives severely underestimated the electoral fallout from cutting this rate from 50% to 45%. The move was highly controversial, as the additional rate was unpopular even among a large share of Conservative voters. It sparked a long-term Tory dive in the polls and provided a learning experience, as they have since refrained from pushing for the abolishment of the additional rate.

Income tax policy in the UK has since centered on thresholds only. Freezing, and even lowering, the higher rate threshold was perhaps the neat, invisible way of raising additional revenue for deficit reduction during the coalition years. The economy was in much better shape when the Tories won a majority in 2015. They now specifically targeted raising tax thresholds and disproportionately targeted the richer income segments and delivered on their 2015 pledge to raise the PA to £12,500 and the higher rate threshold to £50,000 in successive budgets from 2015 to 2018. These were moves that perhaps were less visible to the 'ordinary' voter, as I will discuss in the next chapter.
### Chapter 8. Visibility of rates and threshold limits

In the dissertation, I have rested on a series of assumptions on the tax instruments that are key for the conclusions I draw. For example, I have demonstrated how the Right refrain from pursuing the preferable option of cutting income tax rates (on the rich) when the political room to maneuver is institutionally constrained and then assumed it is in part due to a 'visibility mechanism'; the rate is the most visible, but politically contested, legislative component of the income tax schedule and voters are assumed to be more capable of grasping how changing rates rather than threshold limits affect their tax liabilities. Yet, such a notion of causal blurring is only one way of interpreting the macro and case study findings, and it is tough to validate this explanation without hard empirical evidence on the central assumption.

While this visibility proposition has remained untested, both in the dissertation and in the literature at large, this chapter attempts to dig deeper into how such mechanisms establish themselves among voters, whom politicians may either wish to please or deceive when seeking to alter the policy status quo.<sup>275</sup> I put them to a novel test by fielding a survey among a sample of Danish voters with the goal of disentangling whether they perceive tax reforms conducted via rates and thresholds differently, and what drives their support. The cornerstone is a set of two survey experiments centered on the top marginal income tax rate in Denmark ('topskatten'), the highest income tax bracket, as noted previously. Respondents are asked to list their support for two fictitious tax proposals: (1) one that aims at raising (or lowering) the top bracket threshold, and one that lowers (or raises) the top marginal rate. Next, I pose the central visibility question that taps into how proficient voters are in correcting linking each type of policy change to the 'true' causal change in the tax liabilities of high-income earners.

<sup>&</sup>lt;sup>275</sup> One can go into a hefty discussion whether it is the voters' perceptions of tax instruments that might impact the partisan leeway to reform, or whether it is the politicians' perceptions of the voters' attitudes that are key here. It presents two different approaches to this factor: one clearly driven at the micro-level, and one founded at the elite level. My theoretical frame follows a top-down approach, fundamentally, and I thus tilt towards the latter argument, which is perhaps a valid reason not to rely on survey data to test this proposition. But the survey approach still have its clear merit in my view, as I expect the elite perspective on voter attitudes to be closely aligned with what is going on at the micro-level, for no other reason than politicians have a huge interest in knowing how voters actually perceive these policy questions.

Overall, I find that instrument choice matters significantly for voters' ability to grasp its content as well as their reform support. Rates are at least 10 percentage points easier to comprehend when we measures it as the share of respondents who are able to submit the 'true' causal impact. It is a non-trivial difference. In addition, I find that raising the raising threshold, in a moderate fashion albeit, is the most feasible way of altering the Danish 'top tax', whereas the suggestion to lower the marginal rate gathers more voter opposition than support. The results seem, therefore, to align with the theory: tax rates are visible and typically not a politically popular mode of cutting taxes at the top end.

In series of supplementary analyses, I explore the implications of (low) visibility. My findings show that this causal confusion is strongly linked to political indifference among the voters; they do not oppose (or support, for that matter) even radical reform proposals to cut or raise income taxes if they do not properly understand their impact. It is even the case for voters with a strong Left-Right identification, which we expect to hold quite settled opinions about proposals that tax the rich, given their immediate redistributive consequences. Finally, the analyses in this chapter confirm that among 'informed' voters we find significant differences in policy causal beliefs at either ends of the ideological spectrum on a more ontological level, instead of them merely disagreeing over which of the central tax functions they wish to give more or less political weight. Right-leaning voters tend, for example, only to see the favorable effects of high-end tax cuts, i.e. policies as growth-stimulating, whereas they to much less extent do not see, or at least heavily downplay, the adverse effects on inequality and the primary balance.

# 8.1 The incomplete knowledge of voters' grasp of tax instruments

The literature on voters' redistributive preferences, a dimension of obvious relevance to the tax question, is one of the most discussed intersections of policy science and economics, starting with the seminal works of Romer (1975) and Meltzer and Richard (1981). Such models tend to highlight the importance of material self-interest in shaping preferences,<sup>276</sup> voters are expected to align in a single-dimensional spending or tax policy, and political processes gener-

<sup>&</sup>lt;sup>276</sup> Material conflict over redistributive policies divides voters primarily according to *income* and/or *risk exposure* (Rehm, et al. 2012). Either way, the material living conditions of voters, now or in the future, become a main source of social preferences (Jensen 2014).

ate policy outcomes within this space. They predict that preferences for redistribution decline with income, and those at or below the median income are more likely to demand more redistribution at higher levels of inequality.<sup>277</sup> Irrespective of the specific findings, the spending and the revenue side are considered to be closely intertwined, which may explain why taxes have often been subsumed under *one* measure of the size of government (Ballard-Rosa, et al. 2016). Most often, it has translated into the study of voters' preferred level of (total) taxes raised.

A more recent branch of the literature has rejected, wisely, the notion of unidimensionality and fixed more on the tax question, specifically, rather than the redistributive issue as a whole. Multiple studies have argued that voters, when evaluating tax policy, care about two things at once: the level of revenue raised by governments and its structure, i.e. progressivity (see e.g. Barnes 2015, Beramendi and Rehm 2015, Sumino 2015, Berens and Gelepithis 2018). Many of them rely on a similar type of self-interest approach to the analysis of tax preferences. Income, in particular, is expected to be a powerful predictor of voters' views on tax progressivity<sup>278</sup> but to a lesser degree of tax levels.<sup>279</sup>

These newer studies also share a strong overlap in data sources. When the goal is to study tax preferences cross-nationally, studies tend to rely on similar international surveys to do so, in particular the International Social Survey

<sup>&</sup>lt;sup>277</sup> High-income voters are more likely to oppose redistributive policies (Iversen and Soskice 2006).

<sup>&</sup>lt;sup>278</sup> High-income voters are on average less likely to support progressive tax policies than low-income voters. Yet, the operational phrase 'on average' is key. For example, Barnes (2015) finds a non-linear effect of income across the income scale, which at a minimum leads us to consider that multiple logics could be at play, not solely related to income.

<sup>&</sup>lt;sup>279</sup> The picture is murkier regarding preferences for tax levels. Higher income is assumed to entail higher tax payments, although not all tax systems are strongly progressive in practice (Prasad and Deng 2009), as we have seen in earlier chapters. But spending programs also shape tax preferences. Beneficiaries of spending are generally found to be more supportive of the taxes that finance it (Mettler 2011). The propensity to receive welfare benefits may be conditioned by income but also depends on more complicated 'horizontal' characteristics, such as employment status, sector affiliation, age, health, civil status or dependent children. These are often tied to various social risks (Barr 2001, Moene and Wallerstein 2001). Barnes (2015) finds, perhaps a bit surprisingly, an inverse U-shaped support of high tax levels when gauging the effect of income. She shows that middle-income groups are the most sanguine about a high overall tax burden, in contrast to the expectations based on much of the redistribution-focused literature where support is thought to decline monotonically with income.

Programme's (ISSP) Role of Government questionnaire from 2006. The ISSP is one of the lone large-scale survey collections that actually get at tax preferences as such and not just use generic redistributive statements that reveal whether the respondent wishes to change the size of the (welfare) state, or if the government should do more or less to reduce income differences in society. The ISSP surveys the citizens' sense of (income) tax burdens in their respective countries. It asks, specifically, about perceptions of burdens relating to three core reference groups, low, middle, and high incomes,<sup>280</sup> however judged by the respondents, and these items are frequently used to construct the dependent variables. Studies like Barnes (2015), Sumoni (2015), and Berens and Gelepithis (2018) compute a measure of preferences for progressivity, which captures whether the respondent's assessment of the taxes paid (relative to their ideal) decreases with income (Barnes 2015: 62).<sup>281</sup> The same items are sometimes used to measure attitudes towards *levels* as well, and the authors then take the average score across all income groups as a token of whether taxes are generally too high or low.<sup>282</sup>

Whereas their strength lies in their extensive coverage, they are hardly ideal measures for studying evaluations of potential tax reforms, as it is not easy to translate voters' principled position on taxation into tangible policy, which one can support or oppose. For example, if a respondent believes the rich gets away too easily (i.e. demands more progressive taxation) and thinks tax levels are generally too high, it is unclear what the specific course of action should be, as there is a host of potential tax plans, as seem in the previous chapters. The results do not consider whether such preferences are feasible, consistent options when we go from principle to practical political solutions. It is, hence, a challenge to transfer insights from *this* literature on tax preferences to explaining something more concrete when it comes to policy dynamics.

There are, of course, studies with a more policy-centric approach. In one of my favorite studies, Ballard-Rosa and his colleagues (2016) survey a representative sample of Americans on their preferred income tax structure. They rely on a conjoint setup in which respondents choose among fictional income

<sup>&</sup>lt;sup>280</sup> The wording of the questions is: "Generally, how would you describe taxes in [country] today? We mean all taxes together, including national insurance, income tax, VAT and all the rest. For those with [high/middle/low] incomes taxes are: (much) too low; about right; (much) too high; can't choose."

<sup>&</sup>lt;sup>281</sup> It yields a binary response. 1 indicates respondents who think the rich are taxed too little, relative to the lower income groups.

<sup>&</sup>lt;sup>282</sup> 'Much too high' is coded as 1, and 'much too low' as 5, so increases in the average tax variable indicate greater support for higher taxation.

tax plans. The authors use six tax brackets and their threshold limits as fixed parameters<sup>283</sup> in their design and then vary the potential tax rates assigned to each bracket with only minor restrictions.<sup>284</sup> The plans include then a final dimension that features a rough estimate of the costs of each plan in terms of revenue, grouped as to whether it would produce (much) less revenue than before the reform, about the same revenue level, or (much) more revenue. The authors find unequivocal strong support for a progressive distribution of income taxes in the American public.<sup>285</sup> Their favored scheme is one that taxes all income below \$85,000 at a 15 percent rate or less<sup>286</sup> and income of \$175,000 and above at minimum 35 percent. The results align neatly with what we have found elsewhere on the share of progressive voters across the OECD, and in the US in particular (Barnes 2015: 72). However, the study adds much more specific predictions on the type of policy reform voters at large should prefer if given the choice.

Ballard-Rosa and co-authors (2016) do a lot to advance our discussion of voter preferences for income tax reform, working with experimental designs. Yet, it is clear from the theory presented in this dissertation that there are still a lot of conceptual propositions we must revisit. Three points, in particular, spring to mind. The first is how to define the proper role of the policy status quo in such survey setups, which we know carries significant appeal for (risk-adverse) voters, when they are pressed on choosing between new and old policy. If we take the ISSP path, it is evident that judgements of specific tax burdens as 'too high' or 'too low' refer to an underlying yardstick for comparison between perceived burdens and an ideal. However, it is not clear what specific status quo these voters base their implicit assessment on, and to what extent these yardsticks are systematically different from the 'true' burdens taxpayers face. The conjoint setup does a better job on one of these dimensions, as it

<sup>&</sup>lt;sup>283</sup> The six income brackets used in the survey had cutoffs of \$10,000, \$35,000, \$85,000, \$175,000, and \$375,000, which closely matched the existing US tax code at the time.

<sup>&</sup>lt;sup>284</sup> The possible rate levels were 0 percent (only for < 10,000 bracket), 5 percent, 15 percent, 25 percent, 35 percent (not for < 10,000), 45 percent (only for the two top brackets), and 55 percent (only for the top bracket).

<sup>&</sup>lt;sup>285</sup> Respondents were consistently less likely to support a given tax plan when the tax rate on the poorest groups would increase but more likely to support it when the tax rate on the richest income groups was high. What was perhaps most interesting about the US experience, also given the case study on the Trump tax reform, was that respondents generally favored tax plans that raised more revenue than the baseline and opposed plans that generated less (Ballard-Rosa, et al. 2016: 7-8).

 $<sup>^{286}</sup>$  In 2014 when the survey was fielded, average earnings in the United States were \$57,410.

makes sure that we can link the voter evaluation to specific policy values and not just perceptions. But it does not solve the status quo issue, as having a strategy of analysis that by design varies the values each reform attribute can take does not explicitly inform the respondent of what is the current policy in place, and what are deviations from it. In essence, one is presented with forced choices between a set of (almost) randomly generated income tax plans and not between the current policy and its alternatives, which is, arguably, the more realistic choice of politics.<sup>287</sup>

Second, the whole visibility proposition, as advanced in this dissertation, is still lurking. Most recent work on voter tax preferences rests on the rather critical assertion that voters hold if not exhaustive views on and knowledge about the tax system, then at least sufficiently informed opinions to deliver meaningful survey responses. Yet as noted, this is not an easy debate to settle with theory alone. Most scholars probably agree that voter biases clearly exist within the tax realm but do not agree upon their specific size and scope. Without a metric to capture such cognitive limitations, it is not possible to decompose voter attitudes into what we know can be attributed to actual 'preferences' and what are the mere result of biases or lack of tax knowledge. Of course, the relationship between these two, the truly informed view and the bias, will undoubtedly vary a lot across the different dependent variables we can study, which may include voters' views on both the general direction of tax levels in society ('more or less income taxation') to the detailed legislative interventions. I see, therefore, a clear need to unfold this discussion of how easy or difficult it is to interpret the specific components of the tax code more wholeheartedly, if we wish to develop a deeper understanding of the role of voters' (lack of) informational priors.

The third and final proposition relates, of course, to the central maxim of the dissertation on the type of instrument choice. It is clear that existing surveys have done very little to disentangle views on tax reform as conditioned by the use of different tax instruments. The study by Ballard-Rosa and his collaborators (2016) is, again, a positive exception in this regard, as it considers how tax rates (at various levels) affect policy preferences and does so in a highly detailed manner by gauging these effects across six tax brackets. Given the distinction between the rate *and* the threshold limit, we can raise the obvious

<sup>&</sup>lt;sup>287</sup> The authors choose the sets of tax (potential) rate levels for each tax bracket based on 'pretesting results and previous work on ideal marginal tax rates among the US electorate' (Ballard-Rosa, et al. 2016: 5). It seems a little strange that they do not make it a key point for selection to include a set of tax rates that actually correspond to the US income tax code and would make them the baseline for their voter evaluations.

criticism that their analysis only studies the one side of the coin. Why are new threshold limits not considered as an integral part of the proposed tax plans, if only to confirm that these types of instruments had zero or little impact, relative to tax rates, on respondents' tendency to support a given tax plan? One reason may be, as touched upon earlier, that in the US, the IRS, not policymakers, generally sets these threshold limits on the year-by-year basis. Consequently, such policy instruments may not have been on the authors' radar, even though they are highly relevant in other national contexts.<sup>288</sup>

## 8.2 A survey experiment on rates and threshold limits

My intent with the survey is to contribute on all three accounts: draw a much clearer policy status quo, test to what extent prior knowledge affects evaluations of reform proposals, and distinguish between the main instrument types. The design I present fulfills these criteria. The web survey on tax preferences in the Danish context was conducted on Epinion's online panels, 1,561 Danes aged 18 to 75 participated, and interviews were completed between 22 October and 8 November 2020.<sup>289</sup> The survey covered a broad array of themes related

<sup>&</sup>lt;sup>288</sup> Another key reason for not including thresholds in this type of setup is probably that conjoint designs are notoriously sensitive to the number of attributes included, as too many lead to cognitive overload on the part of the respondents. They will tend to find sub-optimal cues to get through the survey quicker, i.e. focus on their preferred levels (scores) on one or two key attributes, instead of evaluating the joint 'quality' of the whole reform package. The authors feature seven attributes in their design (six tax bracket rates plus the revenue estimate), which is already a high number, and adding six more (a new threshold for each bracket) probably creates an unmanageable comparison task for most survey respondents.

<sup>&</sup>lt;sup>289</sup> Respondents were quota-sampled to achieve representativeness in terms of gender, age, and geographical region, which is a set of socio-demographic variables that is used in most surveys. This approach is inferior to the gold standard of random sampling, as Epinion's pool of self-selected respondents may differ in meaningful ways from the general population, and the overall accuracy of the data relies heavily upon the correctness of survey weights. However, Ansolabehere and Schaffner (2014) have shown that conducting online surveys in this way yields similar coefficient estimates and total survey error compared to traditional telephone and mail interview. Further, details on representativeness are typically less important when the primary goal of the survey is to inspect differences in experimental treatments (i.e. reactions to a stimulus), as long as the experimental groups do not differ, rather than a situation where we need to obtain perfectly unbiased estimates of a population parameter of interest.

to taxation policy, but the cornerstones were two survey experiments centered on the top marginal income tax rate ('topskatten').<sup>290</sup> As noted in **Chapter 7**, it is a well-known and politicized tax. The central Danish income tax schedule is a two-tier system with a bottom rate of 12.11 percent (in 2020). The additional top tax rate of 15 percent applies to all taxable wage income above 531,000 kr. (in 2020), equivalent to around €71,000. In 2019, about one in five taxpayers in Denmark working full time reached this threshold.

The experiment was set up to assess the extent to which support to a reform proposal that alters the top tax is affected by (1) the type of policy change and by (2) the partisan affiliation of the person drafting the proposals. Let me be more specific. The survey presents two fictitious policy proposals in sequence: a proposal to alter the threshold limit of the top tax bracket (i.e. the 531,000 kr.), and a proposal to alter the rate (the 15%). Including proposals for both instrument types satisfies the third criterion. The variation in responses across the two experiments is thus a token that voters react differently to the two types of instruments.<sup>291</sup> The specific experimental conditions for each experiment, i.e. the content of the policy change, incorporate two dimensions. The first is a simple sign for the direction of change, i.e. whether the threshold value or the rate is (1) cut or (2) raised, hereby exploring the possible asymmetry between 'gains' and 'losses'. Though the crux of the dissertation is the 'cuts domain', we need, in my view, the other half of the equation to establish a reference. The second dimension is a marker of the degree of change. In operationalized terms, I include treatments that asked respondents whether introducing a (1) 'change' or a (2) 'significant change' affects their propensity to support a given reform proposal, with the expectation that a high proportion of voters are less likely to express support, if the bill is flagged as a largerthan-normal change from the status quo. This yields four treatments for each instrument. Using the rate as the example, they are a treatment to (1) lower the rate; (2) lower the rate *significantly*; (3) raise the rate; and (4) raise the rate significantly.<sup>292</sup>

<sup>&</sup>lt;sup>290</sup> The full questionnaire for the survey can be found in **Annex A.10**.

<sup>&</sup>lt;sup>291</sup> The order of the two experiments (thresholds and rates) is randomized for each respondent to eliminate any bias stemming from the question order. As I elaborate in this chapter's results sections, there is generally no indication that such order, and hence a prior priming, affected answers significantly.

<sup>&</sup>lt;sup>292</sup> The distribution of the assigned treatments, i.e. the number of respondents exposed to each, does not have to be equal. An equal split requires a one-fourth division between them. Due to my larger interest in tax-cutting phenomena, I employ a slightly skewed distribution of treatments to the cuts scenarios for each instrument, with a 60-40 percent split, to boost statistical power here.

One can question the decision not to include even more fine-grained treatments for the size of policy change, perhaps even add specific policy information, e.g. a 1, 2, 5 or 10 percent top tax rate cut, to inform us if or when the marginal decision to support a reform proposal switches. The decision was abandoned due to the issue of statistical power; do we have enough observations to detect a true treatment effect?<sup>293</sup> Given the sample size, the minimum detectable effect between treatments was calculated to 4 percentage points (in rounded numbers), if the experiments kept the four treatment groups, as suggested, and we accept a power of 0.80.<sup>294</sup> If the number of groups doubled, for example, the minimum detectable effect would be around 6.5 percentage points for the same level of power, which is a rather large effect size for experimental conditions. It is thus unlikely that we would even pick up such subtle effects driven by this higher number of treatments. I have therefore sought to keep the experimental conditions generic in their formulation, i.e. looking at cuts and hikes as such, but still clearly distinguishable in their content.<sup>295</sup>

Further, I attach a partisan messenger to the fictitious proposals for two reasons. First, it provides, in my view, a more authentic presentation of the reform bid as not just a random policy idea but something that politicians can realistically propose within a political discussion on taxation. Second, it allows us to test whether a Right partisan cue affects voter reactions to specific reform proposals, whether it is in a positive or negative direction in terms of support. It references, of course, a much wider literature on the impact of partisan cues. To keep it simple, I rely on three messengers: (1) a politician from the Liberals (the major Right party in Danish politics); (2) a politician from the Social Democrats (the left-wing counterpart); and (3) an unspecified politician, a 'neutral' messenger. By focusing on messengers from the mainstream political

<sup>&</sup>lt;sup>293</sup> *Power* is defined as 1 minus the probability of making a type-II error (not rejecting  $H_0$  if  $H_0$  is in fact false).

<sup>&</sup>lt;sup>294</sup> The power calculations were premised on a baseline effect of a 25 percent proposal support (or 0.25 if expressed as a proportion) with a group variance that matches that proportion size (0.1875), an assumption of statistical power ( $\rho$ ) of 0.80 (it is often convention to set  $\rho$  to 0.80 or 0.90), and an uneven sample distribution (60-40) between the cuts and hikes treatment groups, as previously discussed.

<sup>&</sup>lt;sup>295</sup> There is something to be said for the ecological validity of such "treatments", since real-life tax policy changes, as we have seen, are most often lumped into major legislative packages that may contain policy instruments outside the income tax domain. Similarly, tax reforms frequently can hold tax cuts and tax hikes for different instruments in the same package, not just a single-measure change. It is a fair criticism. However, we must walk before we can run. We must first understand the constitutive effects of the single instruments before exploring any combined effects on electoral support.

parties in Denmark, it provides a harder test for finding any effects of partisan cues, if we had chosen niche parties or the (smaller) parties at the extremes on the Left-Right scale. I prefer to use the term 'politician' as an individual to 'parties' as collective, since it relaxes how strictly we can match the messengers with policy content. Some combinations of treatments mesh less well in terms of real-life credibility, i.e. steep rate cuts proposed by a left-leaning politicians, but having them come from a single member of the party rather than from the party itself makes a noticeable difference in terms of believability, as we frequently see politicians propose new policy that is outside the traditional party lines.

The experiment for the top tax threshold thus took the following form:

The next questions concern *your* view on the income tax.

Politicians have different views on the income tax. The discussion often concerns the *top tax,* which is a 15 percent extra tax on income above 531,000 kr. (in 2020) after labor market contributions.

**[partisan messenger]** has in a recent political debate argued that the *threshold* for the top tax (531,000 kr.) should be **[policy treatment]**. Do you agree or disagree with such a proposal?

Tapping into the feasibility of the different proposals, respondents were asked to list their support on a five-point scale: 'fully agree', 'slightly agree', 'neither agree nor disagree', 'slightly disagree' to 'fully disagree'. A 'don't know' response was allowed to signify political indifference or lack of knowledge.<sup>296</sup> A few points are worth noting here. The choice between the policy change and status quo should feature clearly in the responses given by those surveyed. Hence, I made it a priority to define what the top tax is, precisely, to eliminate any myths surrounding the existing policy, and to make sure the respondents knew that the tax consisted of two policy parameters, the rate and the threshold.<sup>297</sup> My ambition was to get ahead of the 'weak knowledge' criticism, which

<sup>&</sup>lt;sup>296</sup> The formulations of the survey experiments were tested, beforehand, on a pilot sample of 267 respondents to see whether there was a high rate of drop-outs and don't know responses, which could indicate that the experiment was too complex for the respondents to grasp. However, these figures were in no way alarming.

<sup>&</sup>lt;sup>297</sup> To reduce such biases further, the survey featured a so-called 'knowledge test' on Danish taxation rules asked directly prior the survey experiments to familiarize respondents with the workings of the tax code or simply brush up on their knowledge. The test consisted of seven true/false statements on income taxation, including three specific for the top tax. After the respondents had given their answers, the correct statements were explained to them to help them prepare for the survey experiments. Hence, they were presented with a significant learning opportunity before having to

will inevitably be directed any survey that looks at tax preferences. We can thus expect that disagreeing with a proposal reveals a relatively clear preference for keeping these parameters at their current levels, when the alternative is to change one of them. Flagging the attraction of the status quo in this way differs from the previous accounts where respondents are essentially to design their preferred tax system from scratch, but it is, in my view, more consistent with the way new policy is typically judged; does the proposed change improve or worsen the existing policies that are in place?

After stating their support to each experimental proposal, respondents were tested on the visibility proposition, the key element of the experiments. The respondents were more specifically tested on their ability to identify the 'true' causal effect, i.e. how raising or lowering either instrument affects the level of income taxes paid by a taxpayer liable to the top rate. In my view, the operationalization meets the Piersonian understanding of visibility as voters being able to reconstruct the causal chains of the (unpopular) policy if they are to exact retribution, i.e. where the relation between the voter and the policy is central. As laid out in **Chapter 2**, we must expect a proposal to lower the top tax rate or to raise the top tax threshold to *lower* tax burdens on the richer taxpayers, and vice versa.

The follow-up question for the threshold experiment was worded as follows: 'Imagine a **wage earner** who pays the top tax on her personal income. Would the proposal to **[policy treatment]** the *threshold for the top tax* mean ...?'. Answer categories: the wage earner pays [more/the same/less] income tax going forward. This part of the experiment is very simple in its structure, as the treatment only differs with respect to its policy direction (cut or hike)<sup>298</sup> and instrument choice (rate or threshold). I made sure to align the treatment conditions across the survey questions, so the same treatment would be used for the question measuring support and the one measuring visibility, to avoid confusion and keep the stimulus clean. For all respondents, I simply coded whether they were able to identify the 'true' causal effects, given the experimental conditions, via a binary response (1 = true interpretation).<sup>299</sup>

gauge the experimental policy effects. The respondents got an average of 3.86 statements correct of the seven, and scores from 0 to 7 were generally normally distributed. 5 percent of respondents got zero statements right, while 5 percent got all seven right.

<sup>&</sup>lt;sup>298</sup> I do not distinguish between the sizes of the proposed policy change here, as it does not affect the direction of the causal change in the tax liabilities, i.e. *more* or *less* income taxes, not *how* much more or less.

<sup>&</sup>lt;sup>299</sup> For the proposal to lower the top tax rate or to raise the top tax threshold, the correct response was, of course, that the taxpayer paying the top tax would pay *less* 

**Figure 27** provides a basic overview of the survey structure. Since I also wish to gauge the impact of voter ideology on proposal support, the analysis relies on one of the most used ways to measure ideological position in the literature, Left-Right self-placement on a ten-point scale. 86% of the respondents chose to answer this question. To obtain relatively unbiased estimates of ideology, these analyses include a set of common demographic and economic factors that may explain ideology as well as proposal support: sex, age, education level, employment status, level of tax knowledge, trust in politicians, personal income (in deciles), top tax status, and partisan bloc affiliation. The operationalization of the controls can be found in **Table 27** in **Annex A.X**.

Figure 27 Brief overview of the survey structure



**Notes:** The survey themes as shown in ascending order from when they appear in the survey. The 'white' themes are essentially unrelated questions to the experiments as such, while the 'light grey' themes, in turn, are related. The follow up questions to the experiments on the policy effects and the proposal's believability are referenced, more specifically, in the results sections.

income taxes. For the proposal to raise the top rate or lower the top tax threshold, the correct response was *more* income taxes.

The respondents were, of course, randomly assignment into treatment groups, making sure the groups were similar in every way, including in ways that we cannot easily observe or measure. This includes their baseline support for different types of tax reforms and ability to grasp their policy consequences. Hence, the random assignment eliminates any selection bias (Angrist and Pischke 2015: 15-16). A *balance check*, comparing sample averages for the treatment groups across covariates, confirms that the randomization was successful, as the group differences are non-trivial across the key variables sex, age, education type, employment status, trust in politicians, level of tax knowledge, income decile and whether the person currently pays the top tax. It boosts our confidence that the groups are equalized across all non-treated potential outcomes. The full balance check across treatments groups and size of the individual groups can be found in **Table 28**, **Table 29** and **Table 30** in **Annex A.XI**.

## 8.3 Exploring the visibility and feasibility of instrument choice

Let us now dive into the results. Based on these experimental data, we can prove that thresholds are more difficult to comprehend than rates in terms of visibility, and that they are the less unpopular way of cutting income taxes at the top of the income distribution.

**Figure 28** displays the visibility of each proposal, simply measured as the share of respondents who are able to identify the true policy consequences for a taxpayer paying the top tax (*y*-axis), broken down for each of the four main treatment groups and the associated 95% confidence intervals for each instance. The left half of the figure thus contains the two threshold conditions, and the right half holds the two rate treatments. All are estimated via logistic regressions that employ robust standard errors. Given the setup of the survey experiment, results are best illustrated via figures. Here and below, I discuss a set of post-estimation plots, while the tables illustrating the underlying logistic regression results are relegated to the appendixes.<sup>300</sup>

Several observation are noteworthy when inspecting the figure. First, the visibility difference stands out clearly. The predicted shares for both threshold treatments lie in the fifties; 57% correctly say that raising the top tax threshold entail *less* income taxation for high-wage earners, while 53% note that lowering the threshold means the taxpayer will pay *more* income taxes going forward. This difference between them is significant at a 0.1 level. What explains

<sup>&</sup>lt;sup>300</sup> The full regression estimates behind **Figure 28** be found in **Table 31** in **Annex A.XII**.

this slightly lower rate of successful guesses may be the non-intuitive interpretation, as I have touched upon before; a negative change in the treatment condition (lowering the threshold) produces a positive change in outcome of interest (tax liabilities). Contrast this to raising the threshold, where a positive change in X generates a negative impact on Y. This explanation seems perhaps a little too peculiar, but in my estimation it is something habitual in the way we usually interpret relationship between variables that takes the form: "the more of X, the more or less of Y", and seldom starting with "the less of X". Figure 28 shows, secondly, that the visibility shares for the rate treatments lie around 70 percent; 71% for raising the rate and 68% for lowering the rate.<sup>301</sup> This is, of course, the key comparison according to the theoretical argument. The difference in successful guess rates, compared to the threshold treatments, is thus 13 and 15 percentage points for the proposals to either lower or raise the tax parameter in question. In my view, it is a staggering effect size given that the choice of instrument is the one component that varies across the sub results.302

There are obviously different paths to achieve this variation in terms of survey responses. One possibility is a variability in lack of knowledge across the two set of instruments, which should then be reflected in the share of 'don't know' answers relative to the successful causal interpretations. Another option is a difference in the share of responses that are plainly wrong, i.e. false causal interpretations of the treatment effects. Whereas the former reflects a lack of competence (or willingness) to engage with policy proposal, the latter

<sup>&</sup>lt;sup>301</sup> This difference is not statistically significant at conventional levels.

<sup>&</sup>lt;sup>302</sup> One could wonder whether the order by which the experiments were presented to the respondents (threshold first or rates first) affects the rate of successful guesses, since they offer causal interpretations in opposite directions. It may cause (further) confusion on the part of the respondent, who must adjust their mindset to this new policy direction on the fly. There is only partial evidence to support this view. For the threshold experiment, the share of true interpretations falls to 48% for the 'lowering thresholds' treatment when the *rate* experiment is presented first, a difference significant at the 0.01 level. Interestingly, the share for the 'raising thresholds' condition is unaffected by the experimental order. In the same vein, the share of successful guesses increases to 75% for the 'raising rates' treatment when the rate is first (significant at a 0.05 level), while the share for the 'lowering rates' condition is not affected by the same influence. See Table 32 in Annex A.XII for the full regression coefficients. It is not easy to provide a coherent explanation to this pattern. One possibility may be that two tax-cutting treatments, the ones unaffected by the question order, are commonly occurring in the Danish political debate, as we have seen in previous chapters, whereby this specific tax knowledge may be more settled and less frail to crisscross stimulus.

expresses qualities on the part of the specific instruments, which make them inherently more or less difficult to interpret. Studying the numbers in depth, the evidence lends credence to a visibility mechanism. Comparing the two taxcutting treatments – raising the threshold and lowering the rate – the share of respondents who answer 'don't know' is virtually the same; 15% for the threshold and 14% for the rate. It is, hence, not the major source of variation that drives the findings in **Figure 28**.

**Figure 28** Successful identification of the true causal interpretation for each proposal



#### Source: Own survey.

**Notes:** See **Table 31** in **Annex A.XII** exact regression coefficients. Lines indicate 95% confidence interval. Success guess is operationalized as the share of respondents who correctly whether a wage earner paying the top tax rate would pay less, the same, or more in income taxation following each proposal.

Neither are the groups answering that a wage earner in the top tax bracket would pay 'the same income tax' going forward, which reflects an inability to link the change in instrument to change in tax liabilities, whether positive or negative, for those affected. These shares lie between 10% and 11% for both stimulus treatments. The largest gap persists for those who simply get the policy consequences of the treatments wrong. For the threshold treatment, 16% of respondents mistakenly believe that raising this parameter leads to more income taxes in the future, whereas the same error rate is just 8% for the 'lower rate' treatment. The picture is even more pronounced for the treatments of the opposite policy direction; 21% of respondents predict that lowering the threshold leads to less income taxes, while 7% make the opposite mistake for 'higher rates'. The type of instrument clearly makes an interpretive difference on the parts of voters.

The main story is, hence, the difference in responses across the instruments, rather than the 'absolute level' of visibility reflected in the respondents' answers. It is not easy to say whether the shares reported in Figure 28 are the true point estimates for the population of voters. On the one hand, we must expect that the levels reflect attentiveness to the survey experiments in some capacity, as some respondents may have adopted answer strategies that reduce the cognitive engagement required to answer the questions correctly (and sincerely).<sup>303</sup> For example, the relatively high shares of 'don't know' replies may conceal a group of respondents with the ability to answer these visibility tests correctly, hereby deflating the sample estimates of the 'true' population parameters. On the other hand, the simplicity of the survey design should have done plenty to boost the share of successful responses. Respondents were not asked to calculate any specific effects of the cut or hike in question but merely to get the overall direction of the causal mechanism right. Second, we need to bear in mind that respondents were not simply put on the spot to deliver 'cold answers' without a prior introduction to the policy context. Rather, as a result of the specific priming text before the experiment of what the top tax is as well as the knowledge test on Danish taxation earlier in the survey, the respondents were given ample information about the workings of the tax schedule. Especially one statement informed them how to interpret tax payments that stem from the top tax, namely that taxpayers with the highest incomes pay the top rate only on income above the top tax threshold.<sup>304</sup> This piece of information makes interpretation of the effect of a higher or lower threshold limit much clearer. It is possible that the shares of successful answers would have been lower if not for these simple treatments and priors, and the visibility gap between the threshold and the rate in **Figure 28** larger.

Which factors drive the ability to identify correctly the true causal effect at the individual level? The question is explored in the supplementary analyses, which regresses whether the respondent guessed correctly on the experimental conditions and demographic and partisan covariates. The separate models for the threshold and the rate, respectively, are found in **Table 33** in **Annex A.XII**. These results suggest that demographic factors such as age

<sup>&</sup>lt;sup>303</sup> For instance, respondents may have chosen an easier option (such as a 'don't know' reply) or simply filled in answers at random.

<sup>&</sup>lt;sup>304</sup> The question wording was: 'On which range of the income is the top tax paid?' with the following answer categories: (1) Persons with the highest income pay the top tax on <u>all of their personal income</u>; (2) Persons with the highest income pay the top tax on <u>the amount which lie above the top tax threshold</u>; and (3) Don't know.

(positive effect) and education length (positive effect), as well as personal income measured in deciles (positive effect) predict the respondent's ability to identify the correct causal mechanism of each proposal. Interestingly, partisan factors such as political bloc affiliation and Left-Right self-placement do not affect the success rate. The respondents' generic tax knowledge, measured via a sum index constructed from the seven true/false questions on the Danish income tax code, correlates, not surprisingly, strongly with the ability to guess correctly. Those who identified zero true statements in the knowledge test had a 48% probability of guessing the true causal effect in the rate experiments, while those who identified all seven statements had an 86% probability.

We shelve the discussion on visibility for a moment and turn to the other key instrument quality, namely the feasibility of the policy change. Figure 29 shows the estimated support for each of the eight proposals under consideration; the four threshold treatments in the upper half of the figure (both policy directions times the two sizes of policy change) marked by black circles; the four rate treatments in the lower half marked by grey triangles. Asterisk marks proposals where the policy instrument in question was raised or lowered significantly. There is a lot to unpack in the figure. First, the results seem to confirm the expectation that proposals to alter the top tax do not attract widespread electoral support in the Danish case. None of the percentage tallies are anywhere close to numbers where we would say that an overwhelming share of respondent, in fact, supports the idea. The most popular policy of the eight, operationalized as the share of respondents who 'fully agree' or 'slightly agree', was the proposal to raise the top tax threshold, with 38% estimated support. Again, it is hardly a number one would deem as a straightforward vote-winner. As the figure demonstrates, merely tuning up the size of the policy change, adding 'significantly' to the proposal, causes the support to drop 8 percentage points. In fact, supplementary analyses show that when respondents were asked to list their support or opposition,<sup>305</sup> all but the policy to raise the top tax threshold<sup>306</sup> received more opposition than support. Hence, for seven of the eight proposals, a larger share of respondents prefer the policy status quo to change. The results are thus indicative of a hierarchy of solutions in terms of popularity. If one seeks to *cut* income taxation at the top end – disregarding for now which policy goals (Right) politicians wish to promote via their tax policy, and which means are most effective to do so – the proposal to cut rates achieves the least support relatively speaking, with an estimated support at

<sup>&</sup>lt;sup>305</sup> Those who 'fully disagree' or 'slightly disagree' with the proposal.<sup>306</sup> More precisely, 33 percent of those sampled oppose this proposal.

around 30% (just 23% if the rate is cut significantly).<sup>307</sup> This confirms our immediate theoretical presumption from **Chapter 4**.



Figure 29 Estimated support for each treatment

### Source: Own survey.

**Notes:** See **Table 34** in **Annex A.Xll** for exact regression coefficients and predicted probabilities. Lines indicate 95% confidence interval. Support is operationalized as the share of respondents who "fully agree" or "slightly agree" with the proposal. The asterisk \* means that the policy change *notice-able* according to the experimental condition.

A bit surprising to this writer at least, the support for all types of proposals is generally not affected by the second set of experimental conditions, the political sponsor. Attaching a partisan label does not alter support for the threshold proposals in any significant way if we study the one-way main effects of this variable (see **Table 35** in **Annex A.XII** for the full results). When it comes to lowering tax rates, in particular, we find a positive effect of right-wing affiliation (a politician from the Liberals) over the left-wing reference that is also associated with a substantial difference in the baseline support.<sup>308</sup> One reason

<sup>&</sup>lt;sup>307</sup> As evident in **Figure 29**, the least popular of all proposals were those aimed at lowering the top tax threshold, as the share of support plummeted to around 20 percent here. One explanation, which I back up with numbers below, is that Danish voters would not expect policymakers on the Left or the Right to make such proposals in a political debate, contrary to the six remaining, giving them a sense of unfamiliarity that probably detracts support.

<sup>&</sup>lt;sup>308</sup> The marginal support for the right-wing partisan sender is 32 percent compared to 22 percent for the left-wing messenger and 26 percent for the neutral sender.

may be that voters generally find such proposals much more believable coming from a Right party. The survey did tap into this notion empirically in the follow-up questions to the survey experiment. If the proposal sponsor was partisan, then a question was asked that that specifically gauged the likelihood that the proposal in question could come from the party the particular politician represented.<sup>309</sup> The results show that a whopping 73% of those surveyed find it likely that the Liberals would propose to lower the top marginal tax rate compared to just 15% for the Social Democrats. The picture was virtually reversed for the proposals to raise the top marginal rate; here 54% saw it as a likely Social Democratic suggestion while only 26% would ascribe it to the Liberals.<sup>310</sup> Some of it may be driving this messenger effect, as it is clear that respondents interpret these treatments with the 'correct' partisanship in mind. In supplementary analyses, I attempted to predict proposal support as a twoway interaction between the proposal sponsor and the voters' affiliation to the Liberals to see whether this relatively moderate effect was mainly driven by 'loyal partisans'. Though there is a slight tendency for Liberal voters to follow their in-partisan cues more than if the proposals are attached other sponsors, the effect is not statistically significant across the treatments. For these reasons, I do not proceed further with this sponsor perspective here.

After having dealt with the two propositions separately, one might be keen to understand their fusion at the individual level; how do voters' abilities to comprehend the policy content affect their specific reform evaluations? It is a crucial intersection, if one wants to uncover to what extent the reluctant support for these policy changes are a function of unpopularity *per se*, as previously discussed, or of the limited knowledge on the part of voters. Though the distinction may appear trivial, it should certainly not be for policymakers contemplating reform; aiming for confusion among the voters when proposing new policy may be better than searching for outright opposition.

<sup>&</sup>lt;sup>309</sup> The complete wording of the threshold proposals was: "Do you consider it likely or unlikely that **[party of sender]** as a party would put forward a proposal to **[policy treatment]** the <u>threshold for the top tax</u>?" with answer categories 'very likely', 'somewhat likely', 'somewhat unlikely', 'very unlikely', or 'don't know'.

<sup>&</sup>lt;sup>310</sup> The full estimates for these likelihood assessments can be found in **Table 36** in **Annex A.XII**. Generally, these results reassure the face validity of the treatments. The tax-cutting treatments are generally deemed more right-wing, while the treatment for lower marginal tax rate is clearly left-wing. Finally, the treatment to lower the top tax threshold is confirmed as the odd one out, as voters do not find it particularly likely that the Social Democrats (39 percent) or the Liberals (29 percent) would generate such a proposal.

Based on my data, there is no doubt that a lack of grasp of the policy consequences is directly linked to weak policy preferences in general, or *indifference* to frame it more positively. It is the case across all experimental proposals. One way to operationalize indifference is to look at the share of respondents who answer, faced with the content of the tax proposals, 'neither agree nor disagree' or 'don't know', i.e. they do not take sides. Across the rate proposals, 30% of respondents gave indifference answers. However, the share was close to half (46%) for those who were unable to identify the correct causal mechanism of the proposals, compared to just 23% for those who guessed successfully. A closer look at the answer distribution reveals that it is, in fact, a spike in the share of 'don't know' answers that is driving this difference. It spikes from 3% to 19% when the guess on the causal effect goes from right to wrong. Many voters, especially those who are more ill-informed on tax matters, thus have real difficulties forming strong opinions about new policy suggestions.

This point can also be proven by studying the other side of the coin - howa better grasp of the causal impact is associated with stronger opinion formation with regard to policy content. With a key clarification, though. Theoretically, a larger share of non-indifferent answers can be consistent with more support to these proposals, more opposition, or a combination. Yet, the results show that this is unambiguously an 'opposition phenomenon'. The data show that respondents with and without a basic understanding of policy effects are almost as likely to exhibit the same level of proposal support, regardless of instrument choice and policy direction. As Figure 30 reveals, it is not the case when we measure opposition. The figure shows the predicted share of opponents for each of the four main proposal types under consideration<sup>311</sup> across the two groups – whether the respondents provided the true or false causal assessment - yielding eight models in total. The threshold proposals (T) are aligned to the left, while the rate proposals (R) are on the right. It is the withinproposal comparison we must pay close attention to here, and the differences are considerable to say the least. For the proposal to raise the top tax rate (the medium grey triangles), for example, the share of opponents is 44% for those who hold the true causal interpretation and only 23% for those who do not. However, it is a general trend, as evident from **Figure 30**. The general level of opposition may vary across the proposal types, but within-differences are pretty much the same; spikes in opposition shares between 18 and 21 percentage points. There seems to be a 'visibility impact' on attitude formation at both

<sup>&</sup>lt;sup>311</sup> The data are not split according to the size of the policy change here to keep the presentation of the results relatively neat.

the instrument level, as demonstrated by the results above, and at the individual level, where a weak causal understanding instills policy indifference, while a strong one generates opposition.

**Figure 30** Estimated opposition for each treatment moderated by voters' causal grasp



#### Source: Own survey.

**Notes:** See **Table 37** in **Annex A.XII** for exact regression coefficients and predicted probabilities. Lines indicate 95% confidence interval. Opposition is operationalized as the share of respondents who "fully disagree" or "slightly disagree" with the proposal. T is an abbreviation for *threshold limit*, R stands for *rate*. 'False' indicates those respondents that did not hold the correct causal grasp of how the proposed change affects the tax liabilities of someone paying the top tax. 'True' indicates the opposite.

### 8.4 Low visibility discourage partisan conflict

The visibility results in the last section is the key result of this chapter. The findings over the next short sections are related, exploratory analyses that try to take a look some of the immediate implications of this main finding.

The impact of visibility seems, first of all, also to apply to the role of ideology on proposal support, if we dwell more on the partisan drivers. Building on **Chapter 3**, we should expect that right-leaning voters are generally more inclined to support bills that would lower income taxes, especially on higher incomes as is the experimental case here. 'Right-leaning' can be understood through a lens of representation or affiliation to the parties on the Right, or, as laid out in the theory, through the ideological convictions that are typically ascribed to such parties. Here, I gauged the effect of the former by regressing the proposal support on the ideological self-placement of respondents from 0 to 10, with 10 being as 'Right' as possible, while controlling for potential confounders (see **Table 27** in **Annex A.X**). A positive coefficient thus means that more right-leaning voters are more likely to support the proposal in question than left-leaning voters, and vice versa.

Are such effects of ideology similar across the different proposal types? The answer is a definitive 'no' if we look at the models for the four policy types in Figure 31. The left-most panel contains the Left-Right estimates for the whole sample, displayed here as average marginal effects. We witness a clear, but somewhat surprising, pattern of results: support to the two proposals to cut income taxes at the top end (raising the top tax threshold and lowering the top tax rate) is associated with strong ideological divisions in the expected direction; right-leaning respondents are more inclined to support tax cuts. In substantial terms, the predicted probabilities from the 'lower rate' model suggest that the estimated support ranges from 10% to 47% going from the most left-leaning to the most right-leaning voters in our sample, a truly sizable effect.<sup>312</sup> If cuts and hikes worked in symmetry, we should observe the inverted picture in the results for the latter. Yet, it is not true as I hinted already. The effects of voters' Left-Right positions on the tax-hiking reform proposals are negative but statistically indistinguishable from zero. In terms of coefficient sizes, the ideology effect is smaller for both the threshold and the rate experiment by a factor of (about) 2.5 when comparing the hike and cut scenarios. The case idiosyncrasies of the Danish 'top tax' notwithstanding, it is a truly novel finding; the ideological effects on the part of voters are conditional, insofar as ideological divisions are 'activated' much more when the discussion concerns cuts at the top end rather than hikes. There is an asymmetry at play. The simple explanation is perhaps, in relation to earlier discussions, that voters simply hold stronger and clearer differences in their understanding of what a tax cut does – in terms of its effect on revenue intake, redistribution, and efficiency – compared to tax hikes.

Equally interesting, **Figure 31** also breaks down the results across the four models on the respondents' causal grasp in the middle and the right panel for those with a false and a true causal assessments, respectively. The results validate the importance of 'visibility' as a key moderator. Among the 'false'

<sup>&</sup>lt;sup>312</sup> The effect is substantial too, if we consider the more moderate comparisons of ideological position, as going from three to seven on the Left-Right scale produces a shift in the predicted support from 17 to 33 percent.

voters, Left-Right position is in no (!) experimental setting a significant predictor of proposal support at the conventional 95% confidence level,<sup>313</sup> and all effect sizes are curbed compared to the results for the total sample. It is striking – to this writer at least – that the Left-Right position, such evident markers of a respondent's ideological stance, can hardly explain any of the variance in proposal support for this large subgroup of 'weakly informed' voters.

**Figure 31** Average marginal effects of Left-Right self-placement on support for treatments



Source: Own survey.

**Notes:** Lines indicate 95% confidence interval. 'False' indicates those respondents that did not hold the correct causal grasp of how the proposed change affects the tax liabilities of someone paying the top tax. 'True' indicates the opposite.

The right panel shows that the effect of ideology is, in turn, augmented among voters with a better causal grasp. The average marginal effect is still the strongest when we look at cuts, though the negative coefficients for the hike treatments are now statistically significant, implying that rightist voters with more sophisticated knowledge – on average – are more likely than left-leaning voters with similar knowledge to oppose the tax-hiking proposals. The effect sizes are remarkable too. If we take the strongest effect in absolute terms, once again the 'lower rate' model, the estimated support jumps from 9% to 51% when comparing a zero and a ten on the Left-Right scale. Working with electoral data, it is rare to find one variable that can 'move' the support towards

<sup>&</sup>lt;sup>313</sup> The average marginal effect for 'lower rate' model is significant, though, if we apply a 0.1 significance level.

any type of policy change more than 40 percentage points, even though it is starting from a low level.

The visibility proposition manifests itself, therefore, both as a predictor of policy indifference in itself and as an interacting factor on more traditional explanatory variables of policy preferences such as ideology. However, the interrelation does make substantial sense; if voters cannot properly orient themselves in the consequences of a given (tax) measure, then ideology should only function as a weak cognitive anchor for judging such policy. A strong political compass such as the Left-Right self-assessment is only expected to function once the voter understands the actual mechanism behind the policy.

# 8.5 Ideology associated with conflicting causal beliefs – not just conflicting goals

We can next ponder in these additional analyses what differences in the underlying causal beliefs between the Left and the Right are driving these relationships (in **Figure 31**). For example, where do leftish and rightist voters exhibit a similar or a diverging belief system regarding the economic impact of the tax proposals? And how does visibility at the level of the individual moderate these assessments?

To explore such questions, the survey dug further into the reasons why individuals support or oppose each experimental proposal. These reasons were formulated as close-ended causal assessments that align with the main functions of taxes (see **Chapter 2**). More specifically, I gauged whether the respondent thought a reform proposal as presented would entail more inequality, more economic growth, worse welfare service and/or hurt the public budget balance.<sup>314</sup> The aim was *not* to test whether the respondents knew the textbook 'econ answer' to these questions but to see how different types of voters link the policy proposals to such effects. Is there, for example, evidence of

<sup>&</sup>lt;sup>314</sup> The question battery was formulated as follows: 'One can use different motives to change the income tax. To what extent do you think the proposal to **[policy treat-ment]** the <u>threshold for the top tax</u> will contribute to ... ? (1) increase the economic inequality in society; (2) increase growth and employment in society; (3) weaken welfare benefits and services; (4) weaken the public budget balance.' The answer categories were 'not at all', 'to a lesser extent', 'to some extent', 'to a great extent', and 'don't know'.

a partisan way to interpret how much inequality lower marginal tax rates on income will generate?<sup>315</sup>

The empirical evidence seems to imply it. To demonstrate, I display the results for the proposal to lower the top marginal tax rate, specifically, as it is likely where we find the largest discrepancies in causal beliefs across the Left-Right scale, given the predictive power of the latter for the reform support of this type. Hence, to reduce complexity, results are not shown for all four treatments. **Figure 32** shows the share of respondents holding the particular causal belief<sup>316</sup> across the four kinds of possible effects mentioned: the inequality item in the upper left corner, the growth item in the upper right corner, the welfare item in the lower left corner, and the budget item in the lower right. The predicted shares are then, first, broken down according to the respondents' Left-Right position (from 0 to 10) on the *x*-axis and, second, split according to their grasp of visibility. The black line highlights the respondents with false causal assessments, as seen in the section above, and the red line signifies those with true assessments.<sup>317</sup> The dashed lines represent the 90% confidence intervals.

The estimates for the true guesses (red lines) generally reveal stark ideological differences between left-leaning and right-leaning voters. Three relationships are distinctly negative – the inequality, the welfare, and the budget items – while one – the growth item – is positive. The effects are substantial too. In the inequality graph, the predicted share of respondents expecting that a lower top tax rate leads to an increase in economic inequality at large is a whopping 79% for the left-most voters but only 41% for the informed rightmost voters. As noted, the picture is turned on its head for evaluations of whether cutting the rate induces economic growth and employment: 57% of right-wingers compared to 19% of left-wingers believe it is the case. The figure tells a similar story for the assessments of whether a lower rate leads to poorer welfare benefits and services and a worse balance between revenue and spending. It is, hence, not difficult to see why support to new tax proposals divides

<sup>&</sup>lt;sup>315</sup> Because the experiments were tilted towards investigating tax cuts, the survey arguments were formulated so they would align in the same direction as their expected effects, as per economic theory. One could have also chosen to flip the effects signs, e.g. whether the proposals would produce less inequality or less economic growth,

<sup>&</sup>lt;sup>316</sup> Here, I simply take the share thinking that the proposal would entail that particular policy effect 'to some extent' or 'to a great extent', i.e. contribute to this effect in a tangible way.

<sup>&</sup>lt;sup>317</sup> The models are estimated with an interaction term between Left-Right self-placement and a dummy for the false/true causal assessment.

according to ideology. The results seem to indicate that sufficiently sophisticated voters, at either ends of the political spectrum, disagree not only which policy goal to give more or less political weight, e.g. equality versus efficiency, but more fundamentally on what the policy consequences are. Based on the results, it seems fair to say that many rightist voters are blind to, or at least downplay, the fact that cutting the top tax rate may have unfavorable effects on inequality, social provisions, and the primary balance, while most leftish voters seem to neglect that a lower rate may actually boost macro-economic performance in a positive way. It is a different type of disagreement than trade-offs, because the Right side tends to spot the policy benefits only, while the Left is mainly preoccupied with the drawbacks.

**Figure 32** Share of voters holding specific causal beliefs as conditioned by Left-Right self-placement



#### Source: Own survey.

**Notes:** Lines indicate 90% confidence interval. 'False guess' indicates those respondents that did not hold the correct causal grasp of how the proposed change affects the tax liabilities of someone paying the top tax. 'True guess' indicates the opposite.

These conflicting causal beliefs are cancelled out when we look at the 'false guess' (black lines) estimates in **Figure 32**. Across all models, the coefficient for the Left-Right self-placement measure is indistinguishable from zero, reflected by the virtually flat lines. Again, visibility is a key moderator. For this

group of respondents, about 30% in the rate experiment, ideology does not predict differences in the particular types of causal beliefs they hold, which perhaps explains why the former is not a good predictor of support in this subgroup. What seems to be driving some of these insignificant results is, not surprisingly, a larger share of 'don't know' replies when it comes to evaluating the causal effects. For the inequality item, this share is 23% for the 'false group'<sup>318</sup> compared to just 7% for 'true group'.

### 8.6 Can we generalize the Danish reform case?

We must, of course, consider the external validity of these findings in a critical manner, as it is not immediately obvious to what extent they are generalizable across other types of tax brackets and in different country contexts. Studying the top income tax, as we have here, makes us ponder whether the same mechanisms (or lack thereof) can be found if the target of the experiment was a lower-placed bracket within the tax schedule, e.g. a bracket designated for low or middle incomes. The answer to this question is probably conditional. In terms of popularity, cutting taxes at the bottom is expected to yield higher levels of electoral support than cuts to the highest incomes, if for no other reasons than it would reap personal benefits to a much wider coalition, though this move should involve great fiscal costs. The logic should persist regardless of the specific instrument choice. When it comes to the visibility proposition, I see no good reasons why rates should not be the clearer instrument in terms of their causal interpretability, irrespective of the tax bracket's location. We have our theoretical arguments to support the claim. All three main parameters we expect to drive this visibility mechanism – the frequency of exposure, the direction of their causal effect, and the impact of political non-decisions are general to the rate versus threshold nexus and not tied to the specific cutoff value(s) of the threshold limits. The effects should extend to lower tax brackets too, though it is an obvious next step to substantiate this claim with further empirical evidence.

Returning to the spatial generalizability, one can ask which (other) countries have tax schedules that look like the Danish one, where the findings would be most directly applicable. This comparison has been a major theme of the dissertation to this point. To iterate, the top tax bracket in Denmark is more directly comparable to what we find in the other Nordic countries and Ireland and to some extent in the United Kingdom. As shown in **Figure 33**,

<sup>&</sup>lt;sup>318</sup> The same shares are 25 percent for the growth item, 29 percent for the welfare item, and 32 percent for the budget item.

it pertains both to the total number of tax brackets (*x*-axis) and to the placement of the income bracket (*y*-axis).



**Figure 33** The number of tax brackets and the placement of the top income tax bracket's threshold

Source: Own calculations based on OECD (2019b).

**Notes:** All values refer to 2018 data. Luxembourg and Austria are excluded from the figure due to extreme values on one dimension; Luxembourg with a much higher number of tax brackets (18); Austria with a very high ratio of threshold value divided by average earnings (22.9). Reference lines for the Danish position on each axis.

The Danish case is marked by the red circle, surrounded by the remaining OECD countries, and it is safe to say that it is not a 'typical' or 'average' case. The leftward position on the *x*-axis proves that the Danish top tax bracket is one of just two brackets in the schedule, whereas it would merely be 'one of many brackets' in the countries further to the right. It reveals, perhaps, that the top tax bracket takes a more transparent and prominent position within the tax codes of the former group. At the same time, the low score on the *y*-axis<sup>319</sup> shows that the top tax rate in Demark is relatively inclusive when it comes to the share of taxpayers liable to the top tax (sets in at 1.1 of AW).<sup>320</sup> This adds a dimension of comparison, where the Danish case can mimic the top tax bracket in countries like Belgium, New Zealand, and the Netherlands

<sup>319</sup> These results were shown, first, in Figure 4 in Chapter 2

<sup>&</sup>lt;sup>320</sup> The figure shows a relatively strong pattern, as countries with the fewest tax brackets feature the lowest threshold limits for the top income bracket. There is clearly large variability, though, in particular within the group of countries with a moderate or a high number of tax brackets.

(follow the horizontal reference line in **Figure 33**). Here, the thresholds for the top tax brackets are roughly similar, which may produce similar evaluations of reform support. One could contrast this to cases such as the United Kingdom (4.2 of AW), Germany (6.4) or the United States (8.1) where similar the equivalent type of policy proposals would target a much more confined segment of very rich taxpayers. In these countries, the best comparison with the Danish 'topskat' would probably be to study reforms of a lower-placed bracket that is closer to the national average earnings.<sup>321</sup>

A final note on comparability. We should mention that the Danish top tax is a special case in another respect; it triggers a huge jump in marginal tax rates compared to the rate paid on the next highest bracket. For the Danish schedule, this represents the 15 percentage point hike from the bottom to the top rate. It ranks second among the countries studied, only trailing Ireland (which holds a 20-point jump), and the difference is about 2.5 times larger than the cross-country mean of 5.9 percentage points.<sup>322</sup> How should this jump affect voters' reform evaluations? This may, on the one side, instill the view in Danish voters that there is generally larger room for cutting the top marginal tax rate while retaining steep (extra) taxation on the richest groups, generating a natural pressure for ironing out some of this difference. On the other side, the large current jump in marginal rates paid may serve to familiarize voters with a notion that it is both normal and preferable to tax the top income bracket at a much higher rate than those immediately below. In any case, the Danish top tax rate plays a much larger role for ensuring the progressivity of the income tax schedule than in most other countries, which serve only to reinforce its policy importance.

### 8.7 Conclusion

The conclusion of the chapter is simple enough. Instrument choice matters to the visibility of income tax policy change from the voter's perspective. This is shown via experimental treatments applied to the Danish top tax. The findings, thus, support the main theoretical contention of the dissertation of an added layer of politics to our discussion of instrument design which politicians might – or at least should – take notice of. The difference in visibility across

<sup>&</sup>lt;sup>321</sup> For example, the higher rate threshold in the United Kingdom was placed at 0.9 percent of AW in 2018 (1.2 before subtracting the personal allowance), which is essentially a much closer match to the Danish tax than for proposals to alter the parameters for the additional rate.

<sup>&</sup>lt;sup>322</sup> The full overview of rate shifts, across countries, from the next-highest bracket to the highest one can be found in **Table 38** in **Annex A.XIII.** 

the instrument types is present even after we prime the respondents with extensive information on the factual policies in place. As the more than 10 percentage point gap between rates and thresholds exists in in this rather simple experimental setup, where the respondent needs only to evaluate one moving piece at a time, there are good reasons to believe that this difference could be even larger in real-world settings where policy packages are a lot more complex. One dimension not considered in this chapter is the whole ordeal with regard to policy design. As highlighted in earlier chapters, one 'normal' mode of policy change when it comes thresholds (i.e. indexation) makes it even harder to judge whether high-income earners (in this case) are actually benefitting from higher nominal thresholds limits. This ambiguity may, of course, be preferable for Right that wish to cut income taxes, as very few tax policy proposals are not decidedly unpopular with voters.

My approach to uncovering tax preferences at the voter level is a novel one, as it is one of the first – to my knowledge – that actually taps into specific policy proposals, and which does not look at the 'wider' tax outcomes. Further, the survey tackles the issue with voters' alleged lack of tax knowledge head on, as it, first, sizes up the specific scope of the 'problem' across different instruments, and secondly inspects the impact of this weak causal grasp on attitude formation. As shown, we have a relatively large segment of voters that do not have a very good understanding of how tax policies work, and they are for the same reason rather indifferent when it comes to policy outputs.

## Chapter 9. Concluding remarks

The aim of this dissertation was to investigate the scope and types of income tax reform in the OECD from 2000 onwards. Income tax rules in advanced democracies are thus under constant change and a frequent topic of discussion among the political elites. They are important to get 'right', since the way policies are structured carries immense consequences for both the revenue intake of modern-day states and key societal outcomes such as inequality and economic growth. It is a topic that has naturally attracted the attention of economists (Steinmo 1998, Hakelberg and Seelkopf 2021b), concerned with setting the policy that strikes the 'optimal' balance between the conflicting goals, and their expert opinions are often inputs in the public discussions on these matters. Yet, anyone who has studied the tax domain to a slight extent is aware of the often large gap between the policy recommendations by economic scholars and what politicians then actually adopt policy-wise. To the great frustration of many economists. The trained political scientist has a good intuition as to why policymakers choose differently. Some of the 'possible' policy solutions may not align with their core ontological and normative beliefs of what the tax system should ideally do. Further, there are a lot of tax proposals that simply cannot yield support from a political majority, whether it is among voters or in parliament.

The dissertation dwells on these 'political causes'. It does so by providing theory-building as well as novel empirical contributions at the macro, the reform case and the voter levels. As revealed, it is not an easy task given that modern (income) tax systems are incredibly complex legal entities that do not come with an easy and instruction sheet on how we should ideally study them. My hope is this dissertation has proven that it is worthwhile for political scientists to dedicate a lot more of our collective attention to the politics surrounding taxation. By doing so, the dissertation contributes to research within our own ranks, which has been notoriously skewed towards the spending-side branches of the state. My work shows that we can not only transfer a lot of the rich concepts and theories from this extensive literature and apply them (in altered versions) on tax questions, but also that our understanding of spending issues is oftentimes incomplete if we do not account for the apparent revenue dimension that is underlying them.

With this dissertation, I join a relatively select group of political scientists that have focused on the tax issue whole-heartedly. It is clear we should seek to explain the drivers behind the vast country variation in tax outcomes and the relative burdens across different tax types, as a dedicated part of tax literature has already been doing. But we should care too about the specific policy choices that are made, because they are (a) often the true object of conflict at the level of policymakers, and because they are (b) ultimately linked to outcomes. There is significant room for improving our understanding of the latter perspective. In this dissertation, I have attempted to demonstrate what such type of analysis can look like if we take a look, specifically, at the income tax, the cornerstone of most, if not all, countries' tax systems. What I found can essentially be boiled down to four key conclusions.

First, we must understand that there are two cruxes to income taxation. The income tax schedule is as fundamental as any collection of policies on the tax-side, and policymakers setting the rules that govern this schedule must decide on two key sets of policy parameters: on tax rates, i.e. how much taxes must be paid, and on tax thresholds, i.e. who must pay. These concepts provide us with language to describe much of the spatial and temporal policy variance in the OECD. Both types of instrument can be used in independently as tools for cutting or raising taxes. Yet, their distinction is key because they are not functional equivalents. Not from an economic point of view, as the (marginal) rate is thought to foster the strongest behavioral responses. But even more importantly, I argue, they are very different political tools. Applying Pierson's (1994) visibility logic, the causal impact of changing tax rates is relatively easy to comprehend, while the interpretation of thresholds is murkier: the causal mechanism works in reverse (raising a thresholds entails lower taxation) and they are a function of constant changes in income levels. It is a proposition that is sustained empirically in a survey experiment among Danish voters. Looking at the design of income tax reform at the case level, we observe too that the instrument choice is of vital importance for how politically contentious new legislation is perceived by various stakeholders. In this way, the 'rules' of politics tend oftentimes to supersede what may be the preferred solution if these tax instruments had been more alike in terms of visibility.

Second, the trend of income tax policy across the OECD over the last 20 years has been one of nominal cuts. Formally, policies of today would have yielded a lot less revenue in 2000 all things equal. Much of this adjustment is 'necessary' to circumvent bracket creep, but it is still fundamentally a political choice to leave the political status quo, which by default would bring in additional revenue with rising wage levels. The reform patterns have, nonetheless, varied to a significant degree. Some countries have cut income taxes mainly by raising tax bracket thresholds, while others have cut income tax rates too. We find that the latter group – those countries have successfully cut income tax rates – are typically also those that have lowered income taxes as a whole the most. There are clear institutional imprints on these patterns: in countries

with few tax brackets, the long-term trend is not to cut rates, probably because it comes with greater political and fiscal costs in this setting. As the literature suffers from a lack of valid and meaningful policy-based dependent variables, these analyses of the aggregate policy level build on novel measures of the *rate effect* and the *threshold effect*, which I have constructed from the raw OECD policy data.

Third, the political Right is the key actor to study if we wish to understand the dynamics of income tax policies. They hold the most obvious share in this question and they are ideologically motivated by the 'virtues' of tax cuts, willing to pursue this ambition often *despite* the inherent economic and political costs. Cuts are not vote-winners, as they are costly in terms of foregone revenue, and because they typically have the effect of raising the level of post-tax inequality. Still, the Right has capacity to act, as the analyses have demonstrated. Right cabinets are, on average, a key driver of the largest tax-cutting reforms during this period, especially when the reforms mainly contain cuts the rate(s). It is, however, a 'selective' effect for the high-income segments, as a similar 'positive' effect cannot be found for those lowest on the income scale. If anything, the macro-findings are indicative, that Right elites are in some cases more content than their non-Right counterparts with enacting reform that actually raises income taxes on low-income wage-earners.

Fourth, the tax strategies of the Right are quite heterogeneous across institutional contexts. I argue, more precisely, the typically mode of reform is shaped by the composition of the income tax schedule. The two central factors - the number of tax brackets and the progressivity of the schedule - guides the instrument choice and the Right's political priorities, respectively. This means that the Right faces the least constraints when both institutional factors are 'high', as the Right then have a lot of potential instruments to target and a strong incentive to cut taxes on the high-income groups. In contrast, when there are few tax brackets and low progressivity to begin with, the Right should typically resort to reforming the tax thresholds, which is politically safer, and spread their tax-cutting efforts across the income scale. I find evidence to support these institutional claims. Both when looking at the long-term macro paths across the OECD, but the mechanisms are also grounded with case study findings from tax reforms in Denmark, the United Kingdom, and the United States. Showing how the Right navigate the politics of income taxation across different institutional setups has hopefully given the reader a more profound understanding of the diverse reform tracks we have witnessed across the OECD in recent years, and the findings seen here should make us confident that we are able to find the similar traits in right-wing strategies across a larger number of country studies.

The conclusions of the dissertation carry strong relevance for the taxation literature, as well as the neighboring literatures on partisan politics and public policy. The findings can serve to inspire with new research ideas on multiple fronts, and I will encourage those interested to join the 'tax cause', as it is still a club looking for more members. My humble hope is that the dissertation has left the reader with a more nuanced understanding of the policy change that has transpired within the income tax domain, and all the politics involved with setting these policies. And persuaded you that we need to analyze the cause(s) as an interplay between specific instrument qualities, partisan actors and tax legacies.

I will end the dissertation by elaborating on some of the broader implications. As noted, the findings should serve as a call for revising the way we generally study the state's tax-side and spending-side. We should at least try to equalize some of the uneven attention devoted to the two. For example, scholars interested in knowing how parties attempt to redistribute from rich to poor or provide protection against social risks via welfare state policies cannot paint the full picture of such efforts without taking into consideration what happens with taxation at the same time. It is of obvious importance when looking at grand-scale questions such as the rising income equality across the Western world since the 1980s. Here, it has been largely a failure of tax systems, rather than of social policies, to offset the increases in market equalities that explains this particular outcome (Caminada, et al. 2017). But the integration must extend to the policy-side too. Further, we can find a lot of examples of policy reform packages, as evident for the **Chapter 7** case studies, which contain a mix of tax and welfare measures. This linking is especially obvious in countries where tax rules are set in relation to yearly budgets. On this front, a lot more can still be done in terms of integrating taxes and spending more explicitly in joint frameworks in future research.

Similarly, we should recognize that the sides feature mirrored logics to some extent. In the welfare state literature, the notion of 'dismantling by default', a way of eroding the generosity of social benefits by essentially doing nothing to sustain them (see e.g. Lindbom 2007, Bauer and Knill 2012, Green-Pedersen, et al. 2012), has been mentioned as one prominent strategy where policymakers through the programmatic design can pursue hidden or indirect retrenchment. In a nutshell, the default favors those critical of generous social provision. The picture is essentially reversed when we gauge the tax-side, as we have seen. Since thresholds are fixed to monetary amounts too, the failure to raise them in line with rising wage levels leads to 'tax hikes by default'. It is a mechanism, as we have seen, that hits especially those that hold a disproportional share of the (income) tax burdens to begin with. This difference of the default creates, needless to say, uneven incentive structures across parties on the Left-Right scale, and from this view it is easy to understand, why parties on the Left are so keen on continuously 'expanding' social provisions, while parties on the Right must actively cut taxes to avoid them from rising. Those are key ground rules to be aware of when analyzing either side.

## 9.1 The Right dilemma between simplicity and room to maneuver

Speaking of parties, the dissertation has done plenty to hint at some of the dilemmas and trade-offs involved with setting the 'Right' tax policy. One thing is to strike the balance between revenue, redistribution and efficiency, where the Right due to ideological reasons will often prioritize lower and flatter income taxes. Another equally important balance is the one between the pure economic considerations and the political costs, as I have argued. The pursuit of tax cuts, especially at the top end, is a risky strategy for the Right parties in power as the left-wing opposition expectedly will use the opportunity to criticize the distribution of these cuts and frame the idea as a bad deal for the majority of taxpayers. Also, the Left will make the Right come up with good reasons as to why they would choose to prioritize revenue for cutting taxes over social spending. With electorates not tilting in favor of tax cuts over more spending, as seen in **Chapter 4**, it demands a committed effort from Right to go after the former. The macro results (in **Chapter 6**) confirm that the Right still pursues cuts to a significant degree, which speaks to the level of their dedication for lower income taxes: they pursue them *in spite of* the political risks.

It is clear that the dissertation does not iron out all of the wrinkles related to this puzzle. One thing not baked into my comparative theory is a more elaborate explanation of the different ways the Right handles the immediate fiscal costs stemming from cutting income taxes. The three case studies are indicative of as many approaches. In the Danish case, income tax reform was partly financed via tax hikes, partly by drawing resources from the government's *economic leeway* ('økonomisk råderum'), i.e. its projected future revenue streams stemming from the general growth of the economy. Essentially, this is to earmark the use of such revenue for tax-cutting purposes instead of using them for spending increases. In the UK cases, the Conservative-led cabinets, situated in the midst of great economic crisis, chose the harsh 'austerity' route. The government combined their ambition for fiscal orthodoxy and lower income taxes by not only putting a lid on spending, but the Tories actually cut real expenditure to a significant degree.<sup>323</sup> Yet, Conservatives still found a way to cut income taxation in every budget they presented. The US case is too a peculiar one. Despite of the stated Republican goal of *not* increasing the budget deficit and the debt, the Trump tax reform would be financed exclusively by adding to the projected long-term debt. What seemed to be the only thing reigning the tax-cutting Republicans in was the \$1.5 trillion debt limit set in their own budget reconciliation, as former versions of the reform plan had the debt increasing manifold in the long-run. It is puzzling to what extent Republicans disregard the notion of fiscal responsibility, as hardly any 'trickledown' Conservative could convincingly argue that this package would 'pay for itself', even though several key Republicans did just that publicly (Insider 2017a).

The US case stands out even more, if we take a look at government deficits more broadly in the OECD. **Figure 34** compares the government deficit in the United States (black line) to 15 OECD economies (grey lines) after 2000. What stands out is the US consistency; in virtually all years since the early 2000s, the American government has run among the largest budget deficits comparatively speaking. Both in boom and crisis years. Bear in mind, it is a period with a Republican president in the White House for the majority of time ('01-'09; '17-'21). As a result, the US government debt increased from 75% of GDP in 2000 to 136% in 2018, almost doubling in relative size.<sup>324</sup>,<sup>325</sup> The question is whether the case of US fiscal responsibility is a *sui generis*. The EU

<sup>&</sup>lt;sup>323</sup> According to the OECD datasets on government expenditure, spending dropped about 2 percent in real terms from 2010 to 2018, and especially took a plummet during the coalition term from 2010 to 2015, the top of the crisis, where real spending fell 6 percent from the 2010 baseline.

<sup>&</sup>lt;sup>324</sup> Though the US debt levels have surged, markets have generally not shied away from buying US bonds, rendering (new) borrowing historically cheap (The-Atlantic 2020). What is more interesting for this dissertation is, of course, the politics surrounding the debt question. Here, I can merely observe that getting serious about deficit reduction, by cutting spending and raising taxes (or at least not cutting them), has not been the politically profitable strategy of Republicans over the last 20 years. At least during Republicans presidencies. Instead, the strategy pursued look a lot more like 'starving the beast', i.e. by cutting taxes enough to deprive the federal government of revenue in a deliberate effort to force it to reduce spending.

<sup>&</sup>lt;sup>325</sup> In the US, spending cap rules have actually been tried, yet never strictly enforced. For example, Congress enacted discretionary spending caps In August 2011, aimed saving about \$900 billion over a decade. As a result of the failure to adopt a comprehensive deficit reduction plan, additional spending cuts (the so-called 'sequester') came into effect in March 2013. These additional cuts, if not repealed by Congress, would have produced savings of \$1.2 trillion over a decade, with one-half coming
member states of the OECD, for example, have had their fiscal autonomy severely constrained, as they comply with the Maastricht criteria that limits deficits to 3% of GDP. With the Fiscal Compact (2012/2013) these rules included reinforced monitoring and enforcement procedures of member states running excessive deficits. When enforced, it of course puts an effectively lid on the political Right's ability to cut taxes on a large, unfunded scale. In any event, there is plenty of room for future research to investigate this conundrum in further detail: how are income tax cuts specifically financed by the Right, and what causes the variation in such fiscal strategies?



Figure 34 General government deficit as percentage of GDP, 2000-2018

#### Source: OECD (2021a)

**Notes:** The benchmark countries are Australia, Austria, Belgium, Denmark, Finland, France, Germany, Iceland, Italy, Luxembourg, Netherlands, New Zealand, Sweden, Switzerland, and the United Kingdom. Norway was excluded as an extreme positive outlier (due to the surplus revenues from its petroleum sector). Japan lacked deficit observations from 2000 to 2004. Ireland, Portugal, and Spain were excluded due to their entry into respective bailout programs in the aftermath of the 2008 Financial Crisis.

The dissertation reveals also a Right trade-off on a more unexpected front perhaps. One of the main contentions is that the maneuverability of ways to cut

from defense spending and the other half from domestic programs, excluding Social Security, Medicaid, parts of Medicare, and certain other entitlement programs. A bipartisan budget agreement in December 2013 partially replaced the sequester in fiscal years 2014 and 2015 with small mandatory savings. The Bipartisan Act of 2015 then canceled the discretionary reductions for 2016 and 2017 and set new caps for those years. Consequently, what US policymakers have agree the most upon is not to do anything that would tackle the long-term debt issue.

taxes is directly link the number of tax brackets: with more brackets come more instruments one can target. On the one hand, the Right should cherish this policy flexibility. On the other hand, it is clear that it is at odds with another predominant objective that is often promoted by the Right too: the idea of taxing incomes as simply as possible. An implication of my argument is that reducing complexity by scaling back the number of tax brackets, but presumably also by eliminating specific tax allowances and credits, may very well produce a tax system that is simpler to understand and administer. But it also creates one with a lot less instruments when conducting future reform. Since the number of tax brackets is moderately and positively linked to tax progressivity (as shown in **Chapter 4**), the Right may ultimately still prefer an income tax system that is simpler and not too redistributive. Yet, it does beg the question how the Right ideally navigates in such political waters. This dissertation claims that their main response is to target tax thresholds as the more feasible policy option left. I admit, though, that future research could perhaps benefit from looking at the Right's strategies in this confined policy space a little broader, e.g. by exploring to what extent the Right systematically target either specific tax deductions that are to the benefit of middle-to-high income groups, or go after reducing burdens on other forms of taxation that act as 'stand-in taxes' on the rich, including the property, the capital gains, and/or the inheritance tax. The dissertation has looked at income taxes first and foremost, which is arguably where the biggest political conflict lies, but it may be useful to expand the slate of policy instruments a little more.

A final partisan topic worth commenting on is, of course, my sharp focus on Right. One could reasonably wish a broader partisan focus. To what extent would the conclusions on tax strategies have been any different, if we had instead chosen to focus on the party elites on the Left or at the Centre of the political spectrum? This is in many ways a reasonable objection, especially given my methodological choices, as I only at tax reforms look in-depth when the Right conducted them. There are potential insights to unlock by studying reforms across other partisan configurations. I do think it is a valid enough to start with the Right, as the tendency to cut taxes, which have been the main mode of politics over the last 20 years, is much more down their alley. The macro results confirm too that reforms aiming for (high-end) tax cuts are to a wide extent a right-wing phenomenon. It is, in my view, unlikely that the same mechanisms extend seamlessly to other partisan constellations. This justifies the 'Right' in the title of the dissertation.

What could, instead, serve as an intriguing extension to this dissertation's framework is to consider the tax strategies pursued by the Right where they do *not* hold political power. The theory, as it is presented here, is de facto one

of right-wing *qovernments*, i.e. what the Right does when they control the political executive and the best positioned to reforming the status quo. We know from other policy areas, however, that opposition parties, especially if they hold an 'issue ownership', may exert some influence on government policies by directing enough attention to particular policy issues that the government would feel pressured to act in accordance with the opposition's preferences (Jensen and Seeberg 2015). Such type of conflict could materialize itself in the tax domain. If a Left government, for example, considered raising taxes on the highest income groups to reduce inequality and to generate revenue, it would be relatively easy for a right-wing opposition to paint a picture of the leftish parties as 'over-taxing' and damaging economic growth and job creation, acting as a political deterrence. And where we saw a clear role division between the Right government and the Left opposition in the country reform studies in this dissertation, with the former clearly taking the political initiative to cut income taxes, it would be interesting to study, whether the reversed roles would apply as stringently, if we look at similar tax-cutting reforms under leftwing rule. Or whether such reforms are in some capacity the result of political pressure coming from the Right.

## 9.2 Instrument choice: looking beyond rates and thresholds

The conceptualization in this dissertation has focused almost exclusively on the composition of the income tax *schedule*, defined by the two sets of policy parameters: the rate(s) and the threshold(s). As evident from the case studies, it is not unreasonable to suggest that *they* are at the core of most income tax reforms. Much of the political conflict resolves around them. Yet, we know – both from the existing tax literature and from the same cases – that they are not the only instruments that can be changed. I made a conscious decision early on in this dissertation by not including the various forms of tax exemptions into my comparative theory due to the enormous variation in their count, scope and design across countries. They are, hence, tricky to study, and our empirical evidence on such tax expenditures is relatively limited (von Haldenwang, et al. 2021).<sup>326</sup> But I do acknowledge we cannot write the whole

<sup>&</sup>lt;sup>326</sup> Much recently, the first comparative database on tax expenditure has been released by Agustin Redonda and his collaborators (2021), titled The Global Tax Database (GTED), with a scope of as many as 97 countries in selected years. The goal of the database is mainly to document the number and scope of tax expenditure measures in individual countries as well as providing an estimate of the level of forgone revenue that can be attributed to such policies.

story of the politics of income taxation without accounting for these measures. Such exemptions, designed to favor a particular group, class or activity, are assumed to be the hidden elements of the tax system, with their ambiguity serving as their key political feature: real costs and benefits are unknown or deliberately kept away from public scrutiny. In the US context, they have been regarded as key tools for distributing money to the core constituencies of the major parties (Faricy 2016).

As mentioned, the focus on tax exemptions is likely warranted if we seek to explain the broader tax strategies of the Right. But before we incorporate these instruments into our models, we need to engage in critical discussion of how they fundamentally differ from the tax measures employed in this dissertation and whether the assumptions made about their instruments qualities are indeed the right ones. Is it, for example, true that the visibility of the individual tax exemptions is lower, and more blurry in the eyes of voters, than the baselines established for the rate and the threshold? It is not the case, in my view, that introducing a new tax allowance for a specific group involves a causal interpretation that is more difficult to grasp than say if one would raise thresholds: it has the direct effect of alleviating tax burdens on those particular persons or objects, and a large share of voters should be able to recognize that. Perhaps, the key difference with exemptions is that policymakers purposely highlights the target group for tax cuts, making it *easier* for voters to come to the conclusion that the policy intends to directly benefit this target group. Maybe it is just the case that the visibility gets lost once the number of exemptions reaches a high enough number.<sup>327</sup> Figuring out what specifically make tax exemptions politically profitable instruments, as we can indeed observe that they are,<sup>328</sup> is an obvious avenue for further studies.

<sup>&</sup>lt;sup>327</sup> Scholars will often point to the fact that tax exemptions are 'hidden' because their revenue impact does not figure on the official fiscal sheets; the revenue foregone is not something that is logged in the budget in the same manner that government spending items are logged. I buy *this* discrepancy without any objection. I do not buy, however, that it differs significantly for how tax cuts are generally tallied in budget-ary processes. For example, policymakers and administrators do not keep explicit track how much spending is lost by having a top marginal tax rate on income that is lower than the level it potentially could have been. Or by having tax thresholds set at certain levels, but which, in theory, could have been set at lower monetary amounts to bring in more revenue. Consequently, I believe the main differences in instrument qualities between exemptions on one side and rates and thresholds on the other should be found elsewhere.

<sup>&</sup>lt;sup>328</sup> Otherwise, their prevalence would be much more limited.

The call to look beyond the instruments covered in the dissertation can, as mentioned, also involve looking at instruments within the related tax domains, which can become potential targets of reform once the possibilities of altering the income tax have been exhausted. From the Right vantage point, it may include those forms of taxation that tend to be very progressively distributed, e.g. capital gains or inheritance taxation. But it certainly extends too to the other common tax levied on payroll income, i.e. social security contributions. Since SSCs typically grants access to earmarked, contribution-based entitlements, it is perhaps also where the fusion between the tax-side and the spending-side of state takes place most evidently. The decision not to study the politics of the SSCs is natural to me given my Danish origin, as these taxes comprise virtually nothing in the total pool of tax revenue, 0.1 percent in 2018 according to the OECD.<sup>329</sup> But they play a much larger role in many comparable countries, as tax revenue stemming from SSCs comprise more than 34 percent of all revenue in Germany, the Netherlands, France, and Austria. In these settings, we would imagine more contemplation of the part of policymakers on whether to reform the income tax or SSCs if the goal is to lower or raise taxation on income. Not least when it comes to a visibility standpoint. In line with this dissertation, I think such future analysis should take in its starting point at the instrument level rather comparing the two tax types as such. Studying the Continental European countries, especially, should be a good entry for uncovering to what extent the political conflict over the Right income tax policy differs significantly from what goes on with the SSCs.

### 9.3 Future reform paths

Based on the dissertation findings, it is, of course, relevant to contemplate to what extent we can predict future reform tendencies. Should we essentially witness a continuation of the tracks that have been paved over the last 20 years? And can we define a likely 'endpoint' for income tax policies? Naturally, I cannot provide certain answers to such questions, but I am willing to speculate a little bit.

One thing learnt from the past decades is that income tax policies differ in times of economic boom or crisis, as this was evident from the period *during* and *surrounding* the Financial Crisis. With the economy in turmoil, the tax trade-off will tend to switch, orthogonally to the government's political leanings, making revenue sufficiency a higher priority to close the (large) budget

<sup>&</sup>lt;sup>329</sup> Only Australia and New Zealand had a lower share among the countries studied in this dissertation, as both had no tax revenue at all stemming from social security contributions in 2018.

deficits. Hence, the strong partisan conflict over income taxes is mainly something we will witness when the economy is running at normal or above its long-term growth trend. This leads us to think that governments in the midst of the recent macro-economic challenges, ignited by the COVID-19 crisis, will look to new tax-side policies that are first and foremost geared towards raising revenue. With the epidemic as its main cause, there are reasons to expect the duration of the current downturn will be noticeably shorter compared to the last Financial Crisis. Nevertheless, there is clear and present need for someone to foot the fiscal bill from the extensive fiscal 'recovery packages' that have played a vital role in supporting incomes, preserving jobs and keeping businesses afloat in the individual countries. To raise such revenue, a few countries, including Canada, New Zealand and Spain, have actually introduced a new top personal income tax bracket (OECD 2021e), mimicking some of ratehiking reforms we witnessed from 2010 to 2013 (as per Figure 19 in Chapter 6). Other countries have chosen the politically quieter route. The Conservative government in the United Kingdom, for example, made the move to freeze the size of the personal allowance and the higher rate threshold at their current levels until the fiscal year 2025-26 (!) as one initiative to pay the extensive public borrowing: a bracket creep that is expected to bring in an estimated £8.2 billion a year at the end of this period (HM-Treasury 2021).

Beyond the immediate COVID-19 aftermath, I expect the political conflict to return to something resembling the patterns described in the dissertation. On the broad level, there have only been slight indications that income tax policies have followed a 'convergence' track. The cross-country mean nor the variance for the top statutory tax rate on income has moved that much during the period,<sup>330</sup> implying that these top marginal tax rates have generally not been moving towards to a certain tax rate level, whether it is in an upwards nor downwards direction. Further, a parameter which has too exhibited remarkable stability is the number of tax brackets (as shown in Figure 7 in **Chapter 4**). Despite the broadly stated political ambitions of simplifying the tax schedule, there is little evidence to support the notion that the structure of schedules has become simpler over the past 20 years.<sup>331</sup> I expect that the institutional factors, under scrutiny in this dissertation, will continue as rather 'fixed' quantities and, hence, remain as key moderators that income tax politics that plays going forward. The theoretical arguments tied to the tax progressivity and the number of tax brackets should have sustained relevance.

 $<sup>^{330}</sup>$  In 2000, the mean for the 21 countries my analyses was 49.0% (st.d. = 6.6). In 2018, it was 48.6% (st.d. = 6.4).

<sup>&</sup>lt;sup>331</sup> The reserved is, of course, also not the case: schedules have not become more complex on average either.

A key question in that respect is, of course, to what extent the Right will keep their position as the dominant political force. The reason I write this is tied to the realization that the parts of the discussion surrounding the income tax question have moved significant in the recent years. On the one hand, mainstream economists have long, and still continue, preached to the Right choir, arguing for still lower tax burdens on 'productive' economic activities such as work, while putting taxation on those objects and activities that are more inelastic to higher tax levels, e.g. basic consumption goods and properties. One the other hand, there is growing awareness of the great rise in the within-country income inequality across the Western world, coming both from parts of academia, with the French economist Thomas Piketty (2013, 2020a) as the most prominent voice, and from the intergovernmental economic organizations too, with both the OECD and the IMF recognizing that too much inequality can serve as detrimental for macroeconomic stability and for sustained long-term growth. The conundrum then becomes how we can design policies that tackle inequality without (too many) negative repercussions for growth. It is difficult to predict exactly how this rising attention to the inequality question will manifest itself within political debates and conflicts, but it should have tangible implications for the income tax area. It is not obvious that this development will make the Right reevaluate how they fundamentally position themselves on the large tax trade-offs. But it may lend more credibility to the actors that promote income equality. From the scholarly perspective, an intriguing conflict to study over the coming years is to what extent the Left is able to overcome political and institutional resistance and succeed in raising (income) taxes on the wealthiest groups in society. And not least with what policy tools they manage to do so. In any event, I will not be surprised if we partisan struggle over income taxation becomes more balanced in the next decades, and that we, if so, should let the Left play a larger role in the theory that explains policy change.

### Annexes

## Annex A.I. Tax progressivity and top statutory tax rate on income

**Figure 35** Bivariate relationship between progressivity and top statutory tax rate on income



Source: Own visualization based on OECD (2008a).

**Notes:** Data on progressivity refers to the progressivity of household taxes in the mid-2000s for the working age population. Data for Portugal and Spain are not collected in the study and are therefore excluded from the figure.

Table 12 Overvie	w of the OE	CD policy data	a for the Unit	ed Kingdon	1, 2000-2018				
Country	Year	PA	TC	S	${ m R_i}$	$M_1$	$\mathbb{R}_2$	${ m M}_2$	$\mathbb{R}_3$
United Kingdom	2000	4,385	NA	NA	10.0%	1,520	22.0%	28,400	40.0%
United Kingdom	2001	4,535	NA	NA	10.0%	1,880	22.0%	29,400	40.0%
United Kingdom	2002	4,615	NA	NA	10.0%	1,920	22.0%	29,900	40.0%
United Kingdom	2003	4,615	NA	NA	10.0%	1,960	22.0%	30,500	40.0%
United Kingdom	2004	4,745	NA	NA	10.0%	2,020	22.0%	31,400	40.0%
United Kingdom	2005	4,895	NA	NA	10.0%	2,090	22.0%	32,400	40.0%
United Kingdom	2006	5,035	NA	NA	10.0%	2,150	22.0%	33,300	40.0%
United Kingdom	2007	5,225	NA	NA	10.0%	2,230	22.0%	34,600	40.0%
United Kingdom	2008	6,035	NA	NA	20.0%	34,800	40.0%		
United Kingdom	2009	6,475	NA	NA	20.0%	37,400	40.0%		
United Kingdom	2010	6,475	NA	NA	20.0%	37,400	40.0%	150,000	50.0%
United Kingdom	2011	7,475	NA	NA	20.0%	35,000	40.0%	150,000	50.0%
United Kingdom	2012	8,105	NA	NA	20.0%	34,370	40.0%	150,000	50.0%
United Kingdom	2013	9,440	NA	NA	20.0%	32,010	40.0%	150,000	45.0%
United Kingdom	2014	10,000	NA	NA	20.0%	31,865	40.0%	150,000	45.0%
United Kingdom	2015	10,600	NA	NA	20.0%	31,785	40.0%	150,000	45.0%
United Kingdom	2016	11,000	NA	NA	20.0%	32,000	40.0%	150,000	45.0%
United Kingdom	2017	11,500	NA	NA	20.0%	33,500	40.0%	150,000	45.0%
United Kingdom	2018	11,850	NA	NA	20.0%	34,500	40.0%	150,000	45.0%
Source: OECD (2010	(du								

Annex A.II. Example of income tax policy data as recorded by the OECD

**Notes:** All figures are listed in British Pounds ( $\mathcal{E}$  or GBP).

## Annex A.III. Issues related to the construction of novel policy measures

This section of the dissertation dives into the details on how to calculate the corrected rate and thresholds effects in more complex policy scenarios when the number of threshold limits exceeds one (j > 1), which translate to when the number of tax brackets exceeds two. To do this, I expand on the fictious income tax code presented in the main chapter (see **Figure 11**). The example featured a two-rate schedule, a 10% bottom rate, a 30% higher rate, and the threshold limit at 50.

### A.III.I. Rate and threshold effects when j > 1

We now expand the tax schedule with a third rate. Let us say we add an additional 50% rate starting at the threshold value 80. Assuming the taxable income stays 100, as it was in the example, the new tax liability is 24<sup>332</sup>. What happens then if all parameters, rates and thresholds, are changed as a part of an income tax reform? In this example, we raise the threshold limits for T<sub>1</sub> and  $T_2$  with 5 scale points each. At the same time, we lower the basic rate ( $R_1$ ) with 2 percentage points, but raise the higher rate  $(R_2)$  with 2 percentage points and the top rate  $(R_3)$  with 4 percentage points. The taxable income again stays the same for the sake of simplicity. **Table 13** summarizes the policy parameters used. The new tax liability is 22.1333, a -1.9 point net change from the baseline. Hence, the reform results in an overall tax reduction. If we first calculate the rate effect  $(TL_R)$  by lagging all parameter values except for the rates, we obtain a new tax liability of 24.4, a 0.4 point net change from the baseline<sup>334</sup>. The similar threshold effect ( $TL_T$ ) yields then 22.0, a -2.0 net change<sup>335</sup>. In their direct effects, the rate effect is here slightly positive on the tax liability, while the threshold effect is negative. But they do not yet sum to the correct net change (-1.9).

<sup>&</sup>lt;sup>332</sup> The calculation is as follows: TL =  $0.1 \times 100 + (0.3 - 0.1) \times (100 - 50) + (0.5 - 0.3) \times (100 - 80) = 24.0$ 

<sup>&</sup>lt;sup>333</sup> The calculation of the post-reform tax liability is as follows: TL = 0.08 \* 100 + (0.32 - 0.08) \* (100 - 55) + (0.54 - 0.32) \* (100 - 85) = 22.1

<sup>&</sup>lt;sup>334</sup> The calculation of the rate effect is as follows: TL = 0.08 \* 100 + (0.32 - 0.08) \* (100 - 50) + (0.54 - 0.32) \* (100 - 80) = 24.4

<sup>&</sup>lt;sup>335</sup> The calculation of the threshold effect is as follows: TL = 0.1 \* 100 + (0.3 - 0.1) \* (100 - 55) + (0.5 - 0.3) \* (100 - 85) = 22.0

Policy parameter	Before reform	After reform	Net difference
TI	100	100	0
$R_1$	0.10	0.08	-0.02
$R_2$	0.30	0.32	0.02
$\mathbf{R}_3$	0.50	0.54	0.04
$T_1$	50	55	5
T2	80	85	5

**Table 13** Policy scenario with three rates and two thresholds

But because R and T are changing simultaneously, we need to account for the altering tax bases between the observation years. Raising  $T_1$  expands the base for which the basic rate applies, while it reduces the base liable to the higher rate. I therefore correct the effects by subtracting the 'gained' base times the decrease in the basic rate from the calculated threshold effect. Visually, it is represented by the left-most greyish shaded area in **Figure 36** below. Intuitively, it reads as a small additional tax reduction for the taxpayer we need to factor in because the person now pays a slightly lesser rate (8% compared to 10%) on her income between 50 and 55. Conversely, we need to add the 'lost' base times the increase in the higher rate to the rate effect (the left-most navy-colored area)<sup>336</sup>. It reads as a small additional tax cut because the taxpayer does not pay the slightly higher rate (32% compared to 30%) on her income between 50 and 55.

Figure 36 Stylized example of the corrected rates and threshold effects



**Notes:** The grey line represents baseline example. Values for Year 0 are:  $M_1 = 10 \%$ ,  $M_2 = 30 \%$ ,  $M_3 = 50 \%$ ,  $T_1 = 50$ ,  $T_2 = 80$ . Values for Year 1 are:  $M_1 = 8 \%$ ,  $M_2 = 32 \%$ ,  $M_3 = 54 \%$ ,  $T_1 = 55$ ,  $T_2 = 85$ . The greyish shaded area represents the corrections to the threshold effect, while the navy are corrections to the rate effect.

<sup>336</sup> The correction of the threshold effect is:  $-\Delta T_1 * \Delta R_1 = -5 * -0.02 = 0.1$ . The correction of the rate effect is:  $\Delta T_1 * \Delta R_2 = 5 * 0.02 = 0.1$ 

Similarly, raising T<sub>2</sub> expands the base for which the higher rate applies, while it reduces the base liable to the top rate. The yields a similar type of correction<sup>337</sup>. The right-most of the greyish areas thus represents a small additional tax hike for the taxpayer because she pays a slightly higher rate (32% compared to 30%) on her income between 80 and 85. The right-most of the navy areas shows a small additional tax cut because the taxpayer does not pay the higher top rate (54% compared to 50%) on the same income between 80 and 85. The corrected rate effect is therefore; 0.4 - 0.1 - 0.2 = 0.1. The corrected threshold effect is; -2.0 - 0.1 - (-0.1) = -2.0. The sum of the corrected effects (-1.9) corresponds the overall change in tax liability.

The correction of the rate and threshold effects are easy to expand to even more complex settings. Generally, the correction of the threshold effect follows the structure:

 $COR(T) = Threshold effect - (-\Delta T_1 * \Delta R_1) - ... - (-\Delta T_j * \Delta R_{k-1})$ (A.1)

where  $\Delta T$  is the difference in threshold values between time periods, and  $\Delta R$  is the difference in marginal rates. j again lists the total number of thresholds, while k specifies the number of marginal rates (<sub>k-1</sub> is the second-highest of the marginal rates in the tax schedule). Conversely the correction of the rate effect is given by the following expression:

 $COR(R) = Rate effect - (\Delta T1 * \Delta R2) - ... - (\Delta Tj * \Delta Rk) (A.2)$ 

### A.III.II. Rate and threshold effects when j changes from one year to the next

Until now, I have studied relatively well-behaved policy settings premised upon the assumption that the number of thresholds remains constant over time. Yet, one scenario with great empirical relevance is when tax brackets change over time, for example when they are either created or abolished as a part of a reform, whereby their number changes by definition. This creates a 'missing data problem' in my approach to calculating the reform effects.

We can generally distinguish between two scenarios: one in which j drops, and one in which j grows. Let us look at both in turn. Say we use the same fictious income tax code presented in the main chapter, a two-rate schedule with a 10% percent, a 30% higher rate, and the threshold at 50. We now reform the schedule and replace it with a simplified one-rate system featuring an 18% flat-rate. We operate with the assumption that the taxable income stays at 100.

<sup>&</sup>lt;sup>337</sup> The correction of the threshold effect is:  $-\Delta T_2 * \Delta R_2 = -5 * 0.02 = -0.1$ . The correction of the rate effect is:  $\Delta T_2 * \Delta R_3 = 5 * 0.04 = 0.2$ 

The new tax liability is  $18.0^{338}$ , a -2.0 point net change from the baseline. But using our standard calculations to obtain the rate and threshold effects is plagued with an informational problem (as evident by **Table 14**); values for R<sub>2</sub> and T<sub>1</sub> only appear in the 'before reform' scenario. Hence, we cannot conduct a one-to-one comparison of the tax parameters of this year's and last year's values.

Policy parameter	Before reform	After reform	After reform (replaced values)
TI	100	100	0
$R_1$	0.10	0.18	0.18
$R_2$	0.30		0.18
$T_1$	50	•••	100

**Table 14** Policy scenario with a reduction in thresholds

The obvious way to dodge the issue, and the approach I lean on, is simply to act as if the number of threshold was constant, even when it is not. To do this, we need to treat the 'after reform' scenario as if it was still a two-rate system, yet a system where both R<sub>1</sub> and R<sub>2</sub> take the flat-rate percentage with which we have replaced the former marginal rates. Similarly, we need to replace the missing value for  $T_1$  with the value equivalent to the taxpayer's taxable income. We can do this because removing the particular threshold value simply equates to expanding the size of the tax base, so it extends the entire income scale of relevance. Table 14 shows what the scenario looks likes, if we replace the missing values accordingly. It then becomes straightforward to calculate the reform effects. In the example, the direct net rate effect is a -2.0 point change<sup>339</sup>, while the direct net threshold effect is a -10.0 point change<sup>340</sup>. The sum of direct effects are way too large before correcting them<sup>341</sup>. After this, the true rate effect is a 4.0 point net change and the true threshold effect is a -6.0 point net change. They sum to the correct amount. This approach with replacing missing values for the marginal rate(s) with the highest marginal rate observable after the reform, and with replacing missing values for the threshold limit with the value of the taxable income (before the reform) works for all scenarios that involve a reduction in the number of tax brackets.

 $<sup>^{338}</sup>$  The calculation is as follows: TL = 0.18 \* 100 = 18.0

 $<sup>^{339}</sup>$  The calculation of the rate effect is as follows: TL = 0.18 \* 100 + (0.18 - 0.18) \* (100 - 50) = 18.0

 $<sup>^{340}</sup>$  The calculation of the threshold effect is as follows: TL = 0.1 \* 100 + (0.3 – 0.1) \* (100 – 100) = 10.0

 $<sup>^{341}</sup>$  The correction of the threshold effect is: - $\Delta T_1 * \Delta R_1 = -50 * 0.08 = -4.0$ . The correction of the rate effect is:  $\Delta T_1 * \Delta R_2 = 50 * -0.12 = -6.0$ 

The inverted scenario, a rise in the number of effective tax brackets, works in a similar manner. Imagine instead that we would reform the schedule along the same lines in the former section; we expand the baseline schedule with a third top rate of 50% kicking in at 80. This results in a new tax liability of 24, a 4.0 point hike from the baseline. It creates a backwards informational problem, as values for  $R_3$  and  $T_2$  only figure in the 'after reform' scenario. **Table 15** illustrates the issue.

Policy parameter	Before reform	Before reform ( <i>replaced values</i> )	After reform
TI	100	100	100
$R_1$	0.10	0.10	0.10
$R_2$	0.30	0.30	0.30
$R_3$		0.30	0.50
$T_1$	50	50	50
T <sub>2</sub>	•••	100	80

The method for solving the problem is again to assume a consistency in j. We now treat the 'before reform' scenario as a de facto three-rate system, replacing the missing value for  $T_2$  with the taxable income in the baseline year, and by replacing the missing  $R_3$  with the  $R_2$  value. Again, it works as simply expanding the tax base 'on paper'. Now, we can calculate the direct net rate effect as a 0.0 point change<sup>342</sup>, while the direct net threshold effect is also a 0.0 point change<sup>343</sup>. After correcting them<sup>344</sup>, the true rate effect is now a 4.0 point net change while the true threshold effect is still a 0.0 point change. They sum to correct amount. Again, the approach extends to all scenarios which involve a rise in the number of tax brackets.

<sup>342</sup> The calculation of the rate effect is as follows: TL = 0.1 \* 100 + (0.3 - 0.1) \* (100 - 50) + (0.5 - 0.3) \* (100 - 100) = 20.0

<sup>343</sup> The calculation of the threshold effect is as follows: TL = 0.1 \* 100 + (0.3 - 0.1) \* (100 - 50) + (0.3 - 0.3) \* (80 - 100) = 20.0

<sup>344</sup> The correction of the threshold effect is:  $-\Delta T_1 * \Delta R_1 + -\Delta T_2 * \Delta R_2 = 0 * 0.0 + 20 * 0.0 = 0.0$ . The correction of the rate effect is:  $\Delta T_1 * \Delta R_2 + \Delta T_2 * \Delta R_3 = 0 * 0 + -20 * 0.2 = -4.0$ .

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**Table 16** Calculated rate and threshold effects for the United Kingdom, 2000-2018

		Rate effect	Threshold effect	Rate effect	Threshold effect	Rate effect	Threshold effect
Country	Year	50 percent	50 percent	100 percent	100 percent	300 percent	300 percent
United Kingdom	2001	0.00	-0.38	0.00	-0.19	0.00	-0.33
United Kingdom	2002	0.00	-0.04	0.00	-0.02	0.00	-0.13
United Kingdom	2003	0.00	-0.04	0.00	-0.02	0.00	-0.16
United Kingdom	2004	0.00	-0.06	0.00	-0.03	0.00	-0.22
United Kingdom	2005	0.00	-0.06	0.00	-0.03	0.00	-0.24
United Kingdom	2006	0.00	-0.05	0.00	-0.03	0.00	-0.21
United Kingdom	2007	0.00	-0.07	0.00	-0.03	0.00	-0.29
United Kingdom	2008	1.52	-0.99	0.76	-1.49	0.21	-0.74
United Kingdom	2009	0.00	0.00	0.00	0.00	0.00	-0.58
United Kingdom	2010	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom	2011	0.00	0.00	0.00	0.00	0.00	0.51
United Kingdom	2012	0.00	0.00	0.00	0.00	0.00	0.13
United Kingdom	2013	0.00	0.00	0.00	0.00	0.00	0.49
United Kingdom	2014	0.00	0.00	0.00	0.00	0.00	0.03
United Kingdom	2015	0.00	0.00	0.00	0.00	0.00	0.02
United Kingdom	2016	0.00	0.00	0.00	0.00	0.00	-0.04
United Kingdom	2017	0.00	0.00	0.00	0.00	0.00	-0.29
United Kingdom	2018	0.00	0.00	0.00	0.00	0.00	-0.19
Aggregated scores		1.52	-1.69	0.76	-1.85	0.21	-2.24
Source: Own calculatic Notes: 50 percent refer	ons based on rs to a taxpa	OECD (2019b). yer earning 50 pe	rcent of average wages;	100 percent to a t	axpayer earning avera	ge wages; and 300	percent to a taxpayer

# Annex A.V. Descriptives of the major reforms events

							Reform
_			Threshold	- • •	Policy		type
Country	Year	Rate effect	effect	Joint effect	direction	Base share	(driven)
Australia	2002	1.50	0.00	1.50	HIKE	0.00	RATE
Australia	2005	-0.19	-1.14	-1.33	CUT	0.86	THRES
Australia	2007	-0.52	-3.30	-3.82	CUT	0.86	THRES
Australia	2009	0.00	-1.34	-1.34	CUT	1.00	THRES
Australia	2013	-1.02	-0.08	-1.09	CUT	0.07	RATE
Austria	2009	-0.34	-0.94	-1.27	CUT	0.74	THRES
Austria	2016	-0.52	-1.40	-1.92	CUT	0.73	THRES
Belgium	2001	-0.94	-0.16	-1.11	CUT	0.15	RATE
Belgium	2002	-1.04	-0.98	-2.02	CUT	0.48	RATE
Belgium	2003	-0.94	-1.21	-2.15	CUT	0.56	THRES
Canada	2001	-6.90	-0.17	-7.07	CUT	0.02	RATE
Denmark	2007	8.00	-0.11	7.89	HIKE	-0.01	RATE
Denmark	2010	-5.20	-0.86	-6.07	CUT	0.14	RATE
Denmark	2012	1.01	0.00	1.01	HIKE	0.00	RATE
Denmark	2013	1.15	-0.36	1.01	HIKE	-0.46	RATE
Denmark	2015	1.24	-0.11	0.79	HIKE	-0.10	RATE
Denmark	2018	1.03	-0.21	0.83	HIKE	-0.25	RATE
Finland	2001	-0.30	-0.94	-1.25	CUT	0.76	THRES
Finland	2006	-0.97	-0.27	-1.24	CUT	0.22	RATE
Finland	2009	-0.99	-0.44	-1.44	CUT	0.31	RATE
France	2002	-2.32	-0.28	-2.60	CUT	0.11	RATE
France	2003	-1.10	-0.23	-1.33	CUT	0.17	RATE
France	2006	0.11	-10.51	-10.40	CUT	1.01	THRES
France	2018	1.70	-0.19	1.51	HIKE	-0.13	RATE
Iceland	2003	-1.31	-0.06	-1.37	CUT	0.05	RATE
Iceland	2005	-2.35	0.00	-2.35	CUT	0.00	RATE
Iceland	2006	-0.30	-2.10	-2.40	CUT	0.88	THRES
Iceland	2009	1.35	0.00	1.35	HIKE	0.00	RATE
Iceland	2010	-1.56	7.27	5.71	HIKE	1.27	THRES
Iceland	2011	-1.17	-0.17	-1.34	CUT	0.13	RATE
Ireland	2001	-1.92	-0.97	-2.89	CUT	0.34	RATE
Ireland	2007	-0.74	-0.33	-1.08	CUT	0.31	RATE
Ireland	2009	5.00	-0.11	4.89	HIKE	-0.02	RATE
Ireland	2011	0.97	0.53	1.51	HIKE	0.35	RATE
Italy	2002	-1.40	0.00	-1.40	CUT	0.00	RATE
Italy	2007	-0.43	1.31	0.87	HIKE	1.50	THRES

**Table 17** Full list of major reform events across the OECD, 2001-2018

Italy	2011	3.00	0.00	3.00	HIKE	0.00	RATE
Italy	2017	-3.00	0.00	-3.00	CUT	0.00	RATE
Japan	2007	3.01	-2.35	0.66	HIKE	-3.54	RATE
Japan	2013	2.04	0.00	2.04	HIKE	0.00	RATE
Netherlands	2001	-5.34	-2.50	-7.84	CUT	0.32	RATE
Netherlands	2016	-0.43	-0.78	-1.21	CUT	0.64	THRES
New Zealand	2008	6.69	-7.16	-0.46	CUT	15.35	THRES
New Zealand	2009	-7.14	5.52	-1.62	CUT	-3.41	RATE
New Zealand	2010	-2.09	0.00	-2.09	CUT	0.00	RATE
New Zealand	2011	-2.10	0.00	-2.10	CUT	0.00	RATE
Norway	2001	-1.31	-0.25	-1.56	CUT	0.16	RATE
Norway	2002	3.99	-0.18	3.81	HIKE	-0.05	RATE
Norway	2003	-1.75	-0.52	-2.30	CUT	0.24	RATE
Norway	2005	-0.99	-0.20	-1.19	CUT	0.17	RATE
Norway	2006	-1.52	-0.15	-1.68	CUT	0.09	RATE
Norway	2011	1.37	0.00	1.37	HIKE	0.00	RATE
Norway	2016	5.97	-7.15	-1.18	CUT	6.08	THRES
Portugal	2001	-1.11	-0.60	-1.71	CUT	0.35	RATE
Portugal	2011	4.03	-0.15	3.88	HIKE	-0.04	RATE
Portugal	2012	-1.00	0.00	-1.00	CUT	0.00	RATE
Portugal	2013	0.45	2.64	3.09	HIKE	0.85	THRES
Portugal	2018	4.88	-4.88	-0.00	-	-	-
Spain	2003	-5.31	-1.33	-6.65	CUT	0.20	RATE
Spain	2007	-0.34	-0.89	-1.23	CUT	0.72	THRES
Spain	2011	-4.59	0.00	-4.59	CUT	0.00	RATE
Spain	2012	2.42	0.00	2.42	HIKE	0.00	RATE
Spain	2015	-1.25	-1.54	-2.79	CUT	0.55	THRES
United States	2003	-1.44	-0.13	-1.57	CUT	0.08	RATE
United States	2018	-2.64	0.28	-2.36	CUT	-0.12	RATE

**Source:** Own calculations based on OECD (2019b). **Notes:** The table contains a total of 65 reforms. The reference taxpayer is the taxpayer earning 300 percent of average wages.

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Source: Own calculations based on OECD (2019b).

**Notes:** The figure contains a total of 65 reforms. The reference taxpayer is the taxpayer earning 300 percent of average wages. The rate effect is shown on the *y*-axis, while the threshold effect is on the *x*-axis. Reforms are labelled 'neutral' if the combined effect is more than -0.5 and less than 0.5 percentage change from last year's country values.

# Annex A.VI. Presentation of the variable used in the Chapter 6 models

Variables	Measurement	Source
Right government	Derived from the share of cabinet seats held by right-wing parties in a given year. Employed as a dummy variable; 1 = the seat share is larger than or equal to 50 percent.	Armingeon et al. (2020)
GDP growth	Growth of real GDP, percent change from previous year.	Armingeon et al. (2020)
Primary balance	Cyclically adjusted annual deficit excluding net interest payments (general government) as percentage of GDP.	Armingeon et al. (2020)
Total tax revenue	Total receipts (revenue) of general government as a percentage of GDP.	Armingeon et al. (2020)
Number of income tax brackets	A count of the number of different income tax brackets in countries' tax schedules.	OECD (2019b)
Top statutory tax rate on income	Top statutory personal income tax rates, for the combined central and sub-central governments.	OECD (2019c)
Threshold indexation scheme	Indicator of whether the given country has some automatic adjustment scheme on threshold limits in place to prevent fiscal drag.	OECD (2007)
Institutional fragmentation	Additive index that focuses on three nodes of political systems, namely federalism (none, weak, strong), presidentialism (absent, present), and bicameralism (absent, weak, strong).	Lijphart (1999/2012)
PR system	Indicator of the type of electoral system. Majoritarian = 0. PR = 1.	Lijphart (1999/2012)

### Table 18 Variable used in the Chapter 6 models

						Between
Variables	Туре	Mean	St.d.	Min	Max	share
Right government	Dummy	0.51	0.50	0.00	1.00	0.11
GDP growth	Metric	1.85	2.57	-8.07	25.12	0.16
Primary balance	Metric	-0.16	4.38	-29.75	15.72	0.43
Total tax revenue	Metric	43.31	7.97	25.42	59.21	0.95
Number of income tax brackets	Metric	4.08	1.48	1.00	8.00	0.81
Top statutory tax rate on income	Metric	47.95	6.04	33.00	62.28	0.75
Threshold indexation scheme	Dummy	0.68	0.47	0.00	1.00	1.00
Institutional fragmentation	Categorical	1.47	1.35	0.00	5.00	1.00
PR system	Dummy	0.67	0.47	0.00	1.00	0.95

Table 19 Summary statistics for the variables included in the Chapter 6 models

**Source:** Own calculations.

**Notes:** 342 country year observation for 19 countries. The time period for the regression models is from 2001 to 2018. The 'between share' represents the share of between variance of the variable in proportion to the total variance (between- and within variance).

Table 20 Collegation Intactive for the Valiat			maplet 0 1	SIDUUI					
	(E)	(2)	(3)	(4)	(2)	(9)	(2)	(8)	(6)
(1) Right government	1.00								
(2) GDP growth (lag)	0.01	1.00							
(3) Primary balance (lag)	-0.03	$0.22^{*}$	1.00						
(4) Total tax revenue (lag)	-0.06	0.35*	-0.13*	1.00					
(5) Number of income tax brackets (lag)	-0.00	-0.06	-0.21*	-0.22*	1.00				
(6) Top statutory tax rate on income (lag)	0.04	0.22*	-0.11	0.37*	-0.00	1.00			
(7) Threshold indexation scheme	0.06	0.05	0.04	0.45*	-0.39*	0.17*	1.00		
(8) Institutional fragmentation	-0.03	-0.07	0.01	-0.36*	0.51*	-0.02	-0.27*	1.00	
(9) PR system	-0.15*	0.30*	0.02	0.46*	-0.25*	0.05	$0.21^{*}$	-0.42*	1.00
Contree. Own relevilations									

**Table 20** Correlation matrix for the variables included in the Chapter 6 models

**Source:** Own calculations. **Notes:** N=323. \*: p < 0.05.

Table 21 Logistical models of m	najor income tax	reforms (cuts)				
	Model 1A Cut reform 50 percent AW	Model 1B Cut reform 50 percent AW	Model 2A Cut reform 100 percent AW	Model 2B Cut reform 100 percent AW	Model 3A Cut reform 300 percent AW	Model 3B Cut reform 300 percent AW
Lagged DV	0.88 (0.28)	0.60 (0.58)	$0.83^{\dagger}$ (0.48)	0.70 (0.47)	0.80 (0.54)	0.58 (0.54)
Right-wing government	0.18 (0.26)	0.31 (0.32)	0.41 (0.34)	0.54 (0.37)	0.39 <sup>†</sup> (0.23)	0.59* 0.26)
GDP growth (lag)		0.02 0.08)		-0.06	5	-0.01 (0.08)
Primary balance (lag)		0.00		0.07 0.01		0.11 0.05
Total tax revenue (lag)		0.03 0.03 (0.03)		-0.03 -0.03 (0.03)		-0.01 (0.03)
Number of income tax brackets (lag)		0.05 (0.19)		-0.11 (0.15)		0.18
Top statutory tax rate on income (lag)		-0.03 (0.02)		0.02 (0.03)		0.01 (0.03)
Threshold indexation scheme		(0.38)		-0.61* (0.24)		-0.53 <sup>†</sup> (0.30)
Institutional fragmentation		0.12 (0.12)		0.01 (0.12)		0.15 (0.16)
PR system		0.12 (0.48)		0.70 <sup>†</sup> (0.38)		0.59 (0.54)
Constant	-2.44 (0.28)	-1.85 (1.90)	-2.42 <sup>***</sup> (0.25)	-1.65 (1.40)	-2.37*** (0.24)	$-3.55^{+}$ (2.08)

Annex A.VII. Regression results for the predictions income tax reform events

:						
N – ODServations	323	323	323	323	323	323
N – countries	19	19	19	19	19	19
N – positive outcomes	38	38	44	44	45	45
Pseudo R <sup>2</sup>	0.02	0.06	0.02	0.05	0.02	0.06
<b>Notes:</b> <sup>†</sup> : p<0.1; *: p<0.05; **: p<0.01;	**: p<0.001. Clust	ered standard error	in parentheses.			

<b>Table 22</b> Logistical models of n	najor income tax	reforms (hikes)				
	<b>Model 4A</b> Hike reform	<b>Model 4B</b> Hike reform	Model 5A Hike reform	Model 5B Hike reform	<b>Model 6A</b> Hike reform	Model 6B Hike reform
	50 percent AW	50 percent AW	100 percent AW	100 percent AW	300 percent AW	300 percent AW
Lagged DV	1.29 (0.92)	0.91 (0.77)	$1.46^{+}$ (0.79)	0.83 (0.77)	0.66 (0.72)	0.01 (0.72)
Right-wing government	0.70 <sup>†</sup> (0.40)	$0.72^{\dagger}$ (0.41)	0.40 (0.50)	0.50 (0.53)	0.35 (0.41)	0.51 $(0.42)$
GDP growth (lag)		0.06 (0.07)		-0.07 (0.08)		-0.07 (0.09)
Primary balance (lag)		-0.11 (0.08)		-0.19** (0.06)		-0.20** (0.08)
Total tax revenue (lag)		0.05 (0.06)		0.10* (0.04)		0.08* (0.04)
Number of income tax brackets (lag)		-0.01 (0.25)		-0.04 (0.25)		-0.09 (0.29)
Top statutory tax rate on income (lag)		0.02 (0.04)		-0.01 (0.04)		-0.01 (0.04)
Threshold indexation scheme		-0.14 (0.64)		-0.13 (0.64)		-0.66 (0.66)
Institutional fragmentation		$-0.43^{\dagger}$ (0.24)		-0.53 (0.34)		-0.42 (0.31)
PR system		0.10 (0.37)		0.09 (0.60)		0.31 $(0.58)$
Constant	-3.17 <sup>***</sup> (0.35)	$-5.84^{*}$ (2.38)	-3.05*** (0.44)	-6.23** (2.60)	-2.96*** (0.41)	$-5.44^{\dagger}$ (2.97)
N – observations	323	323	323	323	323	323
N – countries	19	19	19	19	19	19
N – positive outcomes	22	22	21	21	20	20
Pseudo R <sup>2</sup>	0.04	0.10	0.04	0.16	0.01	0.14
<b>Notes:</b> <sup>+</sup> : p<0.1; *: p<0.05; **: p<0.01	l; ***: p<0.001. Clus	stered standard erro	r in parentheses.			

	<b>Model 7</b> Cut reform	<b>Model 8</b> Cut reform	<b>Model 9</b> Cut reform
	50 percent AW	100 percent AW	300 percent AW
Lagged DV	0.24	0.43	0.44
	(0.71)	(0.61)	(0.63)
Right-wing government	0.26	$0.68^{+}$	0.66*
	(0.36)	(0.40)	(0.28)
GDP growth (lag)	-0.05	-0.06	-0.08
	(0.10)	(0.10)	(0.10)
Primary balance (lag)	0.03	0.08	0.11
	(0.05)	(0.07)	(0.08)
Total tax revenue (lag)	0.01	-0.03	0.01
	(0.03)	(0.04)	(0.04)
Number of income tax brackets (lag)	0.11	-0.01	0.14
	(0.17)	(0.17)	(0.27)
Top statutory tax rate on income (lag)	-0.02	0.04	0.01
	(0.03)	(0.03)	(0.04)
Threshold indexation scheme	-1.29***	-0.71*	-0.76†
	(0.34)	(0.31)	(0.46)
Institutional fragmentation	0.11	0.06	0.29
	(0.13)	(0.14)	(0.20)
PR system	0.25	$1.03^{+}$	0.31
	(0.46)	(0.355)	(0.66)
Constant	-1.64	-3.26*	-4.46
	(1.60)	(1.55)	(2.85)
N – observations	309	323	323
N – countries	19	19	19
N – positive outcomes	15	15	30
Pseudo R <sup>2</sup>	0.08	0.05	0.07

**Table 23** Logistical models of major income tax reforms (cuts) – extreme reformcases

**Notes:** <sup>+</sup>: p<0.1; <sup>+</sup>: p<0.05; <sup>++</sup>: p<0.01; <sup>+++</sup>: p<0.001. Clustered standard error in parentheses.

	<b>Model 10</b> Cut reform 300 percent AW	<b>Model 11</b> Cut reform 300 percent AW
Lagged DV	0.57 (0.53)	0.48 (0.52)
(1) Right-wing government	1.02 (1.00)	4.59 <sup>**</sup> (1.55)
(1) X (2)	-0.10 (0.22)	
(1) X (3)		-0.08** (0.03)
GDP growth (lag)	-0.02 (0.08)	-0.03 (0.09)
Primary balance (lag)	0.11 (0.05)	0.12 (0.05)
Total tax revenue (lag)	-0.01 (0.03)	-0.01 (0.03)
(2) Number of income tax brackets (lag)	0.25 (0.24)	0.16 (0.18)
(3) Top statutory tax rate on income (lag)	0.01 (0.03)	0.07 <sup>†</sup> (0.04)
Threshold indexation scheme	$-0.56^{+}$ (0.29)	-0.62* (0.30)
Institutional fragmentation	0.15 (0.16)	0.14 (0.16)
PR system	0.58 (0.55)	0.53 (0.54)
Constant	-3.78 <sup>+</sup> (2.09)	$-5.93^{+}$ (2.40)
N – observations	323	323
N – countries	19	19
N – positive outcomes	45	45
Pseudo R <sup>2</sup>	0.06	0.07

**Table 24** Logistical models of major income tax reforms (cuts) – interactive relationships

**Notes:** <sup>†</sup>: p<0.1; <sup>\*</sup>: p<0.05; <sup>\*\*</sup>: p<0.01; <sup>\*\*\*</sup>: p<0.001. Clustered standard error in parentheses.

	<b>Model 12</b> Threshold-based 300 percent AW	<b>Model 13</b> Rate-based 300 percent AW
Lagged DV		0.79 (0.61)
Right-wing government	0.18 (0.49)	0.78* (0.37)
GDP growth (lag)	0.14 (0.09)	-0.09 (0.08)
Primary balance (lag)	0.15 (0.10)	0.09 (0.07)
Total tax revenue (lag)	0.03 (0.06)	-0.03 (0.03)
Number of income tax brackets (lag)	0.02 (0.29)	0.25 (0.18)
Top statutory tax rate on income (lag)	0.04 (0.06)	-0.00 (0.03)
Threshold indexation scheme	-1.62** (0.53)	0.07 (0.42)
Institutional fragmentation	0.43 (0.22)	-0.00 (0.19)
PR system	0.24 (0.64)	0.60 (0.59)
Constant	-7.01** (2.39)	-3.18 (1.95)
N – observations	323	323
N – countries	19	19
N – positive outcomes	15	30
Pseudo R <sup>2</sup>	0.11	0.06

**Table 25** Logistical models of rate- and threshold-based major income tax reforms (cuts)

**Notes:** <sup>+</sup>: p<0.1; <sup>+</sup>: p<0.05; <sup>++</sup>: p<0.01; <sup>+++</sup>: p<0.001. Clustered standard error in parentheses.

## Annex A.VIII. Revenue impact of the Tax Cuts and Jobs Act

	<b>Revenue impact</b>	<b>Revenue impact</b>
Measure	(static)	(dynamic)
Individual		
New income tax rates and thresholds for seven brackets	-\$1,873	-\$1,589
Increase the standard deduction	-\$774	-\$708
Increase the child tax credit	-\$590	-\$562
Raise the AMT tax exemption	-\$209	-\$266
Raise the estate tax exemption	-\$72	-\$46
Repeal the personal exemptions	\$1,318	\$1,227
Cap the deduction for state and local taxes and eliminating other deductions	\$593	\$575
Indexation to the chained CPI	\$151	\$151
Other repeals	\$47	\$47
Subtotal	-\$1,338	-\$1,125
Various corporate tax measures	-\$373	\$408
De facto repeal of the individual mandate	\$314	\$314
Total	-\$1,469	-\$448

**Table 26** Estimated 10-year revenue impact of the Tax Cuts and Job Acts

Source: Tax Foundation (2017b)

**Notes:** The amount listed are in billions of dollars.

### Annex A.IX. Full survey questionnaire

#### [Survey was fielded in Danish. The English translation is presented below.]

[Info] Thank you for participating.

Epinion are in collaboration with a scientist at Aarhus University mapping the Danes' views on current political topics. The survey is a part of a larger research project and we hope you will read the questions thoroughly and answer them all.

It takes about 10 minutes to complete the survey.

How to proceed? You begin your answers by clicking 'Next'. It is important to note there are no right or wrong answers. We are interested in getting your view on the current topics.

**Your answers are treated confidentially** and are part of one joint analysis, with no way of tracing them back to you. The answers are passed on to Aarhus University in anonymized form. Epinion delete your data and answers no later than 3 months after the completion of the survey. Your participation is voluntary, and you are able to withdraw your consent at any time, whereby we delete your information if they are not already anonymized.

#### Thank you!

[back1] First come some short questions on yourself.

Are you?

- o (\_1) Male
- o (\_2) Female
- o (\_3) Non-binary
- o (\_4) Don't wish to answer

[back2] What is your age?

#### o (\_1) Fill in age:<Open Textbox>

```
If back2<18 or back2>74
Terminate survey
```

End If

[back3] In which region do you live?

#### o (\_1) Capital Region

- o (\_2) Zealand
- o (\_3) Southern Denmark
- o (\_4) Central Denmark
- o (\_5) North Denmark
- o (\_6) I live outside of Denmark

```
If back3.ContainsAny(_6)
Terminate survey
End If
```

#### [back4]

What is you highest completed education?

- o (\_1) Primary school
- o (\_2) Upper secondary education
- o (\_3) Vocational education
- o (\_4) Short-cycle higher education
- o (\_5) Medium-cycle higher education
- o (\_6) Bachelor's
- o (\_7) Master's
- o (\_8) Doctoral

#### [back5]

Which of the following describes best you current household situation?

- o (\_1) I live alone
- o (\_2) I live with my spouse/partner
- o (\_3) I live with one or more who is not a spouse/partner

#### [back6]

Which of the following describes best your current occupation? If you fit into more than one category, please choose your primary status.

- o (\_1) Have a paid job (e.g. employee, self employed, flex job)
- o (\_2) Student
- o (\_3) Unemployed
- o (\_4) On parental leave.
- o (\_5) On sick leave
- o (\_6) Pensioner, early retirement (outside the labour force)
- o (\_7) Housework/homegoing
- o (\_8) Other:<Open Textbox>

#### FILTER: If bag6.ContainsAny(\_1)

[back7] In which type of organization are you employed?

- o (\_1) A public workplace (also if an independent institution)
- o (\_2) A private company
- o (\_3) I am self employed
- o (\_4) Other:<Open Textbox>

#### End If

[Info]

Now follow some questions on you private economy.

#### [inc1]

What is your personal monthly income in a typical/average month?

We refer to your gross income, i.e. before taxes and allowances, yet <u>without your pension</u> <u>savings</u>.

In your monthly income can several types of incomes be included, both wage income, capital income, pension payments, unemployment benefits, social assistance, student grants and other types of benefits.

#### If you do not know the exact amount, we are interested in your best estimate.

#### o (\_1) Note amount:<Open Textbox>

#### [inc2]

Do you expect to pay the top-bracket tax rate of your personal income in 2020?

o (\_1) Yes

- o (\_2) No
- o (\_3) Don't know

#### FILTER: If back5.ContainsAny(\_2)

#### [inc3]

#### What is your household's total monthly income in a typical/average month?

We refer to your gross income, i.e. before taxes and allowances, yet <u>without your pension</u> <u>savings</u>.

Her tænkes på jeres bruttoindkomst, dvs. før skat og fradrag, men <u>uden opsparing til pen-</u>sion.

In your monthly income can several types of incomes be included, both wage income, capital income, pension payments, unemployment benefits, social assistance, student grants and other types of benefits.

If you do not know the exact amount, we are interested in your best estimate.

#### o (\_1) Note amount:<Open Textbox>

#### End If

[ind5] Do you own any of the following?

	(_1) Yes	(_2) No
(_1) A house or an apartment		
(_2) A summer house		
(_3) A business		
$(_4)$ Securities (e.g. in the form of stocks and bonds) for more than 25,000 kr.		
(_5) A personal savings of more than 50,000 kr.		

#### [tax1]

Do you agree or disagree with the following statements on your income tax?

		(_1) Fully agree	(_2) Slightly agree	(_3) Nei- ther agree nor disa- gree	(_4) Slightly disagree	(_5) Fully disa- gree	(_6) Don't know	(_7) Not rele- vant
(_1) I have an derstanding th which are subt monthly pay ch	easy time un- e taxes racted on my neck.							
(_2) I have an changing infor advance incom and on my ann turn.	easy time mation on my e statement ual tax re-							

#### [tax2]

Do you agree or disagree with the following statement?

When politicians in Denmark discuss tax policy, I understand only little of what they are talking about.

- o (\_1) Fully agree
- o (\_2) Slightly agree
- o (\_3) Neither agree nor disagree
- o (\_4) Slightly disagree
- o (\_5) Fully disagree
- o (\_6) Don't know

#### [trust1

How much trust do you have towards each of the following institutions?

	(_0) 0 – No trust at all	(_1) 1	(_2) 2	(_3) 3	(_4) 4	(_5) 5	(_6) 6	(_7) 7	(_8) 8	(_9) 9	(_10) 10 - Full trust	(_11) Don't know
(_1) The police and the justice system												
(_2) Politicians												
(_3) Civil serv- ants in the public administration												

#### [Info]

The next questions concern taxation on income.

Before, we would like to know whether you can identify true and false statements on some of the key tax rules in Denmark.

In each of the following are two statements on a tax rule presented, one true and one false. We would like you to specify which statement is 'true'. You can answer 'Don't know' if you cannot assess whether the statement is true or false.

#### [(T) highlights the true statements below.]

[tax\_test\_1] Who is eligible for a personal allowance in Denmark?

- o (\_1) It is <u>only wage earners with a job</u> who is eligible for a personal allowance
- o (\_2) <u>All Danes</u> are eligible for a personal allowance, regardless of employment status or income type (T)
- o (\_3) Don't know

[tax\_test\_2]
What is the size of the personal allowance?

- o (\_1) The personal allowance is (in 2020) <u>lower than 40,000 kr.</u> for persons aged 18 years
- (\_2) The personal allowance is (in 2020) <u>larger than 40,000 kr.</u> for persons aged 18 years (T)
- o (\_3) Don't know

#### [tax\_test\_3]

Which income taxes are paid to the central government?

- o (\_1) Beside the labor market contribution, Danes pay to types of income taxation to the central government: the bottom tax and the top tax (T)
- o (\_2) Beside the labor market contribution, Danes pay three types of income taxation to the central government: the bottom tax, the middle tax and the top tax
- o (\_3) Don't know

[tax\_test\_4]
Which tax percentage is the highest - the bottom tax or the municipal tax?

- O (\_1) Danes pay a higher rate in <u>municipal tax</u> than in bottom tax to the central government (T)
- o (\_2) Danes pay a higher rate in <u>bottom tax</u> to the central government than in municipal tax
- o (\_3) Don't know

[tax\_test\_5] What is the rate of top tax in Denmark?

- o (\_1) The top tax is a 15 percent extra tax on the highest incomes (T)
- o (\_2) The top tax is a <u>50 percent extra tax</u> on the highest incomes
- o (\_3) Don't know

[tax\_test\_6]
Which taxpayers pay the top tax?

- o (\_1) Danes pay the top tax on personal income <u>above 431,000 kr.</u> (in 2020) after labor market contributions
- O (\_2) Danes pay the top tax on personal income <u>above 531,000 kr.</u> (in 2020) after labor market contributions (T)
- o (\_3) Don't know

#### [tax\_test\_7]

On which range of the income is the top tax paid?

- o (\_1) Persons with the highest incomes pay the top tax on <u>all of their personal income</u>
- o (\_2) Persons with the highest incomes pay the top tax on the income amount which lie above the top tax threshold (T)
- o (\_3) Don't know

#### [Info]

You found (X) of the 7 true statements. Below are shown the true statements.

	You an- swered	True state- ment
(_1) Who is eligible for a personal allowance in Denmark		(2)
(_2) What is the size of the personal allowance		(2)
(_3) Which income taxes are paid to the central government		(1)
(_4) Which percentage is the highest – the bottom tax or the municipal tax		(1)
(_5) What is the rate of top tax in Denmark		(1)
(_6) Which taxpayers pay the top tax		(2)
(_7) On which range of the income is the top tax paid		(2)

#### [Info]

The next questions concern your view on the income tax.

Politicians have different views on the income tax. The discussion often concerns the <u>top tax</u> which is a 15 percent extra tax on income above 531,000 kr. (in 2020) after labor market contributions.

#### Randomization: Order of $ex1^*$ and $ex2^*$ is randomized.

[ex1]

(#ex1\_sender) has in a recent political debate argued that the <u>threshold</u> for the top tax (531,000 kr.) should be (#ex1\_treatments). Do you agree or disagree with such a proposal?

- o (\_1) Fully agree
- o (\_2) Slightly agree
- o (\_3) Neither agree nor disagree
- o (\_4) Slightly disagree
- o (\_5) Fully disagree
- o (\_6) Don't know

#### #ex1\_sender (randomize)

- o (\_1) A politician from the Social Democrats
- o (\_2) A politician from Venstre
- o (\_3) A politician

#### #ex1\_treatments (conditional randomize)

- o (\_1) Raised noticeably (30 percent)
- o (\_2) Raised (30 percent)
- o (\_3) Lowered (20 percent)
- o (\_4) Lowered noticeably (20 percent)

#### [ex1\_effects]

One can use different motives to change the income tax.

To what extent do you think the proposal to (#ex1\_treatments) the <u>threshold for the top tax</u> will contribute to ... ?

	(_1) Not at all	(_2) To a lesser extent	(_3) To some ex- tent	(_4) To a great extent	(_5) Don't know
(_1) To increase the economic inequality in society					
(_2) To increase growth and employment in society					
(_3) To weaken welfare bene- fits and services					
(_4) To weaken the balance on the public budget balance					
[ex1\_guess] Imagine a wage earner who pays top tax of her personal income.

Would the proposal to (#ex1\_treatments) the threshold for the top tax mean ... ?

- o (\_1) The wage earner would pay *more* income tax going forward
- o (\_2) The wage earner would pay the same income tax going forward
- o (\_3) The wage earner would pay *less* income tax going forward
- o (\_4) Don't know

#### FILTER: If ex1\_sender.ContainsAny(\_1,\_2)

#### [ex1\_prob]

Do you consider it likely or unlikely that (#ex1\_party) as party would put forward a proposal to (#ex1\_treatments) the <u>threshold for the top tax</u>?

- o (\_1) Very likely
- o (\_2) Somewhat likely
- o (\_3) Somewhat unlikely
- o (\_4) Very unlikely
- o (\_5) Don't know

#### #ex1\_party

- o (\_1) The Social Democrats
- o (\_2) Venstre

#### [Info]

Now we want you to consider a different proposal on the income tax.

#### [ex2]

(#ex2\_sender) has in a recent political debate argued that the <u>percentage/rate on the top</u> <u>tax</u> (15 percent) should be (#ex2\_treatments). Do you agree or disagree with such a proposal?

- o (\_1) Fully agree
- o (\_2) Slightly agree
- o (\_3) Neither agree nor disagree
- o (\_4) Slightly disagree
- o (\_5) Fully disagree
- o (\_6) Don't know

#### #ex2\_sender (randomize)

- o (\_1) A politician from the Social Democrats
- o (\_2) A politician from Venstre
- o (\_3) A politician

#### #ex2\_treatments (conditional randomize)

- o (\_1) Raised noticeably (20 percent)
- o (\_2) Raised (20 percent)
- o (\_3) Lowered (30 percent)
- o (\_4) Lowered noticeably (30 percent)

#### [ex2\_effects]

One can use different motives to change the income tax.

To what extent do you think the proposal to (#ex2\_treatments) the <u>rate for the top tax</u> will contribute to ... ?

	(_1) Not at all	(_2) To a lesser extent	(_3) To some ex- tent	(_4) To a great extent	(_5) Don't know
(_1) To increase the economic inequality in society					
(_2) To increase growth and employment in society					
(_3) To weaken welfare bene- fits and services					
(_4) To weaken the balance on the public budget balance					

#### [ex2\_guess]

Imagine a wage earner who pays top tax of her personal income.

Would the proposal to (#ex2\_treatments) the rate for the top tax mean ... ?

- o (\_1) The wage earner would pay more income tax going forward
- o (\_2) The wage earner would pay the same income tax going forward
- o (\_3) The wage earner would pay  $\mathit{less}$  income tax going forward
- o (\_4) Don't know

#### FILTER: If ex2\_sender.ContainsAny(\_1,\_2)

[ex2\_prob]

Do you consider it likely or unlikely that (#ex2\_party) as party would put forward a proposal to (#ex2\_treatments) the <u>rate for the top tax</u>?

- o (\_1) Very likely
- o (\_2) Somewhat likely
- o (\_3) Somewhat unlikely
- o (\_4) Very unlikely
- o (\_5) Don't know

#ex2\_party

- o (\_1) The Social Democrats
- o (\_2) Venstre

#### [END LOOP]

[Info] Now we want you to consider a last proposal on the income tax.

Randomization: Only one of ex3\* and ex4\* is presented. Which one is randomized.

#### [ex3]

The discussion on the income tax also concerns the *bottom tax* to the central government. The bottom tax is a 12.11 percent tax (in 2020) which applies to all personal income, after the personal allowance is deducted.

(#ex3\_sender) has in a recent political debate argued that <u>the percentage/rate on the bot-tom tax</u> (12.11 percent) should be (#ex3\_treatments). Do you agree or disagree with such a proposal?

- o (\_1) Fully agree
- o (\_2) Slightly agree
- o (\_3) Neither agree nor disagree
- o (\_4) Slightly disagree
- o (\_5) Fully disagree
- o (\_6) Don't know

#### #ex3\_sender (randomize)

- o (\_1) A politician from the Social Democrats
- o (\_2) A politician from Venstre
- o (\_3) A politician

#### #ex3\_treatments (conditional randomize)

- o (\_1) Raised (40 percent)
- o (\_2) Lowered (60 percent)

#### [ex3\_effects]

One can use different motives to change the income tax.

To what extent do you think the proposal to (#ex3\_treatments) the rate for the bottom tax will contribute to ... ?

	(_1) Not at all	(_2) To a lesser extent	(_3) To some ex- tent	(_4) To a great extent	(_5) Don't know
(_1) To increase the economic inequality in society					
(_2) To increase growth and employment in society					
(_3) To weaken welfare bene- fits and services					
(_4) To weaken the balance on the public budget balance					

#### FILTER: If ex3\_sender.ContainsAny(\_1,\_2)

#### [ex3\_prob]

Do you consider it likely or unlikely that (#ex3\_party) as party would put forward a proposal to (#ex3\_treatments) the <u>rate for the bottom tax</u>?

- o (\_1) Very likely
- o (\_2) Somewhat likely
- o (\_3) Somewhat unlikely

- o (\_4) Very unlikely
- o (\_5) Don't know

#ex3\_party

- o (\_1) The Social Democrats
- o (\_2) Venstre

#### [ex4]

The discussion on the income tax also concern the *personal allowance*. The personal allowance is 46.500 kr. (in 2020) for persons aged 18 years which is exempt from the bottom tax and the municipal tax.

(#ex4\_sender) has in a recent political debate argued that the <u>personal allowance</u> should be (#ex4\_treatments). Do you agree or disagree with such a proposal?

- o (\_1) Fully agree
- o (\_2) Slightly agree
- o (\_3) Neither agree nor disagree
- o (\_4) Slightly disagree
- o (\_5) Fully disagree
- o (\_6) Don't know

#### #ex3\_sender (randomize)

- o (\_1) A politician from the Social Democrats
- o (\_2) A politician from Venstre
- o (\_3) A politician

#### #ex3\_treatments (conditional randomize)

- o (\_1) Raised (60 percent)
- o (\_2) Lowered (40 percent)

#### [ex4\_effects]

One can use different motives to change the income tax.

To what extent do you think the proposal to (#ex4\_treatments) the <u>personal allowance</u> will contribute to ... ?

	(_1) Not at all	(_2) To a lesser extent	(_3) To some ex- tent	(_4) To a great extent	(_5) Don't know
(_1) To increase the economic inequality in society					
(_2) To increase growth and employment in society					
(_3) To weaken welfare bene- fits and services					
(_4) To weaken the balance on the public budget balance					

FILTER: If ex4\_sender.ContainsAny(\_1,\_2)
[ex4\_prob]

Do you consider it likely or unlikely that (#ex3\_party) as party would put forward a proposal to (#ex4\_treatments) the <u>personal allowance</u>?

- o (\_1) Very likely
- o (\_2) Somewhat likely
- o (\_3) Somewhat unlikely
- o (\_4) Very unlikely
- o (\_5) Don't know

#ex4\_party

- o (\_1) The Social Democrats
- o (\_2) Venstre

#### [tax3]

Many social services of the welfare state (*public welfare*) like hospitals, elderly care and education are funded using taxes.

If a government in Denmark should choose between *either* raising taxes and spending more on public welfare, *or* lowering taxes and spending less on public welfare, what would you then choose?

- o (\_1) 1 Raise taxes a lot and spend a lot more on public welfare
- o (\_2) 2 Raise taxes a little and spend a little more on public welfare
- o (\_3) 3 Keep the current levels
- o (\_4) 4 Lower taxes a little and spend a little less on public welfare
- o  $(_5) 5$  Lower taxes a lot and spend a lot more on public welfare
- o (\_6) Don't know

#### [tax4]

Let us return to the top tax.

Which is the following statement comes closest to your view In Denmark, there are ...

- o (\_1) ... too many people who pay the top tax
- o (\_2) ... too few people who pay the top tax
- o (\_3) ... about a right number of people who pay the top tax
- o (\_4) Don't know

#### [part1]

Lastly, we want to ask your fire questions on parties and your political leanings.

	(_1) A Social Demo- cratic led govern- ment	(_2) No difference	(_3) A Bourgeois led government	(_4) Don't know
(_1) To reduce the eco- nomic inequality in society				
(_2) To enhance growth and employment in society				
(_3) To improve the public welfare				
(_4) To ensure healthy bal- ance on the public budget				

Which government, do you think, is the best at handling the following political topics?

#### [part2]

In politics, one often talks of Left and Right. Where would you place yourself on a scale from 0 to 10 where 0 is 'Left' and 10 is 'Højre'.

o (\_0) 0 - Left

- o (\_1) 1
- o (\_2) 2
- o (\_3) 3
- o (\_4) 4
- o (\_5)5
- o (\_6) 6
- o (\_7)7
- o (\_8) 8
- o (\_9)9
- o (\_10) 10 Right
- o (\_11) Don't know
- o (\_12) Don't wish to answer

#### [part3]

Many consider themselves supporters of a particular party. There are also many who do not see themselves as supporters of one party

Do you consider yourself as e.g. a Social Democrat, a Conservative, a Liberal or something else, or do you not view yourself as support of a particular party?

- o (\_1) Yes, I consider myself as a supporter of a particular party
- o (\_2) No, I am not a support of one particular party
- o (\_3) Don't know

#### [part4]

For which party would you vote, if there was a General Election tomorrow?

- o (\_1) A The Social Democratic Party
- o (\_2) B The Danish Social Liberal Party

- o (\_3) C The Conservative People's Party
- o (\_4) D The New Right
- o (\_5) F Socialist People's Party
- o (\_6) G The Danish Vegan Political Party
- o (\_7) I Liberal Alliance
- o (\_8) K The Christian Democrats
- o (\_9) O Danish People's Party
- o (\_10) P Hard Line
- o (\_11) V Liberal Party of Denmark
- o (\_12) Ø Red-Green Alliance
- o (\_13) Å The Alternative
- o (\_14) Other party/Candidate outside the parties
- o (\_15) Would vote blank
- o (\_16) Have no right to vote
- o (\_17) Would not vote
- o (\_18) Don't wish to answer

## Annex A.X. Control variables used in survey

Variables	Туре	Description
Sex	Dummy	o = Male 1 = Women
Age	Metric	The respondent's age at the time of the survey.
Education level	Categorical	<ol> <li>Primary education</li> <li>= Upper secondary education and vocational (ISCED 3)</li> <li>3 = Post-secondary and short-cycle tertiary education</li> <li>4 = Bachelor's, Master's and Doctoral</li> </ol>
Employment status	Categorical	<ul> <li>1 = Public sector</li> <li>2 = Private sector</li> <li>3 = Outside labor market</li> <li>4 = Outside labor force</li> </ul>
Level of tax knowledge	Metric	A formative index (0 to 7) derived from the 'knowledge test' consisting of seven the true/false statements on income tax- aton in Denmark
Personal income	Metric	Personal monthly income in a 'typical/average' month split into deciles according the sample distribution.
Trust in politicians	Metric	Trust in politicians measured on a scale from 0 'No trust at all' to 10 'Full trust'.
Top tax status	Dummy	Derived from a question that asks whether the respondent expect pay the top-bracket tax rate in 2020? O = No/Don't know 1 = Yes
Partisan bloc affiliation	Categorical	Party choice recoded into which political 'bloc' of which the party is a member: 1 = Parties preferring a Social Democratic PM ('red bloc') 2 = Parties preferring a Liberal PM ('blue bloc') 3 = Other, non-affiliated parties

## **Table 27** Control variables used in the survey analyses

## Annex A.XI. Balance tables for survey

Variables	Ν	Metric	Raise*	Raise	Lower	Lower*
Sender treatment						
S politician	1.561	Share	0.33	0.29	0.34	0.35
V politician	1.561	Share	0.33	0.36	0.35	0.33
Neutral politician	1.561	Share	0.34	0.35	0.31	0.33
Women	1.561	Share	0.52	0.50	0.49	0.52
Age	1.561	Mean	47.39	48.25	49.24	47.86
Education						
Primary education	1.561	Share	0.10	0.08	0.09	0.12
Upper secondary education and voca- tional	1.561	Share	0.34	0.36	0.35	0.36
Post-secondary and short-cycle tertiary	1.561	Share	0.32	0.33	0.32	0.29
Bachelor's, Master's and Doctoral	1.561	Share	0.24	0.23	0.24	0.24
Employment status						
Public sector	1.561	Share	0.22	0.21	0.22	0.22
Private sector	1.561	Share	0.33	0.35	0.30	0.35
Outside the labor market	1.561	Share	0.20	0.19	0.19	0.18
Outside the labor force	1.561	Share	0.25	0.26	0.29	0.25
Trust (politicians)	1.524	Mean	4.73	4.41	4.62	4.36
Tax knowledge	1.561	Mean	3.86	3.83	3.92	3.82
Income (deciles)	1.553	Mean	5.44	5.47	5.15	5.45
Top-rate taxpayers	1.561	Share	0.14	0.12	0.12	0.12

#### **Table 28** Balance check across treatment groups for the threshold experiment

Source: Own survey conducted by Epinion.

**Notes:** \* denotes an experimental condition where the policy direction in question was changed *no-ticeably*. Differences in shares and means were tested using Bonferroni corrected comparisons. No comparison reached a significance threshold of p < 0.05. The partisan variables – political bloc affiliation and the Left-Right self-placement – are not included in the balance check; they are asked after the survey experiments and hence potentially prone to post-treatment bias.

Variables	Ν	Metric	Raise*	Raise	Lower	Lower*
Sender treatment						
S politician	1.561	Share	0.30	$0.28^{+}$	0.32	$0.37^{+}$
V politician	1.561	Share	0.33	0.36	0.36	0.33
Neutral politician	1.561	Share	0.37	0.36	0.32	0.30
Women	1.561	Share	0.48	0.52	0.51	0.52
Age	1.561	Mean	46.91	49.52	47.52	48.51
Education						
Primary education	1.561	Share	0.09	0.11	0.09	0.10
Upper secondary education and vocational	1.561	Share	0.40	0.36	0.34	0.32
Post-secondary and short-cycle tertiary	1.561	Share	0.31	0.30	0.32	0.33
Bachelor's, Master's and Doctoral	1.561	Share	0.20	0.23	0.25	0.24
Employment status						
Public sector	1.561	Share	0.25	0.21	0.22	0.20
Private sector	1.561	Share	0.36	0.30	0.35	0.33
Outside the labor market	1.561	Share	0.18	0.19	0.19	0.18
Outside the labor force	1.561	Share	$0.20^{*}$	0.30*	0.24	0.29*
Trust (politicians)	1.524	Mean	4.71	4.33	4.74	4.68
Tax knowledge	1.561	Mean	4.03	3.78	3.81	3.86
Income (deciles)	1.553	Mean	5.59	5.15	5.49	5.33
Top-rate taxpayers	1.561	Share	0.13	0.12	0.13	0.11

Table 29 Balance check across treatment groups for the rate experime	ent
--	-----

**Source:** Own survey conducted by Epinion.

**Notes:** \* denotes an experimental condition where the policy direction in question was changed *no-ticeably*. Differences in shares and means were tested using Bonferroni corrected comparisons. Group scores which are significantly different from at least one other treatment group are marked with <sup>+</sup> for p < 0.1; \* for p < 0.05. The partisan variables – political bloc affiliation and the Left-Right self-placement – are not included in the balance check; they are asked after the survey experiments and hence potentially prone to post-treatment bias.

		Thresholds			Rates			
Treatments	V	S	Ν	Total	V	S	Ν	Total
Raise noticeably	163	162	165	490	104	89	99	292
Raise	158	128	156	420	107	113	114	334
Lower	122	117	105	344	143	141	188	472
Lower noticeably	99	99	93	285	147	151	165	463
Total	536	506	519	1.561	501	494	566	1.561

### Table 30 Sample size across treatment groups

**Source:** Own survey conducted by Epinion.

**Notes:** The abbreviations stand for the following: V = 'a politician from Venstre'; S = 'a politician from Socialdemokratiet'; N = 'a politician'.

# Annex A.XII. Survey results and supplementary analyses

	Model 14 Threshold experiments	Model 15 Rate experiments
Treatments		
Raise	(Base)	(Base)
Lower	-0.18 <sup>+</sup> (0.10)	-0.11 (0.11)
Constant	0.32*** (0.07)	0.88*** (0.09)
N	1.561	1.561
Pseudo R <sup>2</sup>	0.00	0.00
Predicted probabilities		
Guess rate		
Raise	0.58 [0.55; 0.61]	0.71 [0.67; 0.74]
Lower	0.53 [0.50; 0.57]	0.68 [0.65; 0.71]

 Table 31
 Successful guess rate for each proposal (logit)

	Model 16 Threshold experiments	Model 17 Rate experiments
Treatments		
Raise	(Base)	(Base)
Lower	-0.07 (0.15)	0.09 (0.16)
Question order		
Thresholds experiment first	(Base)	(Base)
Rates experiment first	-0.00 (0.13)	0.46* (0.18)
Treatment X Sender		
Raise X Rates experiment first	(Base)	(Base)
Lower X Rates experiment first	-0.49* (0.21)	$-0.42^{\dagger}$ (0.23)
Constant	0.32** (0.09)	0.66*** (0.12)
N	1.561	1.561
Pseudo R <sup>2</sup>	0.00	0.00
Predicted probabilities		
Guess rate		
Raise x Thresholds experiment first	0.58 [0.53; 0.62]	0.66 [0.61; 0.71]
Raise x Rates experiment first	0.58 $[0.53; 0.62]$	0.75 [0.71; 0.80]
Lower x Thresholds experiment first	0.60 [0.54; 0.65]	0.68 [0.64; 0.72]
Lower x Rates experiment first	0.48 [0.42; 0.53]	0.69 [0.65; 0.73]

**Table 32** Successful guess rate for each proposal by the order of the experiments (logit)

	Model 18	Model 19
	Threshold experiments	Rate experiments
Treatments		
Raise	(Base)	(Base)
Lower	-0.29*	-0.16
	(0.12)	(0.13)
Partisan messenger		
A politician from Venstre	(Base)	(Base)
A politician from Socialdemokratiet	0.11	-0.15
	(0.15)	(0.16)
A politician	-0.11	$-0.30^{+}$
	(0.14)	(0.16)
Question order		
Thresholds experiment first	(Base)	(Base)
Rates experiment first	-0.19 <sup>†</sup>	-0.18
-	(0.12)	(0.13)
Female	-0.08	0.07
	(0.13)	(0.14)
Age	0.01*	$0.01^{\dagger}$
	(0.00)	(0.01)
Education		
Primary	(Base)	(Base)
Upper secondary and vocational	0.46 <sup>+</sup>	0.27
11 -	(0.25)	(0.24)
Post-secondary and short-cycle tertiary	0.53*	$0.43^{\dagger}$
5 5 5	(0.25)	(0.26)
Bachelor's, Master's and Doctoral	0.70**	$0.53^{*}$
	(0.26)	(0.27)
Employment		
Public sector	(Base)	(Base)
Private sector	-0.28	-0.02
	(0.17)	(0.18)
Outside labor market	0.07	0.00
	(0.23)	(0.24)
Outside labor force	-0.51*	-0.06
	(0.23)	(0.24)
Trust in politicians	0.01	0.01
*	(0.02)	(0.03)
Гах knowledge	0.26***	0.28***
~	(0.04)	(0.04)
Income (decile)	0.09**	0.06†
	(0.03)	(0.03)
Member of top income bracket	0.12	-0.20
	(0.20)	(0.22)

## Table 33 Predictors of successful guesses (logit)

Political bloc affiliation		
Blue bloc party	(Base)	(Base)
Red bloc party	-0.04 (0.16)	0.09 (0.18)
Others	-0.31 (0.20)	0.08 (0.21)
Left-Right self-placement	-0.03 (0.03)	-0.04 (0.03)
Constant	-1.59** (0.49)	-1.01* (0.50)
Ν	1.331	1.331
Pseudo R <sup>2</sup>	0.09	0.07

	Model 20	Model 21
	Threshold experiments	<b>Rate experiments</b>
Treatments		
Raise noticeably	(Base)	(Base)
Raise	0.35* (0.14)	0.07 (0.18)
Lower	-0.48** (0.17)	0.07 (0.17)
Lower noticeably	-0.52** (0.18)	-0.31 <sup>+</sup> (0.17)
Constant	-0.85*** (0.10)	0.18 (0.15)
N	1.561	1.561
Pseudo R <sup>2</sup>	0.02	0.00
Predicted probabilities		
Support		
Raise noticeably	0.30 [0.26; 0.34]	0.29 [0.24; 0.34]
Raise	0.38 [0.33; 0.43]	0.30 [0.25; 0.35]
Lower	0.21 [0.17; 0.25]	0.30 [0.26; 0.34]
Lower noticeably	0.20 [0.16; 0.25]	0.23 [0.19; 0.27]

Table 34 Estimated support to the proposals (logit)

	Model 22	Model 23	Model 24	Model 25
	Threshold	Threshold	Rate	Rate
	experiments	experiments	experiments	experiments
	Raise	Lower	Raise	Lower
Partisan messenger				
A politician from Venstre	(Base)	(Base)	(Base)	(Base)
A politician from	0.17	0.13	-0.21	-0.50**
Socialdemokratiet	(0.17)	(0.23)	(0.21)	(0.19)
A politician	-0.06	-0.11	-0.24	-0.31 <sup>†</sup>
	(0.17)	(0.25)	(0.21)	(0.18)
Constant	-0.71***	-1.36***	-0.72***	-0.75***
	(0.12)	(0.17)	(0.15)	(0.13)
N	932	629	626	935
Pseudo R <sup>2</sup>	0.00	0.00	0.00	0.01
Predicted probabilities				
Support				
A politician from Venstre	0.33	0.20	0.33	0.32
	[0.28; 0.38]	[0.15; 0.26]	[0.26; 0.39]	[0.27; 0.37]
A politician from	0.37	0.23	0.28	0.22
Socialdemokratiet	[0.31; 0.42]	[0.17; 0.28]	[0.22; 0.34]	[0.17; 0.27]
A politician	0.32	0.19	0.28	0.26
	[0.27; 0.37]	[0.13; 0.24]	[0.22; 0.34]	[0.21; 0.30]

## Table 35 Estimated support to the proposals by partisan messenger (logit)

	Model 26 Threshold experiments	Model 27 Rate experiments
Treatments		
Raise	(Base)	(Base)
Lower	-1.66*** (0.19)	2.08*** (0.21)
Party sponsor		
Venstre	(Base)	(Base)
Socialdemokratiet	-2.42 <sup>***</sup> (0.20)	1.23 <sup>***</sup> (0.21)
Treatment X Sender		
Raise X Venstre	(Base)	(Base)
Lower X Socialdemokratiet	2.85*** (0.29)	-3.97*** (0.30)
Constant	0.78*** (0.12)	-1.06*** (0.16)
N	1.042	995
Pseudo R <sup>2</sup>	0.14	0.19
Predicted probabilities		
Likelihood		
Raise x Venstre	0.69 [0.63; 0.74]	0.26 [0.20; 0.31]
Raise x Socialdemokratiet	0.16 [0.12; 0.20]	0.54 [0.47; 0.61]
Lower x Venstre	0.29 [0.23; 0.35]	0.73 [0.68; 0.79]
Lower x Socialdemokratiet	0.39 [0.32; 0.45]	0.15 [0.11; 0.19]

 Table 36
 Estimated likelihood of the proposals (logit)

	Model 22 Threshold experiments	Model 24 Rate experiments
(1) Treatments	•	*
Raise	(Base)	(Base)
Lower	0.62***	$0.42^{\dagger}$
	(0.17)	(0.22)
(2) Corrects guess		
No	(Base)	(Base)
Yes	0.59***	0.88***
	(0.15)	(0.21)
(1) X (2)	0.06	-0.15
	(0.22)	(0.26)
Constant	-1.75***	-1.89***
	(0.35)	(0.37)
Controls	Yes	Yes
Ν	1545	1545
Pseudo R <sup>2</sup>	0.06	0.05
Predicted probabilities		
Opposition		
Incorrect guess - Raise	0.27	0.23
-	[0.23; 0.32]	[0.17; 0.30]
Correct guess – Raise	0.45	0.44
	[0.41; 0.49]	[0.40; 0.49]
Incorrect guess - Lower	0.42	0.30
	[0.37; 0.48]	[0.25; 0.35]
Correct guess - Lower	0.61	0.51
	[0.56; 0.66]	[0.48; 0.55]

 Table 37 Estimated opposition to the proposals (logit)

# Annex A.XIII. Marginal income tax rate across the top brackets

**Table 38** Marginal income tax rates for the highest and next-highest tax brackets across the OECD

Country	Percentage jump in marginal tax rate (next-highest to highest)	Marginal tax rate (next-highest bracket)	Marginal tax rate (highest bracket)
United States	2.0%	35.0%	37.0%
Luxembourg	2.0%	36.0%	38.0%
Italy	2.0%	41.0%	43.0%
Switzerland	2.2%	11.0%	13.2%
Norway	3.0%	21.0%	24.0%
New Zealand	3.0%	30.0%	33.0%
Germany	3.0%	42.0%	45.0%
Portugal	3.0%	45.0%	48.0%
Spain	4.0%	18.5%	22.5%
Canada	4.0%	29.0%	33.0%
France	4.0%	41.0%	45.0%
Sweden	5.0%	20.0%	25.0%
Japan	5.0%	40.0%	45.0%
United Kingdom	5.0%	40.0%	45.0%
Belgium	5.0%	45.0%	50.0%
Austria	5.0%	50.0%	55.0%
Australia	8.0%	37.0%	45.0%
Iceland	9.3%	22.5%	31.8%
Finland	10.0%	21.3%	31.3%
Netherlands	11.1%	40.9%	52.0%
Denmark	15.0%	11.1%	26.1%
Ireland	20.0%	20.0%	40.0%
Mean	5.9%	31.7%	37.6%

Source: Own calculations based on OECD (2019b).

Notes: The table values refer to 2018 numbers. All numbers are rounded to one decimal.

# English summary

The dissertation looks at the politics of income taxation. It studies the scope and the types of income tax policy reform within the OECD world from the year 2000 onwards.

The debate on income taxes is alive and well in contemporary politics. It is a topic that politicians on both sides of the political aisle seem to care a lot about, and we witness, from time to time, both major and minor political reforms of how the income tax code is structured. Since (income) taxes lay the foundation for everything else that modern-day states do, it is simply difficult to imagine a full 'coverage' of politics without them. Consequently, scholars should take great interest in this topic. Yet, the political science literature has to a wide extent, and to much surprise, neglected the whole tax question (Steinmo 1998, Hakelberg and Seelkopf 2021b). Both when it comes to delivering good answers on the type of policy change, that takes place within this domain, and to understanding its causes.

The dissertation attempts to bridge this gap. It goes in depth with the personal income tax, a cornerstone across all tax systems in advanced democracies. Needless to say, the income tax system is an incredible complex entity to study, often spelled out over hundreds, if not thousands, of detailed legislative pages and guidelines at the national level. These vast policy idiosyncrasies pose a significant challenge for comparative research, and their sheer scope may elucidate why we do not have a good theoretical framework for explaining the cross-national policy dynamics. I try to take a swing at this proposition, as the dissertation, more specifically, poses the research question(s): what is the scope of (income) tax policy reform in the OECD from 2000 onwards? And why do we observe different types of reform?

I proceed first by establishing a set of conceptual building blocks, so we can study these problems properly in a comparative manner. The basic task of politicians, within the income tax realm, is to set the rules that decide which rate of income tax the taxpayer must pay at a given level of income. If we take them in reverse order, they cover the questions 'who' must pay and 'how much'. It parcels out the two core choices at level of the policymakers: decisions on (1) tax *rates*, and on (2) tax *thresholds*. The *tax bracket* is what fuses the two. If ones wishes to cut income taxes, the main ways to do is by either lowering the statutory rate on one or more tax brackets, or by raising the monetary threshold for when a certain tax rate kicks in.

The instrument distinction is key because the two are not functional equivalents. We know this from the field of economics, as their theory teaches us that the (marginal) rate is the more powerful tool for affecting key economic outcomes such equality and efficiency. I add they are certainly also not alike from a political standpoint either. Inspired by the visibility argument advanced by Pierson (1994), the rate is the more easy-to-comprehend way of cutting income taxes if we compare the two. It figures front and center on monthly paychecks; it is easy to link changes in statutory rates to changes in taxpayers' living standards; and the rate stays the same, until it is actively changed by policymakers. Contrast this to the thresholds of tax brackets which are instead tied to the annual income instead of the monthly; which hold a causal impact on tax liability that works in reverse (raising a threshold entails lower taxation), and which are as much as function of changes in income levels as they are of changes in the thresholds themselves. I show this visibility claim is not merely a theoretical proposition. Evidence from a novel survey experiment, fielded among Danish voters, find that instrument choice matters significantly for voters' ability to grasp the 'true' causal effect of a policy change: rates *are* easier to comprehend than thresholds. One reason why this is significant from a policy standpoint is that lack of visibility is strongly linked to policy indifference on the part of the voters, and reform-eager politicians will likely prefer ways of changes taxation that augment their connection to the more popular policy tools while, as importantly, distorting or hiding their connection to unpopular ones. Hence, we should only expect the rate to be cut if it is not a widely unpopular idea to do so. In this way, the 'rules' of politics will oftentimes supersede what may be the preferred solution from a pure economic standpoint.

The distinction between the rate and the threshold enables me to shed light on the 'what has happened' question at the macro-level. I show, using novel policy-based tax indicators I construct from the raw OECD legislative data, that virtually all countries have cut income taxes from their policy baselines 20 years ago, rather than to raise it. The pattern makes sense, since policymakers need to actively cut to prevent tax hikes by default in the form of 'bracket creep'. But while the cutting has the norm, the means have differed significantly. The OECD countries fall into two predominant reform tracks: one group has (only) enacted threshold-driven reform, while the other group has cut income tax rates too. I find that the latter group – the 'rate cutters' – are typically those that have lowered income taxes as a whole the most.

I argue that we need to look at the political Right to properly understand the dynamics of income tax policies. The Right is the proactive force pushing to cut income taxes, as they must do so in order to keep tax revenue from rising, and because they expect such moves to breed positive economic consequences, more efficiency at the (accepted) costs of more inequality and lower revenue yields. Tax cuts are too compatible, in a normative sense, with a more performance-based distribution of goods, which rewards individual ambition and the spirit of free enterprise and meritocracy, and which meshes well with Right ideology. I expect the Right to cut tax rates over thresholds preferably, due to the greater growth-stimulating effects, and show in macro-analyses, spanning 19 OECD countries from 2000 to 2018, that Right cabinets, on average, are a large driver of tax-cutting reforms, especially if they contain mainly rate cuts. Yet, the results demonstrates that the Right tends to introduce cuts that disproportionally target the high-income segments, as a similar 'positive' effect cannot be found for those lowest on the income scale.

It is not the whole story, though. I show next that key tax institutions serve to modify the tax reform strategies pursued by the Right. More precisely, the mode of reform tends to follow the composition of the income tax schedule. On the one side, I argue the number of tax brackets guides instrument choice: in settings with fewer tax brackets to choose from, reforming politicians will tend to target the threshold limits to change income tax rules, in part because it is too costly, politically and fiscally, to meddle with the rates, while a higher number of tax brackets enables reforms of both the rate and threshold alike. The progressivity of the schedule, in turn, guides to priorities of the Right: in strongly progressive systems, the Right typically fights for cuts at the top-end of the income distribution, whereas a lower progressivity facilitates a more balanced effort to cut both at the 'top' and at the 'bottom'. I find empirical evidence of both institutional mechanisms. Both when studying the long-term macro-findings across the OECD, but the claims are also grounded with case study evidence from tax reforms in Denmark, the United Kingdom, and the United States. The locus of income tax cuts have, for example, been much more geared towards thresholds by the Right in the low bracket cases of Denmark and the United Kingdom, whereas Republicans in the United States have more overtly attempted to slash marginal tax rates. At the same time, the cuts enacted by the Right in the UK and the US, the high progressivity cases, have been much more skewed towards the top income groups than in Denmark where the strategy pursued by the Right parties has been more broad-based.

The contributions of the dissertation are pertinent for the literatures on partisan politics, (income) taxation and public policy at large, as it presents both novel conceptualization and empirical work on the often forgotten taxside of the (welfare) state. The hope is that the dissertation will provide its readers with a more nuanced understanding of all the politics that goes into policy choice, discarding the notion of treating 'income taxes' as one unified concept which policymakers can just lower or raise. Consequently, the findings should prompt researchers across the social science subfields to pay careful attention to the political visibility and feasibility of different policy options, in addition to the mere economic effects, to explain why so-called 'non-optimal' tax solutions are oftentimes preferred. Lastly, the dissertation underscores the importance of factoring in the existing tax legacies, the policy status quo, as key moderators when we seek to explain the cross-national variance in how seemingly like-minded political actors choose so different reform ends when it comes to income taxation.

# Dansk resume

Denne PhD-afhandling handler om indkomstskattepolitik. Den zoomer ind på omfanget og typerne af reformer på indkomstskatteområdet i OECD-landene fra år 2000 og frem.

Der er stor politisk bevågenhed omkring indkomstskatten i nutidens politik. Det er et emne, som optager politikere på begge sider af den politiske midte, og vi kan løbende observere eksempler på både større og mindre politiske reformer af, hvordan indkomstskatten skal struktureres. Skatten på indkomst udgør således det økonomiske fundament for mange af staters nutidige aktiviteter, og det er svært at forestille sig en fyldestgørende dækning af politik uden et kig på indkomstskatten. Forskere bør af samme grund udvise stor interesse for emnet. Men statskundskabslitteraten har i vid udstrækning, og til stor overraskelse, overset hele skattespørgsmålet (Steinmo 1998, Hakelberg and Seelkopf 2021b). Både når det gælder om at levere gode svar på, hvilken slags politikforandring der finder sted på området, men også når det gælder om at forstå dets årsager.

Afhandlingen forsøger at udfylde dette hul. Den går i dybden med den personlige indkomstskat, som er en hjørnesten i alle skattesystemer i vestlige demokratier. Vi ved, at indkomstskattesystemer er enormt komplekse, som ofte strækker sig over hundreders, hvis ikke tusinders, siders detaillovgivning, cirkulærer og vejledninger på de enkelte nationale niveauer. Disse mange særtræk er en stor udfordring for komparativ forskning, og deres blotte omfang er muligvis en god forklaring på, hvorfor der ikke findes gode teoretiske analyserammer til at forstå de tværnationale politikdynamikker. Jeg giver et bud på en sådan ramme, da afhandlingen mere præcist stiller forskningsspørgsmålet: Hvad er omfanget af indkomstskattereform(er) i OECD from år 2000 og frem? Og hvorfor observerer vi forskellige reformtyper?

Jeg starter min afhandling med at etablere de centrale teoretiske begreber. Hovedopgaven for politikere inden for dette domæne er at definere, hvilken rate eller procentsats som en skatteyder skal betale i skat ved et givent indkomstniveau. Dvs. det kredser om spørgsmålene, *hvem* der skal betale, og *hvor meget* de skal betale. Det er de to kernevalg for lovgivere; beslutninger om (1) skatte*rater* og om (2) skatte*beløbsgrænser*. Hvis man ønsker at skære i indkomstskatterne, er der altså to overordnede metoder til at gøre det; at sænke skatteraten på én eller flere indkomstklasser eller ved at hæve beløbsgrænsen for, hvornår en given rate sætter ind.

Det er en væsentlig sondring, fordi instrumenterne ikke er funktionelle ækvivalenter. Det ved vi fra den økonomiske litteratur, hvis teori peger på, at det er den (marginale) skatterate, som er det stærkeste redskab af de to til at påvirke økonomiske nøglemål som lighed og efficiens. Et hovedargument i afhandlingen er, at de heller ikke er ens fra et politisk synspunkt. Med inspiration fra Pierson (1994) 'synlighedsargument' argumenterer jeg for, at raten er den måde at skære i indkomstskatten, som er nemmest at forstå for vælgerne. Raten fremgår af vores månedlige lønsedler; det er nemt at forbinde en ændring i raten med ændringen i skatteydernes rådighedsbeløb og levestandard; og raten forbliver på samme niveau, indtil den aktivt ændres af et politisk flertal. Beløbsgrænserne har andre egenskaber. De refererer til årsindkomsten frem for månedslønnen; de har en modsatrettet påvirkning på, hvor meget indkomstskat der betales (at hæve en beløbsgrænse indebærer mindre skat); og de er ligesom meget en funktion af ændringer i (real)lønniveauet som en funktion af ændringerne i selvsamme beløbsgrænser. I afhandlingen viser jeg, at denne synlighedspåstand ikke blot en teoretisk idé. Jeg demonstrerer med resultater fra et originalt survey-eksperiment foretaget blandt danske vælgere, at instrumentvalget betyder meget for vælgernes evne til at forstå den 'sande' kausale effekt af en politikændring: Rater er nemmere at begribe end beløbsgrænserne. Det er et væsentligt fund, fordi manglen på synlighed er stærkt forbundet med politisk indifferens, når det gælder vælgerne, og reformvillige politikere vil sandsynligvis foretrække de typer af politikændringer, som fremhæver deres forbindelse til de mere populære værktøjer, mens de ligesom væsentligt ønsker at sløre deres forbindelse til de mere upopulære. Vi vil derfor forvente, at der kun skæres i skatteraten, der hvor det ikke er et meget upopulær forslag. På den måde vil den politiske logik trumfe den løsning, der er at foretrække ud fra alene økonomiske hensvn.

Distinktionen mellem rater og beløbsgrænser gør mig videre i stand til at belyse spørgsmålet om, hvad der er sket politikmæssigt på tværs af OEC-landene. Her viser jeg ved hjælp af et sæt af nye politikindikatorer, som jeg konstruerer på baggrund af OECD's tværnationale skattedata, at stort set alle lande har skåret i indkomstskatten frem for at hæve den i forhold til deres udgangspunkt for 20 år siden. Det er mønster, der er meningsfuldt, eftersom politikere skal aktivt skære for at forhindre automatiske skatteforhøjelser, når en skatteyder løbende skubbes op i højere indkomstklasser ('bracket creep'). Hvor skattelettelser har været normen, så har metoderne til at skære imidlertid været ret forskellige. OECD-landene har fulgt to overordnede reformspor; en gruppe har fortrinstvist på rate-drevne reformer, mens den anden gruppe mest alene har gennemført ændringer i beløbsgrænserne.

I min optik er vi nødt til at kigge på de politiske partier til højre for den politiske midte for meningsfuldt at forstå dynamikkerne på indkomstskatteområdet. De højreorienterede ('the Right') er de proaktive, når det gælder indkomstskattelettelser, da de forventer, at sådanne tiltag skaber positive økonomiske virkninger; mere efficiens på den accepterede bekostning af mere økonomisk ulighed og lavere skatteindtægter. Skattelettelser er samtidig ud fra et normativt synspunkt forenelige med en mere præstationsbetinget fordeling af samfundet, som belønner både individuelle ambitioner og meritokrati, hvilket lægger godt op i de højreorienterede parties ideologiske udgangspunkt. Samtidig forventer jeg, at de højreorienterede vil foretrække at skære i raterne frem for beløbsgrænserne pga. de større forventede økonomiske gevinster. Jeg viser i en makroanalyse, der dækker 19 OECD-lande fra 2001 til 2018, at højreorienterede regeringer gennemsnitlig set er en stor 'driver' af politiske reformer, der har til formål at sænke indkomstskatter, især hvis de primært indeholder reduktioner af raterne. Resultaterne viser dog samtidig, at partierne til højre har tendens til at introducere øremærkede lettelser til højindkomstgrupper, og en lignende 'positiv' effekt ikke kan genfindes for de grupper, der er lavere på indkomstskalaen.

Det er dog ikke hele historien. Jeg viser hernæst, at vigtige institutioner har en indvirkning på de konkrete reformstrategier, der forfølges af de højreorienterede partier. Mere præcist argumenterer jeg for, at reformindholdet har en tendens til at følge opbygningen af indkomstskattestigen. På den ene side styrer antallet af indkomstklasser instrumentvalget: I systemer med færre indkomstklasser vil politikere, der laver reformer, have tendens til at bruge beløbsgrænserne til at ændre på indkomstskattereglerne, bl.a. fordi det har for store politiske og fiskale omkostninger at skrue på raterne. Omvendt giver et højere antal af indkomstklasser bedre muligheder for reformer af både rater og beløbsgrænser. Hvor progressivt systemet er, har omvendt tendens til at styre de højreorienteredes politiske prioriteringer: I meget progressive skattesystemer vil partierne til højre typisk kæmpe for skattelettelser i toppen af indkomstskalaen, hvorimod en lavere progressivitet vil facilitere et mere balanceret forsøg på at skære både 'i toppen' og 'i bunden', De højreorienterede forventes m.a.o. at opleve færrest institutionelle begrænsninger i systemer med mange indkomstklasser, og hvor progressiviteten er høj, idet de her er i en gunstig position til at forfølge skattelettelser til de højestlønnede. Jeg finder evidens for begge institutionelle mekanismer. Både når jeg studerer de langsigtede makrofund på tværs af OECD-landene, men påstandene er også begrundet med beviser fra casestudier af skattereformer i Danmark, Storbritannien og USA. Skattelettelserne gennemført af de højreorienterede har været langt mere funderet på højere beløbsgrænser i Danmark og Storbritannien, lande med relativt få indkomstklasser, hvorimod republikanerne i USA har tydeligere forsøgt med store nedskæringer i de marginale skatterater. På samme tid har nedskæringerne foretaget af disse partier i Storbritannien og

USA, lande med høj skatteprogressivitet, været langt mere gearet mod de højeste indkomstgrupper, mens de højreorienterede i Danmark har forfulgt en bredere strategi for skattelettelser.

Afhandlingens bidrag er væsentlige for en række forskningslitteraturer inden for partipolitik, skattepolitik og offentlig politik i bredere forstand, idet den præsenterer både ny teori såvel som empiri inden for den ofte glemte skatteside af (velfærds)staten. Mit håb er, at afhandlingen giver læseren en mere nuanceret forståelse af al den politik, der går forud for politikændringer, og at den kan være med til at forkaste forestillingen om at behandle 'indkomstskatten' som ét samlet begreb, som politikere blot kan sænke eller hæve. Fundene skulle gerne opfordre forskerne på tværs af samfundsvidenskaberne til at være opmærksom på den politiske synlighed, i tillæg til de egentlige økonomiske effekter, når de vurderer forskellige politiske reformtiltag. Det kan bidrage til at forklare, hvorfor de såkaldte 'ikke-optimale' løsninger på skatteområder ofte er dem, der kan samle et politisk flertal. Slutteligt understreger afhandlingen vigtigheden af at kigge på den eksisterede skattehistorik, den politiske status quo, som en væsentlig moderator, når vi ønsker at forklare tværnational variation i forhold til, hvordan umiddelbart ligesindede politiske aktører vælger så forskellige reformløsninger, når det gælder indkomstskatten.

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