

**K**enneth Clarke and Michael Portillo have an unenviable task. Like George Bush and Helmut Kohl before them, they must swallow the anti-tax rhetoric of more than a decade and find resources to pay debts and finance the services and benefits their electors want.

The approach they have taken, with a secretive spending review, suggests that they believe their task to be primarily tactical. They are wrong. What is now at issue in this, the 2,500th anniversary of democracy, is not just an immediate question of which services will suffer and which taxes will rise, but a much deeper crisis of the legitimacy of representative structures.

Two hundred years ago, the great slogan was, "No taxation without representation". A wave of revolutions ushered in the modern era of national representative democracy. Our political system, based around parties, manifestos, budgets and national civil services, is a product of those revolts. But in recent decades its deficiencies have become ever more apparent, and it is in the field of tax, the decisive relationship between governments and governed, that they have come to the fore.

Since the mid-1970s, politics has been dominated by tax. California's Proposition 13, the rise of anti-tax parties from Norway to Canada, and a series of bitter elections, have all reflected an unmistakable public hostility to tax. Many interpreted this simply as a reaction to the rising levels of tax. But it was also, we believe, a revolt against the forms of tax: the consolidation of all into single pools under the control of treasuries, and the disconnection of taxes from services. It was a revolt against a system in which the main lines of accountability, of public services, health authorities and even local government, went upwards to national government and not downwards to those who used the services.

It is this disconnection which has undermined the credibility of governments and parties: when they call for higher taxes, few believe that the money will be well used. Instead, governments appear as a black hole into which resources disappear. The result is that they have become chronically unable to meet the rising costs of labour-intensive public services and a growing number of dependents, whether old, young or unemployed.

While there was still a consensus on state spending, as during war-time, or in the post-war reconstruction, pooling was not problematic. The shared sense of purpose helped to legitimise higher taxes. Since then the political, moral and administrative foundations of pooling have broken down. There is no longer a clear consensus about the priorities for welfare. A more consumerist society has become used to accountability. A less deferential public has become sceptical about handing blank cheques to government.

At the same time, administrative centralisation has lost credibility. It means that budget makers manage funds for activities from which they are far distant, using standard procedures which are ill-suited to the

# Power to the people in a tax revolution

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Essay

*The public is sceptical about handing blank cheques to the government, argue Geoff Mulgan and Robin Murray. Taxes should be earmarked for particular purposes by democratic consent*

diversities of need and provision. When cuts are made, it is the blunt axe of the Treasury and the secretive interdepartmental struggle which determine who loses. The irony is that at the very time when central planning has been decisively rejected in the East, budgetary centralisation is actually increasing in Britain.

What is now needed is a tax revolution far more profound than anything attempted in the 1980s. It needs the energy of previous reforms, like those at the end of the 18th century which ended the arbitrary privileges of feudalism, or those of the late 19th century which consolidated the tax system around income tax and redistribution.

Like them, the next wave of reform will be driven by two factors: the relentless upward pressures on public spending and the need to legitimate government. Like them, it will in part be designed to address a democratic deficit.

**I**t's central theme will be the remaking of connections. There are three ways in which this can be done. The first is by earmarking, or hypothecating, taxes for particular purposes: tobacco taxes for health, pollution taxes for environmental investment, fuel taxes for public transport, graduate taxes for universities, or insurance systems which transfer tax between different stages of the life cycle. Earmarking helps to clarify the relative virtues of different

kinds of spending, building legitimacy through the connections it makes. It has relevance right across the range of public provision, even redistribution. At the moment, those who vote for tax cuts can be among the first to contribute to Comic Relief. They send in their cheques because there is a clear link between action and effect and because they trust the body concerned. Tax pooling prevents these connections; hypothecation would remake them.

Hypothecation renders services more independent of central budgetary processes. It encourages providers to look outwards, to the public they have to convince and to the funding sources on which they depend. This is why the Treasury and many senior politicians are so hostile to it. But the political advantages should also be recognised. President Clinton's recent decision to earmark increased taxes on the wealthy to a trust fund to pay off the deficit helped to defuse the growing campaign against his tax proposals.

The second step is to link earmarking to democratic consent. This is the simplest way to determine the services which voters value. The national health service is one example where voters could be offered alternative funding options for earmarking income taxes to health in a referendum. London Underground is another example where support for the £300 million investment needed to transform it from an ill-main-

tained and inefficient system into one of world class could be tested in a poll of citizens and businesses. In each case, since central government cannot provide the funds, there is a clear case for passing choice and responsibility downwards, sharing parliament's sovereignty with citizens.

A third principle of reconnection is subsidiarity: devolving the power to set taxes to the lowest appropriate level. This has been common in North America and in Europe. In the UK the movement has been the other way, and local government now raises only 14 per cent of its own revenue. The flaws of the present system are shown in Harlow, where the government is now imposing a 50 per cent budget cut in spite of a petition signed by 20,000 people, 40 per cent of the town's adult population. The alternative is simple: councils would be allowed to hold a local poll on budgets and set in excess of government limits, an idea proposed by Michael Heseltine in 1981 and put into practice by Tower Hamlets in 1992 and 1993, when voters chose the highest tax and spending option on offer. Local democracy could then be further enhanced by giving councils and voters the right to gather signatures to put proposals on the ballot paper for such things as the provision of new nursery places or an Olympic bid.

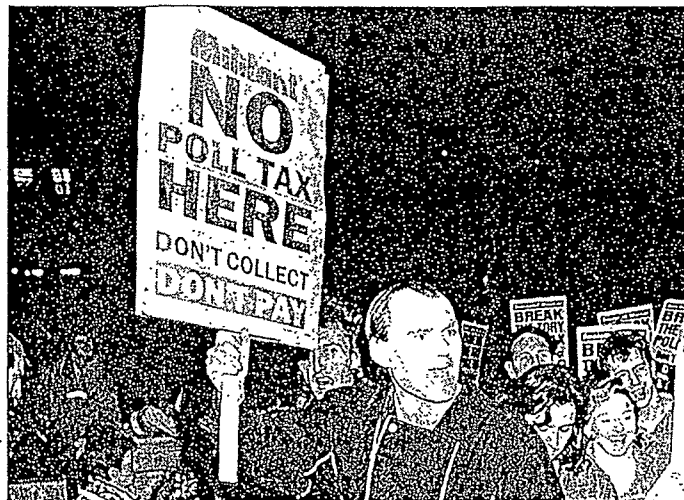
**E**ach of these measures would introduce a new discipline in local government. Inefficient, corrupt and unresponsive services would suffer. Entrepreneurial managers and workforces who met new needs would be rewarded. The crude centralist disciplines of the 1980s would be replaced with a tougher, more relevant discipline. Above all, local civic life would be revitalised with a more varied set of connections than is offered by an occasional vote at elections.

In the past, fiscal crises have reflected deeper political crises. This was the case in England in 1640, in America in 1776, in France in 1789 and again in Britain in the constitutional crisis that followed Lloyd George's budget in 1909.

Today's crisis is also in large part political. It has been brought to a head because the lumbering party and electoral system is no longer up to the job of transmitting the complex preferences of a modern electorate. It cannot restore the credibility of the centralised budget, the party manifesto and the secret spending review.

Tax has historically been the midwife of democracy. For 200 years the trend has been towards the democratisation of the incidence of tax. But at the close of the 20th century the crucial question has moved on to democratising the tax relationship itself. The challenge now is for politicians to match their new enthusiasm for the reinvention of government with an even more far-reaching reinvention of tax.

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Taxing times: the community charge provoked heart-felt protests