ONE

Approaching Tax Fairness

The United States and other mature economies face persistent fiscal problems. The combination of aging populations, increasing demand for health care in the face of rising costs, and commitments toward equality of educational opportunities all outstrip the apparent willingness of the public to levy taxes to pay for these goals. Matching desired expenditures to desired taxation is naturally a difficult political challenge, as it forces the politicians and the public to decide what they really want and what they are willing to sacrifice to obtain it. One should not expect that weighing costs versus benefits in complex settings would ever be easy – or pretty. Making these challenges even more difficult are the questions that swirl around the "fairness" of taxes. Tax fairness embraces a variety of diverse questions and issues: what types of taxes should be levied, who should pay them, how they should be administered, and what processes should be used to make these decisions?

It is tempting to think that tax fairness can be analyzed with a separate set of tools and concepts specifically and narrowly tailored to debates about public finance, but the reality is quite different. Philosophers, economists, psychologists, lawyers, and tax theorists have all discussed tax fairness from very different perspectives. What emerges from this vast literature is that tax fairness needs to be seen as part of a broader discussion of fairness and justice. It cannot be relegated simply to questions that narrowly arise in public finance. Complicating the matter even further is that strong views on tax fairness are also held by the general public. These views are often quite distinct from those held by tax policy theorists. Whose views should prevail?

One image that is etched into the soul of Western civilization is that of Socrates wandering the byways of Athens, probing his fellow citizens for the true meaning of "justice" and related concepts. Inevitably, the

unfortunate citizen upon whom Socrates stumbles will offer an incomplete definition or thought, which Socrates will then demonstrate cannot really be a complete and coherent theory of justice. While we may not agree with the recipe for justice that Plato had Socrates describe in *The Republic*, we nonetheless carry with us the belief that popular conceptions of justice and other moral notions are typically untutored and incoherent. According to this account, it is the job of the philosopher or the applied social scientist to develop more comprehensive theories of justice to educate ordinary citizens.

From this intellectual heritage we defer to expert opinion, despite the fact that in their everyday lives citizens make complex moral judgments and important decisions on a routine basis and offer a wide array of opinions as to what is fair and what is not. These judgments emerge at an early age. Young children quickly learn to express their anger toward playmates who are not behaving "fairly," often resulting in conflicts between them. There is clearly a sense of *folk justice* possessed by ordinary individuals in their daily lives, which sometimes stands in contrast to the concepts of *expert justice* derived from social theorists. In much public discourse, however, the ideas of folk justice are dismissed as naïve or inferior to the experts' views on justice.

This bias against folk justice is deeply imbedded in our social discourse. For example, faced with an increase in measured inequality of incomes or wealth, we typically turn to the intellectuals for their perspectives on how we should evaluate the "problem" of the rise in inequality and what social policies – for example, tax policy – we should employ to combat it.

Sometimes we probe public opinion on these matters, but many political scientists and analysts of polling data view public opinion as malleable and too crude to serve as the basis for policy. For example, in describing why the American public supported the tax cuts of President George W. Bush, which he believes mostly benefited the wealthy, political scientist Larry Bartels writes, "Most of these people supported tax cuts not because they were indifferent to economic inequality, but because they failed to bring relevant values to bear in formulating their policy preferences."[1] From a perspective of an analyst of public opinion, Karlyn Bowman of the American Enterprise Institute expressed a similar sentiment: "Polls can provide useful insights about public thinking, but they are probably too blunt an instrument to be used to make policy directly."[2]

[1] Bartels (2009). Lupia et al. (2007) take objection to Bartels's claims about the tax cuts.
[2] Bowman (2009), p. 106.

As a result of this lack of trust in public opinion, social theorists, many of whom have an egalitarian bent, are only loosely constrained by public opinion. John Rawls's *Theory of Justice*, probably the most influential tract influencing expert opinion on social justice in the late twentieth century, exemplifies this phenomenon. From Rawls's perspective, combating social inequality lies at the heart of the project of social justice and must be aggressively pursued subject only to constraints on basic liberties and the mitigating consideration of individual behavioral responses to taxation.

The economic literature has its own version of an expert theory of justice. Nobel laureate James Mirrlees developed the theory of optimal income taxation.[3] Mirrlees started from a utilitarian perspective of maximizing a social welfare function of the utilities of individuals who differ only in their capacities for earning. He then incorporated the effects of limited information on the part of the government as well as the disincentive effects of taxation into a quantifiable model of income taxation and redistribution. An entire generation of increasingly sophisticated economic practitioners now takes this approach as a starting point for expert models of distributive justice. It has become the economist's equivalent to Rawls's theory as the workhorse of distributional analysis. Indeed, there are some basic similarities. Aside from the notion of basic liberties, economists generally view Rawls's conclusion that we should maximize the welfare of the least well-off – the "maxi-min" principle – as just one possibility within the basic Mirrlees framework depending on the precise specification of the social welfare function.[4]

In contrast to these expert theories of justice, we offer an alternative of folk justice. What is folk justice? Broadly defined, it is the full constellation of attitudes that individuals hold in their daily lives about all dimensions of justice. One clue to ordinary ideas of justice is that in their day-to-day lives, individuals are often much more concerned about *process and procedure* than they are about *purely distributional* issues, or "who gets what." Expert theories of justice inevitably focus on distribution. Folk justice may include distributional concerns, but also includes procedural concerns.[5]

While Socrates may have been the enemy of folk justice, Aristotle was an ally. In his *Politics*, Aristotle emphasizes that humans naturally live in

[3] Mirrlees (1971).

[4] This economist rendition of Rawls's theory is simplistic and neglects the richness and sophistication of his arguments. It does, however, try to make sense of the "maxi-min" criteria in Rawls.

[5] As we discuss in Chapter 2, Rawls's theory has a procedural flavor but its overall goal and thrust is distributional in nature. The influential work of Robert Nozick (1974) also has a strong procedural component.

political environments, that is, environments beyond the family. The distinctive human characteristic is speech, which sets humans apart from bees and other social creatures. Humans, unlike bees, live naturally in political environments because they use a gift of speech not simply to seek a secure life (as in Thomas Hobbes's *Leviathan*) but to secure a *good life*. And essential to securing that life is articulating and debating notions of good and bad and right and wrong in political settings. In other words, humans embrace their own versions of folk justice to discover the good life. The pursuit of folk justice is what makes humanity a naturally political animal.

We no longer have to rely solely on Aristotle for an account of folk justice. There is now a rich body of modern scholarship that can provide us insights into the alternative dimensions of folk justice. Research in social psychology, cognitive science, moral philosophy, and the new field of moral psychology can fill out the dimensions and nuances of folk justice. Let us begin with a brief survey of some of these developments, some of which will be discussed in more detail in the next chapter.

Social psychologists have developed an extensive body of research into the study of *procedural justice*, the notion that process matters greatly in social matters, sometimes even more than outcomes. A recent survey documents how robust the findings of this literature are across empirical methodologies, cultures, and social settings.[6] Two aspects of procedural justice have been shown to be particularly salient: *voice*, the ability to express views or convey one's story; and respect for social standing, or *respectful treatment*. What began as some insights into legal processes has mushroomed into a major field of social psychology that has transformed our understanding in socio-legal studies and organizational behavior, and has slowly made its way toward economic settings as well.[7]

Social psychology has contributed other insights to folk justice aside from procedural justice. Traditionally, psychologists have looked at two other dimensions of ordinary ideas of justice: *restorative justice* (how social wrongs can be corrected) and *distributive justice* (how goods are distributed).[8] Restorative justice is relevant not only in purely legal settings; it also can be relevant in economic or public finance settings, such as policies aimed at preventing tax evasion.[9]

[6] MacCoun (2005).
[7] Dolan et al (2007) examine the components of procedural justice in the context of health care rationing. Ong, Riyanto, and Sheffrin (2012) make a bridge from procedural justice to the game theory literature and the ultimatum game.
[8] Wenzel (2002).
[9] See Braithwaite (1989).

Distributive justice is a broad category that has generated much research, which led to the development of specific theories. For example, one important theory of justice is known as *equity theory*. This approach suggests that judgments of fairness are often based on the relationship between efforts and expenditures on the one hand and rewards and outcomes on the other.[10] This is a notion clearly relevant to assessing economic inequalities that arise in markets, as well as the relationships between perceived tax payments and benefits.

Psychologists, along with economists, have studied in detail how basic norms of *fairness* may affect the allocation of goods and services and lead to seemingly altruistic behavior. There is now a rich experimental literature documenting these findings. Other researchers have documented how individuals may often hold strong moral positions – *moral mandates* – that dominate their social interactions and trump economic concerns. Psychologists have also noted the complex relationships – not always particularly rational – between individual assessments of fairness and social settings. A new body of research, *system justification theory*, describes how individuals bend their notions of fairness to make it consistent with the status quo – roughly, a theory of social cognitive dissonance.[11]

Social psychology is not the only source of the raw material to elucidate folk justice. New and exciting intellectual developments in other parts of psychology and philosophy place deep-seated individual moral judgments at the center stage of their theories. Philosophically, these ideas run counter to the notion of simple deference to expert notions of justice. Consider, for example, the central role that the development of a moral sense and the capacity to make moral judgments play in the field of evolutionary psychology. There is now a growing belief among psychologists that there is an innate capacity for acquiring moral judgments, similar to Noam Chomsky's theory of innate language acquisition skills. As Stephen Pinker has recounted, even though concrete moral assessments differ across societies, anthropologists have found that virtually all civilizations share in their moral categories a small class of core ideas. These include the avoidance of harm, fairness, support for the community, respect for authority, and some notion of purity.[12] These categories serve as the fundamental "grammar" of human morality into which specific societal incarnations are embedded.

[10] See Walster and Walster (1978) and the overview in King and Sheffrin (2002).
[11] See Blasi and Jost (2006).
[12] Pinker (2008).

Evolutionary arguments can explain the capacity of humans to develop these moral traits. Fairness, for example, can be seen as a necessary concomitant of effective social relations within groups to ensure necessary cooperation. Game theorists have developed explicit models of how traits of fairness could be propagated through human populations as survival mechanisms in a hostile world. Even specific features of our morality can be seen in evolutionary terms. Joshua Greene, a neuroscientist and philosopher who studies ethical reasoning, has emphasized that people's moral reactions are much stronger when the harm that may be caused by an action is visible and personal rather than distant.[13] He suggests that the evolutionary environment in which moral traits arose was the close-knit world of our hunter-gatherer ancestors, in which actions – such as an attack of a wild animal – had immediate and visible consequences. As a result, we are less sensitive to actions – such as widespread dispersal of nuclear weapons – that have distant but equally serious consequences.

Modern cognitive neuroscience conceives the human mind as containing modules that operate somewhat autonomously and are integrated at higher levels in the brain. For example, there are modules for vision, tactile sensations, language, and the whole range of human actions. These modules rely on shortcuts and rules of thumb to convey information quickly and efficiently to the brain. Our misperceptions or mistakes in perception often result from these cognitive shortcuts. For example, if our brain uses the clarity of objects to judge distance, we will misjudge distances when conditions are not clear. Moral judgments form one of these modules; we make moral judgments quickly and instinctively, just as in other modules of the mind, based on certain prominent characteristics detected by this module.

Psychologists have long noted that the reasons we give for our actions are often at variance with our actions. In the moral sphere, experiments have shown that we take actions and make judgments instantaneously and provide rationales later. Evolutionary considerations force us to make assessments and judgments quickly – we do not have the luxury to act as philosophers in everyday life.[14]

The relatively new field of moral psychology has also shown that moral judgments enter into all aspects of human interaction in an essential way.

[13] Greene (2003).

[14] Knobe and Leiter (2007) have suggested that, in practice, human ethical behavior corresponds more to the portraits created by Aristotle or Friedrich Nietzsche, where character or instinct determines moral judgments, rather than the writings of Immanuel Kant or John Stuart Mill, with their emphasis on moral reasoning and moral principles.

The work of philosopher Joshua Knobe exemplifies these efforts.[15] Through a series of experiments, he has probed how our moral judgments color our assessments of behavior. Consider the question about whether a given action was intentional or not. We would think that this assessment should *not* be based on moral grounds, but rather on the objective facts of the situation. However, Knobe's experiments reveal that whether we describe actions as intentional or not depends on their perceived moral context. Consider this vignette. The chairman of a company says he will produce a new product for profit, even if it harms the environment. If he does produce the product, many people who are asked about this situation will say that the chairman is intentionally hurting the environment. But if the chairman says that producing a product for profit will help the environment, this "help" is considered unintentional by respondents. Thus, virtually identical actions are described as intentional if harm results, but unintentional if the outcome is positive.[16]

Another experiment Knobe has conducted reveals that even judgments about causality can be subject to a moral lens. Consider this scenario. Receptionists are allowed to take pens from the supply closet but professors are not. One morning, both a professor and a receptionist take a pen, and none are left. A pen is urgently needed later in the day. Who caused the shortage? Virtually all respondents say the professor caused the shortage, although the actions taken that morning by the receptionist and the professor were literally identical. The results from these and related experiments suggest that moral judgments lie at the very foundation of our perceptions and interactions with other human beings. The "moral module" in fact apparently does not operate independently of other modules, but appears to interact directly with our other perceptual modules gauging action, judging intentions, and imputing causality.

The vast amount of research in psychology and related areas suggests strongly that folk justice is not an incidental feature of human nature, but is deeply embedded in the species. In the next chapter, we detail its scope more thoroughly and develop an inventory of the key folk justice concepts. But an important question immediately emerges: how should the core concepts of folk justice stand in relation to notions of expert justice?

We can identify two different investigative approaches to link folk and expert justice. The first route would be a "naturalized" ethics that would largely subsume ethics and justice to human evolution. The neuroscientist

[15] Knobe (2005b, 2005c).

[16] If we assume the chairman was solely maximizing profits for his company, then neither harming nor helping the environment would be intentional actions.

William Casebeer advocates such an approach.[17] Drawing on recent advances in neuroscience, he argues that the type of ethics envisioned by Aristotle "fits" better with the findings of modern research than other philosophical approaches. Because ethics are part and parcel of human nature, any system of ethics must respect its underlying physiological and evolutionary roots. Hence, this can be termed a "naturalized" ethics. Systems of ethics that do not reflect our underlying natures – like Kantian theories based on long chains of reasoning – will fail to do justice to the human situation and provide misleading perspectives on ethical situations. Imagine a system of ethics that makes no realistic contact with how humans actually behave or how they may even think of behaving. Such a theory would simply pass over the heads of the intended recipients and have little social import.

Anyone tutored in basic philosophy may see the potential difficulty here. Ethics is typically thought of as actions that we "ought" to perform, whereas neuroscience and cognitive psychology provide us an understanding of how we behave in practice. As David Hume has warned us, it is a slippery terrain to transit from the "is" of actual behavior to the "ought" of ethical behavior. In practice, the lines between "is" and "ought" are fuzzier than we think, and this distinction may not always be the best way to frame our social theorizing. Possible complexities aside, however, there are clearly difficulties in taking the position that prevailing moral positions held by societies should be enshrined as ideal behavior. The practice of cannibalism might be the extreme example, but it brutally illustrates the point. More generally, drawing on Joshua Greene's insights, the type of moral structures developed for the personal and intimate world of the hunter-gatherer may not be appropriate for the globally connected modern world. Folk morality and folk justice cannot totally replace expert notions of justice.[18]

A second approach, and the one we shall emphasize, leaves intellectual space for notions of folk justice within a broader, philosophical discussion of justice. It respects the distinction between "is" and "ought" and uses the notions of folk justice to help illuminate the "ought" as it becomes embodied in actual social situations and possibilities.

In accord with this broad approach, there are three related and persuasive considerations that require an important role for folk justice in our social deliberations. The first consideration is what I will term the argument from resonance. Unless an ethical or social theory is close enough to folk ideas to resonate with individuals in their everyday lives, the theories or institutions built on the theories will not be easily incorporated into social practice.

[17] Casebeer (2003).
[18] Also see Cohen (2005).

Any ethical or social theory that does not resonate with folk ideas will be doomed to eventual failure as a vehicle for social change. Understanding folk ideas of justice is then essential to building effective social structures. In an interview discussing the deep preference individuals have for one's own children over others, Joshua Greene remarked, "I have no illusions about the fact that this is not a bias that I can overcome. And because other people have this bias, it would be disastrous to try to make them overcome it. So from a *policy perspective*, it would ludicrous to try to get people to equally care about all children"[19] (italics added). If we agree with Greene's assessment, then this moral fact could influence the design of many social policies, for example, education.

Another example of resonance comes from the field of property taxation. Despite the best efforts of Western tax experts to promote the use of market-value-based property taxation in many developing nations in the world, these efforts have had little success. For reasons that the experts did not understand, but which we will explicate, Western systems of property taxation did not resonate with a sense of fairness in these countries.

A second and closely related consideration is the argument from institutions. Existing social institutions will to some degree embody the beliefs, social cognitions, and practices of individuals, building on their ideas of folk justice. Effective reform of these institutions – as opposed to utopian dreams of revolution – will require a careful understanding of existing social practices and norms to make effective policy. Again, in the property tax arena, most U.S. states have placed strong limits on the scope of property taxation. Understanding the reasons for these limitations is essential to thinking about possible reforms of this institution.

A third consideration supporting a key role for folk justice takes its cue from the evolutionary perspective and the idea of expert knowledge. Human beings have remarkable powers to perform certain actions that will even challenge our fastest computers. We recognize faces and distinguish genders instantaneously with little conscious thought. Our social evolution has also equipped us with a host of other important skills, such as distinguishing between sincere and insincere comments, detecting charlatans, or discovering truly socially dedicated leaders, albeit with imperfect accuracy. These social skills and predilections may make individuals particularly sensitive to certain deviations from social norms or behaviors. Individuals have built-in "radars" to detect these deviations. Public attitudes and public opinions may reflect this expert knowledge or tacit knowledge in a way that

[19] Quoted in Sommers (2009), p. 141.

cannot easily be captured in our philosophical idealizations and economic or computer models.

Paying close attention to the attitudes and opinions of folk justice may give us a window to penetrate this fount of expert knowledge. As an example, the survival of our hunter-gatherer ancestors depended on group cooperation, with individuals required to perform in key roles. For these reasons, people may have heightened sensitivities to whether others are contributing their fair share in social interactions. These attitudes may spill over into thinking about fair taxation and the redistribution of income.

Each of these three considerations – resonance, institutions, and expert systems – suggests that notions of folk justice and individual psychology can illuminate social situations. Can we go further? Can we learn something serious about our social system by taking folk justice ideas at face value and then probing their implications in concrete, institutional settings? This is precisely the aim of this book, as we apply this approach to the very concrete and socially contested arena of tax policy.

Tax policy is an ideal venue for this type of exploration. It features an expert realm with multiple layers of overlapping expertise in tax law, tax administration, the economics of taxation, as well as the hybrid discipline of tax policy, which aims to integrate legal, administrative, and economic perspectives. All of these areas have high intellectual barriers to entry and are often perceived as difficult and arcane – just the type of subject matter that seemingly could be left to experts.

In practice, tax policy is too important to be left to the experts. Tax policies affect the lives of ordinary individuals in a myriad of ways, and they express their opinions about taxes and tax policies in often messy and complex fashion. Politicians, partly reflecting their constituencies and personal backgrounds, also hold strong convictions about the fairness and appropriateness of a wide range of taxes. As a consequence, tax policy considerations typically are discussed with the views of individuals and politicians in mind and not just left to the experts.

Moreover, it is precisely in the realm of tax policy that there are a set of important issues on which public opinion or folk justice appear to be at deep variance with established elite thinking. A recent book by Erich Kirchler, *The Economic Psychology of Tax Behavior*, surveys the psychological research on tax perceptions, attitudes, and behavior, and provides considerable raw material for folk justice concepts.[20]

[20] Kirchler (2007). The key folk justice concepts we highlight include several discussed extensively by Kirchler as well as others that are not covered in his book.