Political Institutions and Taxation by the Left: Britain and Sweden Compared

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September 3, 2016

Abstract

This paper is concerned with the impact of ideology on taxation, focusing on left-wing parties and their strategies for redistribution. My argument is that the left is mainly concerned with redistribution – not progressive taxation per se – and when the left is in power, a range of policy tools are available to decrease inequality; taxation is only one of them. One strategy is to use consumption taxes to increase fiscal capacity, and spend the revenue on progressive social programs. This strategy is effective in terms of reducing inequality, but also entails risk because of the inter-temporal mismatch between taxing and spending. This risk is driven by reelection probability, political conflict, and opposition influence. When regressive taxation is perceived to be too risky, the left instead chooses progressive taxation as the main tool for redistribution. The proposed mechanism is evaluated in a comparison of Swedish and British tax policy during the decades following the Second World War. I find that while both strategies for redistribution were seriously considered, the combination of consumption taxes and progressive spending prevailed in Sweden while Labour in Britain chose the safer path of progressive income taxes. A key element of this result was the political risks involved.
The twentieth century saw revolutionary changes in the size of government and its finances. In a sample of mainly Western European and Latin American states, the average government share of the economy more than doubled from 1900 to 2012.\footnote{Based on government revenue data from 31 countries in Andersson and Brambor 2015. The countries included are: Argentina, Australia, Austria, Belgium, Bolivia, Brazil, Canada, Chile, Colombia, Denmark, Ecuador, Finland, France, Germany, Ireland, Italy, Japan, Mexico, New Zealand, Norway, Paraguay, Peru, Portugal, Spain, Sweden, Switzerland, The Netherlands, The United Kingdom, The United States, Uruguay and Venezuela} Not only did the sheer size of government increase, its composition changed radically: from a heavy reliance on trade taxation in the early twentieth century, to income tax mid-century, and finally to the global spread of modern broad-based consumption taxation.

These major changes in size and composition of government budgets coincides with equally dramatic changes in political systems: the rise of modern parliamentary democracy and parties representing the working class. This paper explores how these developments are related to taxation.

Interestingly, some find that countries with a long influence of left-wing parties and with a large welfare state tax the poor and the middle-class harder compared to countries with a smaller welfare state and a weaker left. This puzzle has provoked considerable interest in political science and fiscal sociology more generally. Existing explanations argue that the left is constrained by corporatism (Beramendi and Rueda 2007), emphasize employer organizations (Martin 2015), highlight executive/legislature relationships (Cusack and Beramendi 2006), and the role of tax compliance (Timmons 2010).

I propose that this counter-intuitive pattern – that the left taxes regressively – is the result of different strategies for redistribution. The first strategy is using progressive taxation as the main vehicle for lowering inequality, while the second focuses on revenue maximization and generous transfers. Which of these strategies the left chooses depends on the risks involved, which in turn are a function of the institutional context.

One such institutional factor affecting tax strategy is the electoral system, and a closer inspection of the data indeed reveals that the association between left-wing governments and
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regressive taxation is different in these two institutional contexts. Figure 1 shows the average share of government revenue from taxes on consumption and income in democracies with a left-wing head of government during the twentieth century. The familiar, counter-intuitive pattern only emerges in countries using a proportional representation electoral system. In majoritarian countries on the other hand, left-wing governments rely much more on income tax. It is clear that the association between the left and regressive taxation is only present in countries using a proportional representation electoral system.

The majority of earlier research focus on macro correlations among a large number of countries, presenting similar findings as support for different theoretical claims. By mapping the motivations and actions of key actors in sequence, I seek to distinguish which of the proposed mechanisms has most explanatory power. The theoretical argument is evaluated against existing explanations for left-wing taxation by exploring tax policy in Sweden and

\footnote{The definition as well as the data for democracy is from ?}
the United Kingdom during the decades following the Second World War.

The next section presents the argument, followed by a brief summary of alternative explanations. After that I present my empirical strategy, followed by the two case studies. The final section concludes.

1 Why and When the Left Taxes Consumption

How resources should be distributed among citizens is one of the main differences between parties to the left and parties to the right. While earlier research sometimes equate a preference for equality with progressive taxation, this is not as straight-forward as it seems (Buchanan 1949). Instead, I start with the more general assumption that left parties are characterized by a preference for lower economic inequality. How this goal is achieved is another matter. Redistribution is not only about taxation, it also concerns spending.

Following established conventions in the literature, taxes on consumption (e.g. excises and general sales taxes) are taken to be regressive while taxes on income are considered progressive (see for example Prasad and Deng 2009 and Timmons 2010). Spending also varies in distributive impact. For example, transfers tied to former income (such as some unemployment benefit schemes) are less progressive than flat rate benefits such as (many) child care benefits. The following discussion is concerned with spending specifically aimed at the poor or with a clear redistributive purpose.

It has been shown that a less progressive, but higher yielding tax system, combined with redistributive transfers is a more effective way of lowering inequality than a highly progressive but low yielding tax system (Engel, Galetovic and Raddatz 1999). Thus, there is no paradox in left-wing governments relying relatively more on regressive taxes. This is especially the case if one sees consumption taxes as conducive to economic growth; the left will not oppose regressive pro-growth policies as long as the added revenue will be used to compensate the losers (Lindert 2004 p. 305). Moreover, taxes on consumption are cheaper

3There is a growing literature on the positive effects on economic growth of shifting taxation unto con-
to collect \cite{aizenman2008, bird2005} and lead to less tax evasion \cite{gordon1997}.

Since redistribution can be achieved in a number of ways, simply assuming (explicitly, or as is more common, implicitly) that the left prefers taxes on income over taxes on consumption is problematic. For example, if a left-wing government introduces a value-added tax (VAT) and lowers the rate of income taxes, this can be an attempt to increase revenues and the overall efficiency of the tax system in order to fund highly progressive social programs. It does not necessarily mean the left is constrained (c.f. \cite{beramendi2007}).

Having established that there is no inherent contradiction in having a preference for economic equality and taxing regressively, I now turn to explaining differences in left-wing tax policy with reference to political risk. The strategic situation facing any party contemplating tax reform is undeniable shaped by the institutional environment. This environment also affects the government strategy indirectly by influencing the actions and strategies of opposing parties.

This paper focuses on the inter-temporal aspect of tax reform; that choices today can have important distributive consequences tomorrow. The government needs to consider what happens in a time period where it is no longer in power. This means that political uncertainty over future distribution of power is a central issue with regards to redistributive policies. What an actor does today affects the actions possible for whoever is in power tomorrow. For example, introducing a new tax in period 1 means an additional instrument available in period 2 that will not necessarily be used to benefit the voters of the party in power in period 1. If there are short-term start-up costs associated with the new tax, this shifts the benefits of the policy from the near to the far term, aggravating the temporal uncertainty. Even though a powerful tax instrument can be used for good, it can also be used by your enemies to hurt you. This is a risk that politicians are very aware of. As Senator Marco Rubio put it in one of the Republican primary debates in January 2016, pointing out

\footnote{sumption, see for example \cite{auerbach2006, lee2005, widmalm2001}.}
the risks of introducing a VAT: “...what is to prevent a future liberal president or a liberal Congress from coming back and not just raising the income tax, but also raising that VAT tax”.

Compensating low-income workers for the regressive effects of consumption taxation in practice means expanded social programs such as old age pensions, unemployment benefits, and support for families. For many voters these programs are only valuable under certain circumstances (in the case of unemployment benefits) or in the future (pensions). Thus, while the increase in consumption taxes are felt immediately, the compensation is not realized until later.

If the left anticipates no influence after losing power, and if elections are inherently uncertain, the low-risk option is progressive taxation. However, if elections are more predictable and opposition parties more influential, then the combination of regressive taxation and progressive taxes becomes more attractive.

The risk associated with the temporal mismatch between taxing and spending is a function of several factors. Arguably the most important is opposition influence. When determining tax and spending policy, the government needs to consider what happens if it loses power in the next election. For example, a system with many veto points provides several avenues for the opposition to still affect policy. Opposition influence is also affected by the level of support the government has in the legislature: a minority government frequently needs to negotiate with other parties in parliament to legislate. But, risk is not only affected by what happens when out of power, it is also related to expectations of actually losing it. A strong majority in the legislature, favorable opinion polls, and a long time period to the next election all lower the electoral risks associated with tax reform.

Opposition influence is more important if the preferences of the main political adversaries are highly divergent. That is, if the right vehemently opposes the economic policy and vows

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4The same fears have also been expressed by democrats. Steinmo (1993, p.199-200) reports this quote from a United States Senate staff member: “This is not Sweden. How can we be sure that that extra money won’t just be used to cut the taxes of the rich even more, or to buy more B-1 bombers?”.
to remove a certain tax or subsidy if they win the next election, the stakes are much higher than if a certain consensus exists on the issues. The risk is also tied to public opinion and vote share. If a left-wing government perceives its ability to win the next election as favorable, the risks associated with a (potentially) unpopular tax decision is lower.

Electoral systems are related to several of these aspects: proportional representation is associated with a higher frequency of minority governments, more veto points (in the form of coalition partners), and more predictable election outcomes. A majoritarian electoral system on the other hand, is more volatile since a small change in voter preferences can have a substantial impact on the outcome of the election and ultimately on policy. This system also manufactures strong single-party majorities with little or no influence for the opposition (Powell 2000). Proportional representation systems on the other hand do not exclude opposition parties to the same extent. Rather, post-election bargaining and opposition influence between election reduce policy volatility (ibid.). These effects of the electoral systems are important because they affect the temporal distribution of costs and benefits of different strategies for redistribution.

In sum, taxing consumption can actually be a step towards more effective redistribution and thus not a departure from the core values of the left. The decision whether to shift taxation in a regressive direction is a strategic one that depends on political risks. These risks in turn are driven by reelection probability, political conflict, and opposition influence. These three factors are affected by political institutions such as the electoral system and veto points.

In low-risk environments, the argument predicts left-wing governments pushing for taxes on consumption (either in the form of new taxes or changing rates) in conjunction with progressive spending. High-risk environments on the other hand, changes the strategy of the

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5The argument about opposition influence and uncertainty could be connected to voter preferences. Barnes (2015) shows that low trust is associated with preferences for a smaller government but a more progressive tax system. Volatility and sharp swings in policy should decrease the trust the poor have in receiving compensatory spending, making them prefer progressive taxation and a smaller state. This is especially true when the size of the state cannot be increased using income taxes anymore, so expanding the state necessarily means higher regressive taxation.
left and leads to a heavier reliance on progressive taxation.

2 Taxation and Redistribution: Historical Roots and Recent Evidence

The traditional view of the relationship between ideology and taxation holds that parties to the left act in the interest of the poorer segments of society, and thus push for progressive taxes on income and wealth (see e.g. [Hibbs 1977] and [Cameron 1978]).

This view has been challenged by empirical work showing that countries with strong influence of left-wing parties actually tax more regressively (e.g. [Kato 2003]). These findings have sparked efforts to explore the relationship between the left and indirect taxation, empirically as well as theoretically. The main puzzle is why parties to the left expands the welfare state and simultaneously tax their core constituency relatively harder. Why not work for redistribution on the expenditure and the revenue side of the budget?

Since the association between left-wing government and taxes on consumption coincides with the rapid growth of welfare spending, it has been argued that indirect, regressive taxation allowed left-wing parties to expand government even more ([Kato 2003]). However, the direction of causality is debated; an ever growing welfare state needs financing, and even the income tax has a limit in terms of revenue generated. A shift towards consumption taxation can thus be a function of increasing spending pressure ([Ganghof 2006]).

An alternative explanation comes from the fiscal contract theory. The theory posits that the party in power is more likely to tax its own voters since tax payers engage in less tax avoidance/evasion if their preferred party is ruling. That is, a left-wing voter trust that a left-wing government will use the taxes to benefit left voters and thus is less prone to engage in tax avoidance. This is also the case for right-wing governments and business interest. The key argument relies on the assumption that minimizing avoidance is a prime concern and that the fiscal contract between a party and its voters can reduce this behavior. Empirical
findings suggests left-wing governments tax consumption more, but only when there is low partisan turnover (Timmons 2010).

The argument made in section 1 of this paper shares some of the intuition with the ideas in Cukierman and Tommasi (1998) and Cowen and Sutter (1998), arguing that when a party implements a policy thought to be in the opposite direction of its ideological biases – for example a socialist government introducing a VAT – the public is more likely to believe that the policy is objectively good and less prone to punish the government in the next election. It is harder for a right-wing government to push regressive taxes since this would be seen as a purely ideological move and be more intensively opposed. This effect becomes more important with more veto players since the credibility of the policy becomes more important when an ideological opponent needs to be convinced (Cowen and Sutter 1998).

However, they consider a case where the policy is objectively good, not different strategies for redistribution.

Another explanation for the seemingly puzzling relationship between the left and regressive taxation argues that corporatism constrains the tax policies available to the government. The left is forced to finance increased welfare spending through regressive consumption taxes since taxing labor or capital income would result in increased wage demands and lower investments respectively. Thus, unions and capital interest constrain the left because increasing taxes on labor and capital will terminate the corporatist agreement. Since capital can credible threat to exit (through global capital markets), taxes fall heavier on labor, effectively making labor pay for the welfare state through regressive taxes on consumption. In a low corporatism environment, the left can tax how it pleases and then chooses to tax income and capital rather than consumption (Beramendi and Rueda 2007).

A related argument from Cusack and Beramendi (2006) posits that the effect of left-party government on the average effective tax rate on labor is muted when the executive dominates the legislature. This is the case since these systems often use majoritarian electoral systems

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6A related argument is that objectively good policies can be implemented in systems with many veto players as long as compensation is possible (Lindvall 2010).
that gives relatively more influence to the median voter. Moreover, the degree of wage coordination is important since this leads to higher government expenditures that needs to be borne by labor since capital is mobile. This argument is similar to the one in Beramendi and Rueda (2007), but adds a constitutional dimension, emphasizing institutional complementaries between corporatism, electoral systems, and partisanship. Interestingly, empirical work contradicts the central assumptions regarding electoral systems and the median voter: majoritarian systems are associated with larger swings in policy and proportional representation systems produce policy closer to the preferences of the median voter (Powell 2000, ch. 9).

Hicks’ (2013) explanation for divergence in Swedish and British health-care policy emphasizes how the majoritarian system in Britain was associated with large swings in policy while Sweden (thanks to PR) was more stable. Moreover, this meant that Labour “...could expect unconstrained conservative rule in the near future.” while the Swedish Social Democratic Party (SAP) “...had far less to fear from a right-wing government.” (ibid. p.213, see also Heclo 2010, ch.1). While this hints at the importance of opposition influence, Hicks does not elaborate on this issue. Moreover, explaining how spending programs are implemented are very different from distributional conflicts related to tax reform. For example, while policy insulation (e.g. de Figueiredo 2002) might have an impact on the design of health care systems, it is less important for the development of tax structure.

In sum, earlier research points out a number of different mechanisms connecting left-wing governments with tax policy: from spending pressure, via credible commitments, tax avoidance and ideological biases to institutional factors such as union influence and constitutions.

3 Empirical Strategy

The purpose of this case study is to evaluate the casual mechanism proposed in section 1. Since the goal is to illustrate how institutional factors affect risk through opposition influence,
and in turn what decisions are made with respect to taxation, variation in institutions is key. Constitutional features such as regime type and electoral system rarely changes within a country, which means that a single-country case study must be ruled out. Studying two cases allows me to investigate the conditional impact of ideology on taxation by comparing left-wing tax policy in two different strategic environments.

The post-war years mark the beginning of a period of accelerated welfare state development with a number of reforms related both to taxation and spending. During this time there were key developments in the balance between direct and indirect taxation, culminating the introduction of the value-added tax (VAT). Moreover, tax policy making during this era had a profound impact on the future tax structure.

The most important aspect when choosing cases is that they should be similar with regards to left-wing preferences. If the major political conflict is not distributional, or if the preferences of the left are not primarily to decrease economic inequality, the cases would not be suitable for studying the proposed mechanism. After the Second World War, both Sweden and the United Kingdom were ruled by strong left-wing governments. Importantly, Labour and the Swedish Social Democrats (SAP) had similar preferences with regards to taxation: both advocated for heavier taxation of the rich as a way to fight economic inequality (SAP election manifesto 1944, Dale 2000, p.49f). Moreover, trade unions had significant influence over both the SAP and Labour.

The key intervening variable in my theoretical argument is opposition influence. The left is hypothesized to employ different strategies for redistribution depending on how political institutions shape opposition influence. During the post-war era Sweden operated a proportional representation electoral system, leading to frequent minority governments and coalitions granting significant influence for the opposition. Another effect of the electoral system is that the Social Democrats were facing a right divided among three different parties (the Conservatives, Agrarians, and the Liberals). In contrast, British institutions were characterized by strong concentration of power and low opposition influence. The majoritarian
Table 1: Mean tax shares

<table>
<thead>
<tr>
<th>Tax share</th>
<th>Sweden 1945-1975</th>
<th>United Kingdom 1945-1975</th>
</tr>
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<tbody>
<tr>
<td>Income</td>
<td>47.8</td>
<td>48.9</td>
</tr>
<tr>
<td>Excise and Consumption</td>
<td>38.6</td>
<td>26.6</td>
</tr>
</tbody>
</table>

Sources: Tax shares are from Andersson and Brambor 2015.

electoral system frequently resulted in strong one-party majorities in parliament. If Labour lost, they knew the incoming government would be an unconstrained Conservative one with minimal opportunity for Labour influence. Of the seventeen elections between 1920 and 1980, fourteen resulted in single party majorities, but in only two cases the winning party got a majority of the popular vote (Butler and Butler 2010). In contrast, in the nineteen Swedish elections between 1920 and 1980, there were only one single-party majority government (after the 1968 election). The period is otherwise dominated by single-party minority governments and coalitions (both majorities and minorities) (Hadenius 2003).

An advantage of comparing Britain and Sweden is their similarity on a number of other variables that could affect taxation or mediate the impact of ideology on tax policy. First, many potential cases of left-wing tax policy in majoritarian democracies are also presidential and federal states, factors that could potentially change how ideology and tax policy are related. Both Britain and Sweden are unitary constitutional monarchies. Second, since Britain was victorious and Sweden neutral during World War II, there was political continuity and the left did not come to power as a result of a radical reshaping of the political system.

Sweden and the United Kingdom fits the quantitative pattern in Figure 1 well. Both had strong left-wing governments during the post-war period but Sweden – with institutions granting more opposition influence – had a stronger reliance on regressive taxation than Britain (with strongly majoritarian institutions). Table 1 shows the mean shares of income and excise and consumption taxes for the two countries in the period from the end of the Second World War up to 1975 (when both countries had established a VAT).

Studying Sweden and the United Kingdom allows me to evaluate the proposed mechanism
in two different institutional contexts. It is important to stress that the purpose of the study is to evaluate the causal mechanism, not the causal effect. In writing the case studies I follow the advice of Bates et al. (1998) and pay particular attention to whether the assumptions fit the facts, if the theoretical implications are supported by the data, and how well my argument stands up by comparison with other explanations.

The political party/coalition making up the government is the most important actor to consider since it is effectively setting tax policy. Although the focus is on left-parties, the preferences of parties to the right are also important as they affect the risk assessment of the left. I also pay special attention to interest organizations such as trade unions and employers organizations. As earlier research has shown, these two groups are crucial in explaining tax policy change (see e.g. Martin 2015, Beramendi and Rueda 2007). With that said, it is important to remember that the parliament sets tax policy, not unions (Bradley et al. 2003).

4 Labour Post-War Tax Policy

Traditional Labour priorities were “...fairness, equality and redressing the balance between rich and poor”. (Whiting 2000, p.172). In order to reach these goals – and especially the last one – Labour had been advocating for heavier reliance on taxes on income relative to taxes on consumption. As a general principle, this stance worked well in the 1920s and 1930s when most Labour voters did not reach the minimum income required to pay income tax. However, the Second World War resulted in an unprecedented increase in taxation, and when Clement Attlee was appointed Prime Minister in 1946 the first priority was to return Britain to peacetime public finances; this meant lowering taxes, especially on income. Consequently, in 1947 Labour lowered the standard rate of income tax from 50 to 45 per cent (Thorpe 2008, p. 123). This was not as counter-intuitive as it seems since the income taxes were so high, and so broad, that they affected Labour voters as well. Moreover, Labour had identified middle income workers as crucial electorally; this was the group most likely to swing Tory.

\footnote{In this sense my cases could be seen as what Gerring and Seawright (2006) calls “pathway” cases.}
Table 2: The Attlee Government: 1946-1951

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</tr>
</thead>
<tbody>
<tr>
<td>Income</td>
<td>56.2</td>
<td>48.8</td>
<td>44.1</td>
<td>45</td>
<td>46.6</td>
<td>44.2</td>
<td>47.3</td>
</tr>
<tr>
<td>Property</td>
<td>3.6</td>
<td>4.5</td>
<td>4.8</td>
<td>4.6</td>
<td>4.8</td>
<td>4.6</td>
<td>4.1</td>
</tr>
<tr>
<td>Customs</td>
<td>16.9</td>
<td>19.1</td>
<td>22.2</td>
<td>21.2</td>
<td>20.5</td>
<td>22.3</td>
<td>22.1</td>
</tr>
<tr>
<td>Excise</td>
<td>16</td>
<td>17.3</td>
<td>17.7</td>
<td>18.9</td>
<td>17.8</td>
<td>17.8</td>
<td>16.7</td>
</tr>
<tr>
<td>Consumption</td>
<td>5.4</td>
<td>7.6</td>
<td>8.2</td>
<td>7.5</td>
<td>7.6</td>
<td>8.3</td>
<td>7</td>
</tr>
<tr>
<td>Social Spending/GDP</td>
<td>.</td>
<td>.</td>
<td>.</td>
<td>10.7</td>
<td>9.9</td>
<td>9.6</td>
<td>.</td>
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<tr>
<td>Social Spending/TE</td>
<td>.</td>
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<td>39.6</td>
<td>35.6</td>
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</tr>
</tbody>
</table>

Sources: Tax shares are from Andersson and Brambor 2015 and data on social spending from Flora, Kraus and Pfenning 1983. All figures are for central government.

Consequently, income tax reductions were specifically aimed at this group. The tax relief was financed by increased excises on tobacco, fuel, and beer. In order to compensate the poor for the effects of increased excises, Labour kept – and even increased – food subsidies (Whiting 2000, p. 90-100).

These changes in rates are also visible in the overall budget. Table 2 shows the development of British tax revenue and its sources as well as the evolution of social spending from the first year of the Attlee government to the first year of the succeeding Churchill ministry. As Table 2 clearly shows, the largest change is the decrease of income taxes, reflecting the extraordinary situation during the war and the transition back to peacetime taxation. Interesting to note is that this decrease is almost entirely compensated for by increases in indirect taxation. Importantly, the consumption tax – called purchase tax – had differentiated rates and was primarily aimed at luxury goods. Thus, it was a consumption tax but with decidedly progressive elements. While keeping the tax after the war, in 1948 Labour decided not to broaden the base of the tax since it was “not politically defensible”. (Whiting 2000, p. 91). Overall, the macro patterns show a fairly regressive development during the Attlee era. However, it is important to point out that any post-war government was bound to reduce income taxation.

An important external factor during the Attlee government was the high level of inflation. This led to bracket creep in the income tax, pushing more and more working class people
into the system. For Labour, this was not seen as a problem electorally, while changing the actual brackets was (Whiting 2000, p. 120). Inflation was also used to motivate increases in a number of excise taxes.

Another central issue during this period was tax evasion and its connection to equality. It was generally believed that the rich could easily evade the income tax by transforming their income to capital gains, which was not taxed at the time. Within the Labour party, two solutions were discussed: 1) increased government ownership in the economy and 2) strengthen administrative capacity. Since the first solution (championed by, among others, Aneurin Bevan), was seen as too risky as it would empower the state to an extreme, Labour pushed for the second strategy. Taxing capital was high on the Labour tax agenda, but the current administrative capacity was a barrier (Whiting 2000 p.125f).

In sum, the post-war situation meant Labour was tasked with lowering taxes. They way it did this signals clearly that Labour still first and foremost was a union pressure group, but also that electoral incentives played a role. The reduction in income taxes benefited the lower middle class the most. However, the failure to introduce a tax on capital gains and/or wealth was cited later as main contributor to rising inequality, and shaped the debate during the following years in opposition.

**In Opposition**

The election of 1951 resulted in the greatest vote share in Labour history, 48.8 percent, but the 13 948 883 votes only resulted in 295 seats, while the Conservatives’ 48 percent of the votes produced 321. Thus, despite being rewarded in the polls, Labour lost the election (Thorpe 2008, p. 140).\(^8\)

The incoming Tory government shifted economic policy in a different direction: food subsidies were removed, income taxes decreased, but – as a result of union pressure – wages were increased and a short-run capital gains tax introduced (however, union efforts to lobby for a reformed corporate tax failed) (Whiting 2000 p.155). For the Tories, the capital gains

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\(^8\)These dramatic results caused by the electoral system were not uncommon in Britain, and is an important difference between British and Swedish politics (e.g. Heclo 2010, p.37).
tax was mainly seen as an anti-avoidance measure. In general, the Tory fiscal policy followed the already established pattern and no major changes were made. Tax policy was used as a way to appease unions for wage moderation, rather than providing incentives (Daunton 2002, p.264).

During the time in opposition Labour reevaluated its tax policies. There was a consensus that the income tax was both inefficient and unfair: wide-spread avoidance among top income earners had severely undermined its purported progressivity. Ideas discussed at the time were a new income tax based on assessed spending power, a tax on capital gains, and a reformed corporate tax. Labour also shifted focus towards inequality and fairness, and how to achieve redistribution through taxation rather than nationalization. Importantly, ideas concerning the effectiveness of taxation and its impact on revenue started to emerge. Anthony Crosland stated that what he called ‘socialist’ taxes “should therefore enable us to consider...certain elastic and high yielding indirect taxes – a general turnover tax, a differential payroll tax, or a graduated and much higher employers’ national insurance contribution ... For what matter is the total progressiveness of the tax system – and, if we want to redress its total imbalance, its total yield” (quoted in Whiting 2000, p.151). Another challenge to Labour tax policy orthodoxy came from Richard Titmuss, who argued that since the fairness of the income tax was undermined by extensive avoidance revenue must be found elsewhere (ibid. p.152).

Hugh Gaitskell, shadow Chancellor from 1951 until 1955 (when he became leader of the opposition), also acknowledged that increasing redistribution through the income tax alone was no longer possible, and instead turned his attention towards property as the main culprit of inequality (Ellison 2002, p.86). A proposed capital levy was considered inviable in terms of public opinion and the prevailing position in the later 1950s was in support for a capital gains tax, a tax on gifts, and taxation of unearned incomes. (ibid. p.87f).

In sum, intense debate and deliberation within the party during the opposition years prepared Labour for vigorous reforms when they returned to power after winning the 1964
general election. Importantly, while broad-based consumption taxes were discussed, momentum shifted in favor of taxes on capital.

The 1965 Budget

The first budget under Prime Minister Harold Wilson in 1965 was a big deal: it drew intense opposition and took twice the time in parliament as normal budgets (Whiting 2000, p.160). The budget was not only concerned with raising revenue and minimizing avoidance, but also with making the tax system fairer.

The budget reformed the corporation tax, but the changes did not have a noticeable impact on inequality; the new rate was even lower than the earlier combination of income and profits taxes, but the revenue from the tax remained the same.

Labour also introduced a comprehensive capital gains tax (both long and short term), partly in order to compensate unions for wage restraint (Daunton 2002, p.292). Since the bill was so heavily opposed, Labour also had to make a number of concessions to business interests. One of these was to set the capital gains tax rate at 30 per cent, which was lower than the standard income tax rate (Whiting 2000, p.163). The capital gains tax was more aimed at reducing avoidance than redistribution, and this coupled with an increased awareness of inequality and the failure to introduce a tax on wealth led to disappointment among the more radical members of the party.

Critics within the party argued that the emphasis on avoidance would lead to an overly intrusive tax administration and that the budget was too harsh on small business. Instead, they argued for a broad-based consumption tax and lower income taxes. The Labour leadership was aware that even though the income tax had turned out to be a money machine, it increasingly hit the low-and middle classes. But instead of considering the alternatives, in 1965 Labour made the income tax more progressive and increased efforts to combat avoidance (ibid. p.167). However, according to Whiting the 1965 budget was more an attempt to legitimize income tax and it did not seek “...to redistribute wealth in the traditions of some of Labour’s earlier tax ideas” (ibid. p.171.).
The years following the budget were characterized by tax reform fatigue; there was broad consensus that a break was needed not only because of the fierce resistance to the 1965 budget but also in order for the tax administration to catch up. During these years the value-added tax (VAT) rose to the top of the agenda. (ibid. p.171). The Confederation of British Industry (CBI) was concerned about the level of government expenditure and its relation with higher direct taxes, which it argued had an adverse impact on incentives. Instead, the CBI argued for lower expenditures overall and a shift from direct to indirect taxes (ibid. p.193).

As emphasized above, poverty was no longer a clear and simple class issue, meaning that reducing inequality was no longer only about taking more from the rich, but also about spending more on the poor. This meant taxing union members. At the same time better empirical evidence on the incidence of indirect taxation started to emerge, showing just how hard the poor were hit by taxes on consumption. These findings in combination with the rising influence of academics such as Titmuss within the new field of social policy put the poor high on the agenda. This led to increasing tensions within Labour between representing the unions and reducing inequality, and slowed down Labour’s efforts to redistribute from the middle to the poor (\textit{Whiting 2000} p.173ff). Nevertheless, reduced inequality as a result of government tax and spending policy did occur in the 1960s, and there were real improvements for the poor (ibid. p-181-183).

\textbf{VAT or SET?}

Early in its term (starting 1964), Labour was in dire need for a solution to Britain’s balance of payment problem (\textit{CAB/129/121} 1965). Since it did not want to devalue the pound sterling, other measures such as changes to the tax system had to be considered. A value-added tax was first proposed as a way of offering export incentives without violating the rules of the General Agreement on Tariffs and Trade (GATT). But critics pointed out that the existing purchase tax did not fall on exports, so replacing it with a VAT would not be an improvement.
Regardless, there were other advantages with the VAT. First, to squeeze more revenue out of the income tax Labour would be forced to tax the less well off harder, which would lead to demands for wage increases. Moreover, Labour had explicitly ruled out any increases in the income tax in a public statement before the 1966 election (Whiting 2000, p.197f). A VAT would solve the revenue issue without these problems. Second, subjecting more goods to the purchase tax would mean Labour needed to motivate and fight for every new good included. Introducing a new broad-based tax on consumption, covering most goods and services (not covered by the purchase tax) would be more expedient politically (Daunton 2002, p.294). However, Labour had traditionally been hesitant towards taxes on consumption because of its regressiveness and had made sure that the purchase tax contained progressive elements (e.g. higher rates on luxury goods) (Whiting 2000, p.197). In 1963 when the National Economic Development Council (NEDC) suggested a VAT linked with abolished profits tax in order to boost economic growth, Labour fiercely criticized the proposal’s detrimental effects on equality (Daunton 2002, p.289).

An alternative was put forth by the economist Nicholas Kaldor, who proposed replacing social contributions with a VAT. The argument was that although a VAT was less progressive than the income tax, it was not as regressive as the current system of indirect taxes and social insurance contributions. Kaldor also pointed out that the VAT would raise considerable revenues with less distortion of production and consumption. His proposal was met with heavy resistance from the Treasury, Customs and Excise, the Board of Trade and the Department of Economic affairs. The main issue was the fact that contributions fell on labor, while the VAT would shift costs to groups outside of the labor force, such as married women and pensioners, and this was considered politically dangerous. Moreover, Customs and Excise were concerned about the administrative costs associated with the new tax (Daunton 2002, p.295f).

Kaldor quickly returned with a new plan: the Selective Employment Tax (SET). The tax – introduced in 1966 – was paid by the employer based on the number of employees, with
tax rebates to the manufacturing sector. The SET would encourage reallocation of labor from the service sector to manufacturing, as well as raising revenues (which would partly be used to subsidize exports) (Whiting 2000, p. 198). Most importantly, it would be much more politically palatable than a VAT (Daunton 2002 p.297f).

The question of the VAT in Britain was also intimately connected to the European Economic Community (EEC), since membership required the introduction of a VAT. The CBI advocated for the VAT and a lowering of income taxes prior to a possible entry into the EEC in order to enhance competitiveness of British firms (Rollings 2003, p. 235). Likewise, the Conservatives supported British membership as well as a VAT (Lynch 2003 p.59).

In connection with Britain’s second application to the EEC a report was sponsored investigating the impact of introducing a VAT. Despite the expectations of Prime Minister Wilson, the report recommended not to introduce the VAT – although it acknowledged that a VAT would solve the revenue problem – for three reasons: 1) Britain did not have the problem with cascading turnover taxes that made other European countries advocate for the tax, 2) introducing the VAT would mean a significant increase in administrative costs, and 3) a VAT would not contribute to industrial efficiency the way the SET was claimed to do. Since the second application was also vetoed by de Gaulle, the report was never discussed in the committee (Whiting 2000 p. 204).

However, the failed application to the EEC was not the only reason for Labour being reluctant to introduce the VAT: the Trades Union Congress (TUC) strongly opposed it. The main complaint was, unsurprisingly, the regressive impact of the tax. In negotiations with the CBI in the NEDC, the TUC demanded a number of compensatory measures for accepting a VAT, one of which was a wealth tax. This demand effectively halted negotiations since the CBI was firmly opposed to any taxes on wealth. The lack of a clear plan of compensation made the TUC very suspicious of the VAT. This insecurity regarding compensation was acknowledged by the director of the NEDC (Fred Catherwood) who wrote to the TUC

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9The first application was submitted by the Macmillan ministry, but was vetoed by Charles de Gaulle in 1963.
representative: “What would happen would very much depend on the mixture of taxes and social benefits at the time and I still think it possible that a non-regressive, non-inflationary mix could be devised. However, I can well understand your lack of enthusiasm for the risks of a major change like this” (quoted in Whiting 2000, p.204). This is a clear example of how regressive taxation can be compensated for by spending, but when the uncertainties are deemed too high for key actors to be willing to take the risk.

**Conclusion**

The main reason the left was hesitant towards the VAT was its regressive impact. Even though it was acknowledged that the regressive effects could be compensated, a move towards a VAT was deemed too risky. The risks associated with the VAT were especially salient for the TUC, which apparently did not trust that Labour would be able to compensate its members for the costs associated with a VAT. This is hardly surprising given that Labour would have had no influence if they lost the next election.

**5 Swedish Post-war Tax Policy**

**Background**

During the Second World War all parties in the Swedish parliament (the Riksdag), except for the pro-Soviet Communists, were represented in government. The Social Democrats (SAP) were victorious in the 1944 election, but the war-time government remained in office until the end of the war. When SAP Prime Minister Per Albin Hansson died in 1946 he was succeeded by Tage Erlander, who went on to lead the country for the next twenty-three years.

When the war ended, consensus among all political parties was that Sweden should return to peacetime taxation, which meant removing temporary taxes and lowering others. The SAP tax policies were heavily influenced by – and debated with – the Swedish Trade Union Confederation (LO) and two prominent LO economists: Gösta Rehn and Rudolf Meidner.
Post-war Tax Reform

The need for sharply increased spending during the Second World War led to the introduction of a temporary sales tax (the “Oms”). The universally disliked tax – especially among the left-wing parties who criticized its regressivity – was abolished in 1947.

Traditionally, the SAP was skeptical towards indirect taxes which were seen as regressive and unfair. The 1944 party program (in effect until 1960) explicitly called for progressive taxation, redistribution and taxes on wealth. In an economic environment with stable prices and high brackets for the income tax, shifting taxation from indirect taxes to direct meant that better off citizens paid more. However, inflation led to bracket creep, pushing more and more lower income earners into the income tax. As if this was not enough, tax evasion at the top was rampant, with the well-off having little problem transforming their income from wage to capital. This prompted the labor movement to reevaluate its stance on indirect and direct taxation.

Interestingly, the SAP finance minister overseeing the removal of the Oms – Ernst Wigforss – later described the abolition of the tax as a mistake driven by political necessity. Wigforss’ states that because the SAP was already committed to lowering income taxes significantly, it ruled out keeping the Oms since it would not be possible to lower a progressive tax like the income tax and at the same time keep a regressive consumption tax, especially not since SAP had a very narrow majority in the parliament (Wigforss 1954, p. 336ff.).

But it was not only actors within the ruling left-wing party that mourned the demise of the Oms, as early as 1946, Gösta Rehn and Rudolf Meidner – prominent LO economists – started to argue for the benefits of indirect taxes on consumption (e.g. Rehn 1946). This was followed by similar articles in the SAP magazine “Tiden” (1948) and in the LO outlet “Fackföreningsrörelsen” (1946). Rehn (together with Per Åsbrink) argued that removing the 10The tax is usually called the “Oms”, short for “omsättningsskatt”. A tax referred to as “försäljningskatt” was introduced in 1948, but although the literal translation is “sales tax” this tax concerned only a few goods: precious metals, pearls, certain carpets, and gramophone records and related equipment. (års kommitté för indirekta skatter 1957, p.60.) I employ the commonly used translation “sales tax” for “omsättningsskatt” (see for example Steinmo 1993, p.126) or just “Oms” when referring to this tax.
Oms had been a mistake and that judging indirect taxes only on its incidence and not what the revenue is used for was like throwing the baby out with the bathwater (Åsbrink and Rehn 1951). For instance, taxes on consumption do hit the less well off relatively harder, but if the tax revenues are spent disproportionally on these groups then there is no quarrel with the tax on distributional grounds. Moreover, taxation of consumption had two additional advantages. First, it was harder to evade than the increasingly avoided income tax. Second, in a time of rising prices and full employment, consumption tax was seen as a formidable tool for balancing the economy. Conscious about the political difficulties of such a reform, Rehn and Meidner cited a recent poll gauging the level of opposition towards the recently removed Oms. Respondents were asked whether they preferred removing the Oms or keeping the Oms if it financed certain social policies. Among the working class, thirty-nine percent wanted to keep the Oms while fifty percent wanted it abolished (Rehn 1946). Rehn’s point was that the electoral risks associated with the Oms were exaggerated.

It was not just Rehn’s articles in the labor press that advocated for a changed perspective on taxation. Rehn, Åsbrink and Meidner also met regularly with Prime Minister Erlander as early as 1951, discussing ideas about general sales taxation and inflation. Erlander writes that although these ideas later became central to SAP economic policy, they were politically impossible to implement at the time (Erlander 1974, p.235f and Erlander 1976, p.39).

Another source into the thinking and strategy of tax policy comes from two influential public inquiries into direct (1951) and indirect (1957) taxation. The report issued in 1951, which was the result of the committee on direct taxation commissioned in 1949, is interesting for several reasons. First, the report – supposedly focused on direct taxation only – spends considerable amount of ink on the balance between indirect and direct taxation, sparking a serious debate on the issue. Second, the report allowed Gösta Rehn, an official member of the commission, to fully express his views on the matter. However, since his opinion deviated from that of LO, he could not use his own name. The dissenting opinion of E. Oskar Åkerström is in fact the opinion of Rehn (Elvander 1972), and states that taxation
of consumption is not to be considered detrimental for social progress since its yield can be used to compensate the poorer segments of society. Moreover, Åkerström/Rehn argues (as does the main report) that indirect taxes on consumption are less susceptible to tax evasion.

In its response to the report, LO agreed with the main points – even that income taxes had reached a point where they had unfavorable effects on tax morale and production – and recommends an inquiry into a shift from direct to indirect taxation, but only on the condition that compensation is paid out to the less well-off through social programs (Konseljakt 31 mars 1952).

The Federation of Swedish Industries (Sveriges industriförbund, SI) expressed a strong preference for an immediate decrease in public spending. It also expressed concerns regarding the negative effects of direct taxes on employment business and savings. That the report (SOU 1951:51) found evidence for considerable tax evasion was seen as a clear indication that the rates were too high. In order to finance reduced direct taxes, the Federation advised a permanent, general, indirect tax (Konseljakt 31 mars 1952).

1951-1957: Deliberations

Notwithstanding the recommendations from the 1951 report – or the support from LO and SI – no major changes were made to indirect taxation during the following years. The priority for economic policy was to limit inflation and among the various measures to do so – a reintroduction of sales taxation was as mentioned above one of these – the government chose excises and increased interest rates.

During this period Rehn and Meidner met repeatedly with Erlander discussing the issue of indirect taxation. In 1955, Meidner suggested a reintroduction of the Oms, but representatives from the government were hesitant, and the Finance Minister (Per Edvin Sköld) was outright hostile to the idea (Erlander 1976, p.265). The ideas of Rehn and Meidner, while planted in the early 1950s, took until later in the decade before they were put into policy (ibid. p. 235ff.). Rehn continued his advocacy not only in meetings and internal memos to

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11 At one point LO disagrees with the report: on the general level of taxation, where the report recommends a lower general level of tax revenue.
the SAP, but also – as mentioned above – in labor movement press.

**Reintroducing the Oms**

The eventual reintroduction of the general sales tax was preceded by the second major tax inquiry of the decade, published in 1957: the 1952 Committee on Indirect Taxation (of which Rudolf Meidner was a member). The report was published in 1957 and concluded that indirect taxation had several advantages over direct taxation. First, indirect taxes have lower administrative costs, especially compared with the rates of current direct taxes. Second, the report emphasized that a move to indirect taxes on consumption would lower tax evasion and would have a less deleterious effect on work incentives and savings. Third, indirect taxes would provide a more effective and flexible tool for fighting inflation. The report recommended that a new indirect tax should be broad-based with uniform rates (although some goods could be excluded for special reasons). Importantly, the committee acknowledged the fact that these types of taxes hit some groups – such as families and pensioners – especially hard. The committee recommended compensating specific groups using government spending rather than providing exceptions or lower rates for certain goods. The report was careful to leave the issue of whether the tax *should* be introduced or not up to the parliament (1952 års kommittée för indirekta skatter [1957]).

LO’s general view of indirect taxes had not changed since 1951; they still thought that the negative distributional effects of indirect taxes could be neutralized by compensation through social programs. This time, LO is more specific regarding the political risks and the more technical forms of compensation. Fearing that compensation might be a temporary, one-off, arrangement associated with the introduction of a general consumption tax, LO argues for clear regulations regarding which groups have right to compensation and that rates of benefits should be tied to the rates of the consumption tax. LO also agrees with some of the proposed advantages with indirect taxation, such as lower evasion and its possible use in fighting inflation. Nonetheless, LO advises against the tax. The main reason for this is that the way the proposed tax is constructed, most of the incidence will fall on consumers and thus
lead to demands for wage increases. LO cannot abstain from the right to negotiate higher wages as compensation for this. Although LO comes out negative against this particular tax, it states that a value-added tax could be plausible in the future as a replacement for the profit tax (Konseljakt 9 oktober 1959 p.21).

The Federation of Swedish Industries was critical that the committee framed the possible shift towards indirect taxation in terms of increased social spending and not lower taxes overall. The Federation strongly advises against introducing consumption taxes as a way of expanding government, but recommends an immediate shift towards a general consumption tax if it means maintained or lower overall tax levels (ibid.). Thus, both interest groups discussed the pros and cons of the new tax with reference to what the revenue would be spent on.

The Decision

In spite of LO’s opposition, the government decided to go through with the reintroduction of the Oms. In the words of Prime Minister Erlander: “We wanted to continue our policy of reform. But then we have to get money” (Erlander 1976 p. 264, my translation). In practice, the government presented a spending budget generating a considerable deficit, before presenting how it was to be financed, which was heavily criticized by the opposition parties (AK nr).

When it came to the revenue proposal put forward during the fall, the government first thought they would be able to get support from the conservatives and the liberals, but negotiations failed; the one thing the right-wing parties seemed to be able to agree on was their opposition to the Oms. The government also – unsuccessfully – tried to convince the Farmer’s League to support the bill by threatening to raise direct taxes. Another problem was that LO now opposed the tax. Erlander claims that LO was warming up and decided to try to push through the bill with the possible help of the Communist party (Erlander 1976 p.267ff).

In the parliamentary debates, the conservatives (Högerpartiet), the liberals (Folkpartiet),
the farmers (Bondeförbundet) as well as the Communists were strongly opposed to a reintroduction of the sales tax, albeit for very different reasons. The right – primarily the liberals and the conservatives – were concerned about the general level of taxation and the size of government, a return of the sales tax would accelerate this development. For the Communists, the sales tax represented a regressive tax hurting the poorest workers the most, and thus unacceptable (Sweden 1959).

In the end, the Communist Party had to choose between accepting the Oms or in effect terminating the SAP government. According to Erlander, the Communists used the electoral system to save face: it allowed them both to vote against the Oms, but also to abstain and save the government in the subsequent joint sessions vote. The reason they could do this is that tax bills needed to pass both chambers, and if it passed only one, a new vote would take place with both chambers voting together. Thus, the Communist voted against the Oms in the second chamber, and abstained in the following vote (Steinmo 1993, p.127-128)

Aftermath

According to a poll, prior to the 1960 general election, most SAP voters opposed the Oms. Interestingly, after the election, a majority supported the tax. Särlvik (1967) presents data suggesting this was an effect of SAP appealing to attitudes to welfare expenditure and party loyalty during the election campaign. That is, it seems like the compensatory spending helped change the public opinion. Moreover, SAP gained three seats in the election (Nohlen and Stöver 2010, p. 1872.)

Table 3 shows that the reintroduction of the Oms lead to a significant increase of revenues from consumption taxes, less dependence on the income tax, as well as sharply increased social spending (both as a share of GDP and state expenditure). The Oms was turned into a VAT in 1968 (Rodriguez 1981, p.49).

Conclusion

Considering the aggregated tax/spend data as well as the election outcome and the polls, it seems like the SAP managed to reintroduce sales taxes, compensate the poor, and also
Table 3: The Third Erlander Government: 1957-1969

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<td>Social Spending/ Total Expenditure</td>
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<td>48.2</td>
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Sources: Tax shares are from Andersson and Brambor 2015 and data on social spending from Flora, Kraus and Pfenning 1983. All figures are for central government.

avoided electoral backlash.

While the SAP was working closely with LO, it does not seem like their choices were constrained in the way suggested by Beramendi and Rueda (2007). Both actors were conscious about the corporatist agreement and the problem of wage increases and inflation, but eventually found a solution to the dilemma. Importantly, the ideas regarding a reintroduction of the Oms came from within the unions, not from the government as a result of constraints.

Interestingly, in 1959 the SAP stance seems to be more in line with the opinion of the business peak organization than with the unions (and the right-wing parties in parliament, who opposed the tax). In 1951, LO seemed to be willing to accept consumption taxes as long as there was compensation, but in 1959, they explicitly advised against a reintroduced sales tax. They acknowledged that compensation is important — and that it might work – but they judged the political problems too hard to overcome, especially considering that higher prices means workers will demand higher wages. Curiously, in the same document, LO comes out in favor of a VAT, suggesting that the technical implementation of the sales tax was the issue, not the general shift towards consumption taxation.
6 Discussion

There are several similarities in the British and Swedish post-war tax debate. Both countries struggled with what to do with temporary tax measures implemented during the war, as well as with inflation and tax evasion. Moreover, both SAP and Labour came from the same pre-war skepticism towards indirect taxes and in both Britain and Sweden ideas challenging this orthodoxy started to emerge in the 1950s. Why did these new ideas prevail in Sweden while the Labour Party in Britain opted for the SET?

A striking difference is the behavior of the unions, especially the peak organizations the British TUC and the Swedish LO. In Britain, in order to support a VAT, the TUC demanded a tax on wealth. This is not directly a compensation to the people being affected by the VAT, but rather a correction of the redistributive profile of the tax system. In contrast, LO identified specific groups especially exposed to the proposed tax and suggested targeted compensation using government expenditures (for example raised child benefits to compensate families). Moreover – and in line with the theoretical argument – LO (and later SAP) adopted the view that a high yielding indirect tax coupled with social spending would be a more effective way of achieving equality than raising income tax rates even higher.

Both the TUC and LO were concerned that compensation would never materialize, or just be paid out once. This fear seemed stronger in the TUC, and the considerable influence it had over the Labour party was important in explaining why the government abandoned its plans for a VAT. In Sweden, the LO gave somewhat mixed signals during the 1950s. On the one hand, they were positive to more indirect taxation in their opinion on the 1951 report and prominent economists within the organization advocated for the Oms both in the press and in private meetings with Prime Minister Erlander. On the other hand, LO officially came out against a reintroduction of the Oms in its response to the 1957 report on indirect taxation. In the Swedish case, electoral concerns were appreciated early, and Rehn and Meidner used an opinion poll in 1946 to argue for the fact that the Oms would be more palatable for voters if combined with social spending.
As Steinmo (1993, ch.5) has pointed out, an important factor in Swedish politics during this era was the SAP majority in the upper chamber. However, probably more important is the fact that there was no unified strong opposition at the time (see also Hicks 2013). As mentioned above, the SAP had been in coalition with the Farmer’s League from 1951 to 1957, and more often than not, the right disagreed on economic policy. Moreover, when the right-wing parties were unified on an issue, SAP needed to rely on the Communists. The situation in Britain was completely different. There was no moderate right-wing party with which to strike deals, and the governments by design had a majority in Parliament.

Alternative explanations mentioned above emphasizes that the ideological profile of a party allows it to credibly tax its own supporters (Cukierman and Tommasi 1998, Cowen and Sutter 1998, Timmons 2010). This proposed mechanism suggests that a party to the left could more credible claim to spend the revenue from regressive taxes on the working class. We saw that this thinking was present in trade union writings in both Britain and in Sweden. However, it cannot explain why the British TUC would not take the risk of being left with no compensation and a regressive tax, while LO in Sweden actively advocated for it (at least to begin with). A related topic in the debates over income versus consumption taxes was evasion and avoidance (also emphasized by Timmons 2010). Both in Britain and in Sweden, a common view was that the high rates of income tax had eroded tax morale, especially at the top, making the income tax both inefficient and less progressive in reality than on paper. However, I found no evidence for tax avoidance and credible commitments being the main driver behind tax policy during the time. For example, the opposition to the Oms from the Swedish right was driven by a fear that this would open up the floodgates on government expenditures, while the Conservative Party in Britain supported the introduction of the VAT.

Another argument for why the left taxes consumption is spending pressure (Ganghof 2006). In both the British and Swedish case, supporters of the VAT (and other broad-based consumption taxes) emphasized its effect on state revenue, especially in comparison
to existing income taxes. However, taxes on consumption were also seen as important tools in fighting inflation. And as we saw from the British case, there were other ways of raising additional revenue; a broad-based consumption tax was far from the only option.

Hallerberg and Basinger (1998) and Tsebelis (2002) argue that more veto players lead to policy stability and less sweeping tax reforms. The case studies do not provide clear support for this idea. The constitutional system in the United Kingdom produces strong majority governments without additional checks and balances. Nevertheless, as outlined above, there is no uniform pattern of sweeping tax reform in Britain. For example, the conservative Macmillan ministry from 1957 to 1963 achieved only incremental changes while the following Labour government under Wilson introduced truly radical reforms. Moreover, the minority SAP government managed to reintroduce the Oms, although it was opposed by all other parties in parliament as well as the LO.

One aspect of tax policy decision-making that was prominent in the cases – but absent in theories trying to explain it – were consumption tax as a tool for countercyclical demand management. Both parties and unions were deeply concerned about inflation and balance of payments and saw tax policy as a natural tool for dealing with these economic issues. Further research should consider these multiple uses of tax policy when constructing theories linking preferences for redistribution to tax structure outcomes.

This paper has put forth an alternative mechanism for left-wing tax policy focusing on how institutions affect the risk assessment involved in tax policy, and how this leads to divergent strategies for redistribution. The evidence shows that existing explanations fail to explain why Labour and the SAP chose different strategies. Instead, the Swedish and British case highlights the importance of how opposition influence affects expectations regarding compensatory spending, and its impact on union and government behavior.
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