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THE CIVIC DUTY TO PAY TAXES AND THE FAIR-SHARE CALCULATION

Abstract

In its 2009 Taxpayer Attitude Survey, the U.S. IRS Oversight Board asked taxpayers: “Is it every American’s civic duty to pay their fair share of taxes?” Respondents strongly believe it is, with 70 percent claiming they “completely agree” and 25 percent that they “mostly agree.” On very few public issues is it possible to obtain 95 percent agreement and any such broad consensus should be met with skepticism. The near-unanimous response may mean no more than that people recognize that the functions of government must be paid for and that each person should pay a certain part. But in light of the reported \$450 billion annual U.S. tax gap and evidence of declining taxpayer compliance, this paper raises questions about what taxpayers understand by “fair share” and the duty

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to which it gives rise. In this paper, I argue that the key to understanding how there can be a growing problem of tax cheating and yet a preponderance of taxpayers acknowledging a civic duty to pay their fair share, lies in taxpayers' calculation of their fair share.

Keywords: civic duty, fair share (of taxes), tax cheating, tax complexity, tax gap

In *Cheating the Government*, Frank Cowell refers to tax cheating as “an intrinsically interesting economic problem with profound implications for the fiscal relationship between government and the citizen” (1980, 195). Taxpayers in the United States are thought to be more compliant than taxpayers in many other countries (Walter 1990, 84).¹ However, the amount of noncompliance or tax cheating in the U. S. is still significant, with the shortfall equal to 20 percent of the taxes actually collected. Issues that influence this lack of compliance are instructive as they involve fundamental questions in moral and social philosophy.

In its 2009 Taxpayer Attitude Survey, the United States Internal Revenue Services' IRS Oversight Board asked taxpayers: “Is it every American's civic duty to pay their fair share of taxes?” Respondents strongly believe it is, with 70 percent claiming they “completely agree” and 25 percent that they “mostly agree.”² On very few public issues is it possible to obtain 95 percent agreement; and any such broad consensus on such a contentious issue as taxation should be met with at least some degree of skepticism.

In this paper, I argue that the key to understanding how there can be a growing problem of tax cheating and yet 95 percent of taxpayers acknowledging a civic duty to pay their fair share, lies in taxpayers' calculation of their fair share. These calculations are affected by a number of factors, including: 1) growing taxpayer awareness of the tax gap and its implications for honest taxpayers who are subsidizing and enabling the

¹ Ingo Walter reports that tax compliance in the United States has traditionally been high: “Whether because of patriotism, a sense of fairness, the need to finance the functions of government generally approved of, or fear of criminal or civil prosecution, Americans have on the whole paid a significantly higher share of taxes legally owed than the citizens of most other countries” (84).

² No definition of *civic duty* is provided by the IRS Oversight Board; thus, its meaning is assumed to be its most common: “the duty of a citizen.”

growing problem of tax cheating; 2) the model employed by the United States tax code that pits taxpayers' civic duty against their self-interest, leaving taxpayers with a moral dilemma; 3) the complexity of the tax code, blunting taxpayers' ability to understand how the amount determined to be their tax due is also their fair share; and 4) the dramatic differences between tax-accounting income and economic or spendable income, aggravated by what are called *tax expenditures*.

The Tax Gap

To grasp the extent of disconnect between what taxpayers believe is their civic duty to pay and the current level of non-compliance (cheating), an overview of the "tax gap" is helpful.³ The tax gap is "the difference between what taxpayers should pay and what they actually pay on a timely basis" (IRS Fact Sheet 2005-38). An Internal Revenue Service report estimated the tax gap for 1985 at between \$68.9 and \$70.4 billion (IRS Pub. 1415, Rev. 4-96). According to one source, "[T]he extent of tax evasion for the major income and consumption taxes in the U.S. is substantial, more than 20 percent for the federal income taxes" (Netzer 1998, 124). The IRS's most recent estimate of the tax gap was for 2006. The amount of tax paid for that year was \$2.2 trillion. For 2006, the IRS projected the tax gap at over \$450 billion,⁴ 20 percent of the amount actually paid (IRS 2012).⁵

In *The Great American Tax Dodge*, Bartlette and Steele report that if tax cheating were a business, it would be the nation's largest corporation (2000, 13). One experimental study even found that 17 percent of taxpayers intend to cheat on their tax returns (Grasmick and Bursik Jr. 1990). Former

³ I use the term 'tax cheating' in a generic sense to include tax evasion and tax fraud, but more importantly to include the causes of the elements of the tax gap (underreporting income, not filing tax returns or not paying taxes owed). Thus, tax cheating is comprised primarily of negligence, which may be intentional or unintentional, and which involves violating the rules and benefiting as a result.

⁴ Note that the original estimate of a tax gap for a particular year is reduced in subsequent years as the IRS manages to collect part of the unreported or unpaid taxes originally due. This results in a gross tax gap and a net tax gap.

⁵ Some of the concepts and arguments in this paper have been expanded and applied in a book entitled, *Tax Cheating: Illegal—But is it Immoral?* SUNY Press, 2012.

IRS Commissioner Lawrence Gibbs noted, “There will always be a gap—some would say an ever-widening gap—between the compliance level that the law requires of taxpayers and the level of compliance that the IRS can obtain through its compliance and taxpayer assistance programs” (IRS News Release 88-77).

Supreme Court Justice Oliver Wendell Holmes Jr., wrote that “taxes are what we pay for civilized society.”⁶ In light of the reported \$450 billion annual United States tax gap and evidence of declining taxpayer compliance and growing taxpayer dissatisfaction with the current U. S. system, this paper raises questions about what taxpayers understand by “fair share” and the duty to which it gives rise, and ultimately how they view the “civilized society” for which they are paying. Specifically, if 95 percent of taxpayers believe they have a civic duty to pay their fair share, does this mean the tax-gap problem is restricted to the remaining five percent of taxpayers who do not acknowledge such a duty; or is it more likely that while taxpayers overwhelmingly believe they have a duty to pay their fair share, they do not see the current tax code as capable of determining what that fair share is? It is this second alternative which forms the focus of this paper and for which I will provide conceptual evidence.

Noncompliance and the Tax Gap

In its 2007 *Reducing the Federal Tax Gap*, the IRS reports that “estimates of the tax gap are associated with the legal sector of the economy only ... Although they are related, the tax gap is not synonymous with the ‘underground economy.’” “The greatest area of overlap between these two concepts,” the IRS reports, “is sometimes called the ‘cash economy,’ in which income (usually business in nature) is received in cash, helping to hide it from taxation.” One writer tells us that “as many as 43 percent of Americans do not pay the full amount of tax they owe” (Walter 1990, 85). Part of the problem, according to researchers, is that “evaders and participants in the underground economy perceive a lower probability of detection than others” (Hessing et al. 1992). Because the estimated tax gap is based on non-filing,

⁶ In his dissenting opinion in *Compania General De Tabacos De Filipinas v. Collector of Internal Revenue*, 275 U.S. 87, 100, (1927).

underreporting and underpaying, and does not include unpaid taxes on illegal income (illegal drugs, embezzling and other forms of fraud, prostitution, illegal gambling and so on) or whatever additional taxes might be due from the cash or underground economies, or on unreported income from tax-haven investments, it makes a final estimate of unpaid taxes problematic, though certainly the amount is much larger than the IRS's 2006 estimate. In the present political climate, the IRS has little incentive to provide a more accurate tax-gap estimate; and its methodology for calculating unreported income does not allow for the inclusion of these missing components.

In the United States, individuals pay the majority of the income tax, so it is not surprising that the majority of the IRS's \$450 billion annual tax gap estimate is generated by individual taxpayers as well. Specifically, \$437 billion (97 percent) of the total gap is attributed to individuals who either: failed to file (\$25 billion); filed, but underreported their income (\$235 billion); or filed but failed to pay the amount owed (\$36 billion). These are annual figures and, again, exclude undocumented criminal, cash and underground economies and unreported tax-haven incomes.

IRS data shows that individuals operating small businesses account for the single largest portion of the tax-gap at \$122 billion (52 percent of the individual underreporting gap and 27.2 percent of the total tax gap) (IRS 2012). This is not a new phenomenon: Field research by Schwartz and Orleans (1967) shows differences between the income-reporting propensities of the self-employed and those of employees. According to the IRS, understated income, not overstated deductions, produces over 80 percent of individual underreporting, while business activities, not wages or investment income, generate most of the understated individual income (IRS 2005a). Research on tax compliance by economists Slemrod and Bakija (1996, 149) finds that the complexity of the law and the particular circumstances of the taxpayer have increased the variety of opportunities available for tax evasion. So the question addressed here is how this known taxpayer behavior can be reconciled with the survey results noted at the outset showing that 95 percent of taxpayers believe they have a civic duty to pay their fair share.

Taxpayer Knowledge of Noncompliance

Perceptions of widespread tax cheating make it difficult for taxpayers to believe they are paying only their fair share and not their share plus part of someone else's (Loftus 1985; Cialdini 1989; Cords 2005). This perception has at least two important components. The first is the contagious effect of cheating. Psychologists who study the influences of social trends on individual behavior recognize that cheating begets more cheating. Presenting the results of empirical research on trust theory, Kahan (2001) tells us, if taxpayers "believe that others are morally motivated to comply, they reciprocate by complying in turn, whether or not they believe they could profitably evade" their tax obligations. On the other hand, the same writer reports, when taxpayers believe others are cheating, they "behave like amoral calculators posited by the conventional theory." As a result, Cialdini writes, "[i]f taxpayers believe there is even a significant minority of tax cheaters, they may be inclined to cheat as well because the act would have acquired some social validation" (1989, 215). The ethical admonishment, "What if everyone cheated?", begins to lose its force as more people engage in cheating. In a book on tax reform, Slemrod and Bakija write, "human nature being what it is, it won't work to just announce how to calculate the tax base and what tax rates to apply, and rely on taxpayers' sense of duty ... Some dutiful people will undoubtedly pay what they owe, but many others would not. Over time the ranks of the dutiful will shrink, as they see how they are being taken advantage of by the others" (1996, 145).

The second consequence of taxpayers' perception that others are cheating is the belief that if some people cheat it creates a greater tax liability for other taxpayers. This argument claims that if one taxpayer cheats on his or her income taxes, more of the tax burden is shifted onto the rest of the taxpayers—a pecuniary externality. Expressing this tautology, John Stuart Mill observed, "[i]f any one bears less than his fair share of the burden, some other person must suffer more than his share" (1884, 539). Here, taxation is viewed as a zero-sum process. The amount others are being asked to pay (which may or may not be their fair share in any event) is being increased by the actions of someone else who is cheating on his or her income taxes and thereby paying less than the rules require.⁷ In a public poll, 62 percent

⁷ For additional versions of the fair share argument, see McGee (1998, 18–19).

of taxpayers reported believing that if others cheat it increases their taxes (Eicher, Stuhldreher, and Stuhldreher 2007).

But is it literally true that if one individual pays less tax than the rules require, this shortfall will have to be made up by someone else? “Other things being equal,” Slemrod and Bakija inform us, tax cheating “means higher tax rates and a heavier burden for the many people who are honest and who have little opportunity to cheat” (1996, 3). In her testimony before Congress in 2007, Nina Olson, the National Taxpayer Advocate, reported on this “extraordinary burden to ask our nation’s compliant taxpayers to bear every year,” and which she estimated at “an average ‘surtax’ [per household] of about \$2,680 to subsidize noncompliance” (Olson 2007). Though it may not literally be true that non-compliance by some, at least immediately, increases the rate of taxation imposed on others—which requires many intervening events—the perception can lead to the belief that the amount of tax we are required to pay cannot be our fair share.⁸

Civic Duty and Self-interest

Cicero, in *On Obligations*, wrote, “This is the aim and purpose of laws, to keep intact the unifying bonds between citizens” (92). The growing problem of the tax gap represents the severing of these bonds and a sign of civil distrust, which spells trouble for tax collectors. Callahan (2004, 178–179) reports that, “Research across nations has found that tax evasion is higher in societies with lower levels of trust between people. People must want to pay taxes at some level, believing not only that their tax bill is fair, but that their destiny is bound up with that of their fellow citizens.” Scholz (1998, 137) tells us, “Without trust, there is little basis for social cooperation and voluntary compliance with the laws that could potentially benefit everyone.” I do not see a great deal of trust or a sense of common destiny—especially in matters involving Congress—and even less trust in the fairness of the tax laws. “If we do not trust Congress’s behavior in general,” Fox notes,

⁸ It is for this reason that one observer asserts, “[o]ne common bit of nonsense published by the tax bureau is that the evader forces the honest taxpayer to pay more. But tax burdens that are evaded or avoided are not assumed by others. If my neighbor operates off the books and pays no tax, my tax rates do not increase. . . . The less tax paid, the less the government has to spend”. (Adams 1993, 398).

“we cannot be expected to embrace the tax system by which it conducts its affairs” (2001, 4).

More ominously, as trust breaks down, this calls the law’s legitimacy into question as well. David Callahan, author of *The Cheating Culture*, reports, “[s]cholars who have examined ‘the psychology of taxation’ say that a tax system is in big trouble if it lacks legitimacy. Here we are advised to heed Aristotle’s warning in the *Politics*:—‘In all well-tempered governments there is nothing which should be more jealously maintained than the spirit of obedience to law, more especially in small matters: for transgression creeps in unperceived and at last ruins the state’” (bk. V. ch. 8). Ruining the state, in the context of tax compliance, implies an economic dimension that may exceed Aristotle’s original meaning. At present, however, over twenty percent of the nation’s income tax goes missing—as noted earlier—and the problem has grown over recent decades (IRS 2007). In recapping the problems caused by lax or inefficient enforcement, legal scholar Lon Fuller echoes Aristotle’s warning concerning the spirit of obedience to law and its resulting civic duty:

Government says to the citizens in effect, ‘these are the rules we expect you to follow. If you follow them, you have our assurance they are the rules that will be applied to your conduct.’ When this bond of reciprocity is finally and completely ruptured by government, nothing is left on which to ground the citizen’s duty to observe the rules. The citizen’s predicament becomes more difficult when, though there is no total failure in any direction, there is a general and drastic deterioration in legality (1964, 39–40).

In terms of tax compliance, the increasing tax gap and growing special-interest control of the tax code are early warning signs of this breakdown.

From the point of view of some economists and psychologists, the decision between tax cheating and our civic duty to pay our fair share is characterized as a problem of intertemporal choice. *Intertemporal choice* is a term used in decision theory to describe choices made between costs and benefits occurring at different points in time. “Someone may smoke heavily,” according to Frederick et al, “but carefully study the return on various retirement packages. Another may squirrel money away while at the same time giving little thought to electrical efficiency when purchasing an air conditioner. Someone else may devote two decades of his life to

establishing a career, and then jeopardize this long-term investment for some highly transient pleasure” (2003, 66). Loewenstein et al (2003, 2) contend that, “[s]o broad is the domain of intertemporal choice that it is difficult to think of a consequential decision that is *not* an intertemporal choice.”

Many such choices may also be characterized as moral problems, reflecting the role of moral values in their evaluation. John Dewey defined a moral problem not as a choice between good and bad or right and wrong, but as a struggle “between values each of which is an undoubted good in its place but which now get in each other’s way” (1932, 174). As Dewey also noted, moral problems may arise because of conflicting duties or loyalties or incompatible ideals or goals (1932, 174), or because a nearby goal is seen as conflicting with a far-off goal (1932, 200). In the case of a civic duty to pay our fair share of taxes, the moral struggle is between the immediate good for the taxpayer and the more remote good for the society of which the taxpayer is a member and so an indirect beneficiary.

Compounding the navigation of this intertemporal choice is the contextual substructure of the income tax system, comprised of three major elements. The first is the political process by which the specific provisions of the Internal Revenue Code have come into existence. Without a central theme or master plan, the diverse code sections have been clumsily spliced together under the watchful eye of special-interests and opposing political and economic ideologies. It is telling that Webber and Wildavsky (1986, 534) predict, “even if the tax code in its entirety were not supported by a single individual, the odds are against radical change.” This is a reflection of the code’s genesis in compromise and trading favors, resulting in a product no one is pleased with but also that no one wants to reopen for debate for fear of losing a pet exemption, credit or deduction.

The second contextual element in the tax substructure is the federal budget and how the tax money is ultimately spent. It represents many of the same forces at work that created the code. Among national defense, health care, education, foreign aid, disaster relief, bailing out failed institutions of capitalism, interest on the national debt and space research, the best we can hope for is a compromise with which no one is particularly happy. This is the result of the Constitution’s wording in justifying taxation “to pay the Debts and provide for the common Defense and general Welfare” (Art. 1, sec. 8). On this point, Justice Learned Hand wrote, “[t]here is indeed no great difficulty in deciding whether a tax is ‘to pay the debts’ of the United States;

but at times it is hard to say whether a statute is a tax to ‘provide for the ... general Welfare’” (1979, 13). It is this latter problem that also frustrates taxpayers’ calculation of their fair share of the tax burden.

These first two contextual elements are grounded in ethical values and social and political priorities. The third element involves the process of executing and administering the tax code. As Slemrod (1992, 1) observes, “[i]t is impossible to understand the true impact of a country’s tax system by looking only at the tax base and the tax rates applied to that base. A critical intermediating factor is how the tax law is administered and enforced.” In stark contrast to the processes of raising and spending taxes, which depend for their very existence on moral, social and political values, the execution of the income tax system is designed to operate independently of what is fair or just, or helps this group or hurts another. The execution of the tax system is based on disinterested examination of taxpayer records by the IRS, disregarding the values that determine where the tax dollars should come from and where they should go. We should never know whether the IRS auditor assigned to our case is a progressive or conservative, rich or poor, Jew or Muslim. Cheating on the Earned Income Tax Credit (EITC), for example, is not viewed more leniently by the IRS because the cheater is poor and the credit was meant to benefit taxpayers in the lower economic strata.

When it comes to administering the tax law, the IRS is constrained by the limits Congress has placed on its powers and authority. In general, IRS authority in enforcing and collecting taxes does not include personal considerations regarding a taxpayer’s economic status or condition, educational background, medical history or existing medical conditions, mental health, moral standing in the community, stress factors, family circumstances, employment or unemployment, criminal record or other factors otherwise considered relevant to fairness in other arenas of life.⁹ The fact of the IRS’s administrative neutrality in applying the tax code should bolster a civic duty, because we believe the law is fairly applied. However, it also serves to highlight the importance of the elements on either side—the sources of revenue and their uses. The law that is administered

⁹ It should be kept in mind that I am discussing the process of assessing the proper amount of taxes due, where personal circumstances have no bearing. This is in contrast with IRS collection procedures which do allow for installment payments and offers in compromise which do take the taxpayer’s ability to pay into consideration.

neutrally was not borne of neutrality but of the partisan forces that have shaped the tax code.

Over the years, a number of studies have found that perceptions of the tax code's fairness are directly related to tax compliance; the more fair the system, the less reasons for tax cheating (Schwartz and Orleans 1967; Mason and Calvin 1978; Scott and Grasmick 1981; Loftus 1985, Forest and Sheffrin 2002; Henderson and Kaplan 2005; Cords 2005). Recent psychological research on why people obey the law indicates that the fairness of a legal system is not judged by its final outcome so much as by the formula employed to reach that outcome. "Within the general framework of fairness," Tyler reports, "procedural concerns consistently take precedence over distributive concerns" (2006: 97). In the case of an income tax, this implies that the absolute amount of tax owed is not as significant in judging the fairness of the tax as the system used to compute the tax, and whether the same system is uniformly applied to all taxpayers.

Complexity, Self-interest, and Civic Duty

Complexity in the case of the tax code is a symptom of numerous factors, including: 1) a lack of congressional planning and coordination based on a central goal (raising revenue has become only one of many—and often competing—agenda items for tax legislation); 2) the wedging in of new tax provisions among the old in incremental policy making, with little thought to compatibility or wholeness of design; 3) counteracting measures aimed at making the tax fairer to specific constituent groups; and 4) the political market forces that create the law, including horse trading and purchasing votes with promises (Forrest and Sheffrin 2002).¹⁰ The perception of the law and respect for its integrity are important aspects of the law's moral

¹⁰ Forest and Sheffrin (2002) citing Warskett, Winter and Hettich (1998). According to Alan Feld, "[b]oth the lobbyist and the member commit a felony if the former pays the latter to vote in a particular way on a pending matter. In some cases, however, a high correlation exists between contributions from a particular source and legislative action favorable to that source. Do lobbyists contribute to the campaign funds of members who support their clients' positions, or do members support the clients' positions because they have received campaign contributions? Each must leave the connection sufficiently vague and must trust the other to perform as expected." (Feld 2001).

standing, and hence its ability to command respect resulting in a civic duty. “Laws perceived to be poorly conceived or downright foolish,” we are told, “can lead to lowered respect for law generally and greater willingness to flout it” (Nadler 2005).

But tax complexity is a problem and its resolution requires understanding what kind of a problem it is. In a seminal paper on complexity in the sciences, Warren Weaver (1948) identifies two types of complexity: organized and disorganized. By organized complexity, Weaver understands problems that involve “dealing simultaneously with a sizable number of factors which are interrelated into an organic whole.” As examples, he offers: “On what does the price of wheat depend?” and “What is a gene, and how does the original genetic constitution of a living organism express itself in the developed characteristics of the adult?” In contrast, a problem of disorganized complexity is one in which “the number of variables is very large, and one in which each of the many variables has a behavior which is individually erratic, or perhaps totally unknown.” “In spite of this helter-skelter, or unknown, behavior of all the individual variables,” he explains, “the system as a whole possesses certain orderly and analyzable average properties.” The techniques of probability theory and of statistics are used to solve problems of disorganized complexity. As examples, he offers the motion of atoms and the operations of a life insurance company that does not know which of its many policy holders will die next, but does know, on average, the frequency of deaths within the population of which its policy holders are members.

Tax complexity, in the sense in which people speak of it as a problem, is neither an example of organized nor disorganized complexity, for it lacks organic principles and will not yield to statistical analysis. The complexity of the Tax Code is what I call *accretive complexity* caused by the patchwork approach used by legislators. As if filling potholes after a winter’s onslaught, the congressional approach to tax legislation frequently involves no more than adding a subsection here or extending or modifying another one over there.

The complexity of the tax code is frequently cited as a problem for both taxpayers and the IRS. But rarely mentioned is the effect of the code’s complexity on our civic duty to pay our fair share of the tax burden. In one study, researchers report, “there is no necessary theoretical link between the complexity of the tax system and its perceived unfairness”

(Forest and Sheffrin 2002). One reason for the tax code's complexity is the attempt by lawmakers to take account of numerous differences between taxpayers. Kaplow states that an income tax "involves the use of a substantial and complex set of rules imposing significant compliance costs on taxpayers and administrators for the purpose of assessing each taxpayer's circumstances more accurately in terms of some notion of their equitable tax burden" (1996). Much of the tax code's complexity is thus due to attempts by Congress to inject localized elements of fairness applicable to specific constituencies. Whether these efforts level the playing field or make it more uneven is a contentious question, for as Friedrich Hayek warns, "[t]here is all the difference in the world between treating people equally and attempting to make them equal" (1948, 16).

At the same time that some elements in the tax code are designed to render the rules fair to specific constituencies, other elements of the code are charged with instilling fiscal discipline through changes in depreciation rules, providing incentives through targeted credits or delivering some vision of distributive justice, as well as raising revenue. The result is a heterogeneous coagulate of opposing claims to fairness, producing uncertainty in the minds of taxpayers as to their fair share. This kind of uncertainty is antithetical to a civic duty to pay taxes, if that obligation rests on each individual paying his or her fair share. According to Adam Smith, "The certainty of what each individual ought to pay is, in taxation, a matter of so great importance, that a very considerable degree of inequality ... is not near so great an evil as a very small degree of uncertainty" (1991, bk. 5, chap. 2, pt. 2). Knowing how our share of the tax burden was arrived at—even if the amount is determined unfair—is thus preferable to the uncertainty of our current system, which results in any two taxpayers with the same economic or spendable income likely paying different amounts of tax but for no explicable reason.

In 2000, then-IRS Commissioner Charles Rossotti stated, "[f]ew issues have generated as much discussion in recent years as tax-code complexity." This complexity becomes "even more burdensome" to taxpayers and the IRS, according to Rossotti, "when there are frequent changes, or when changes are made effective shortly in the future or retroactively" (WSJ 7/26/2000). In a telling statement regarding its increasingly frustrating position as enforcer of the Internal Revenue Code, the IRS made the following eye-opening admission:

The complexity of the tax code makes it difficult for taxpayers to understand their tax obligations and for the IRS to administer the tax law. Special rules, subtle distinctions in the tax law and complicated computations add to this complexity and foster a sense of unfairness in our tax system which ultimately discourages compliance. Notwithstanding an increasing awareness of the discrepancy in taxes due and taxes paid, the tax law continues to move in a direction of increasing complexity, which frustrates efforts to reduce the tax gap. In 2006 alone, Congress passed six items of legislation that affected the tax law. Within these bills, 223 provisions required over 1,200 actions by the IRS to implement the new requirements. These changes to the tax law further increased complexity and, therefore, lessened the IRS' ability to increase voluntary compliance (IRS Reducing the Federal Tax Gap, 50).

The importance of complexity of the tax code is magnified by the fact that the U.S. employs a system of self-assessment, sometimes referred to as a voluntary system. Fox (2001, 15) notes, “[t]he more incentives Congress creates that pit our self-interest against the national interest, the more dysfunctional tax laws become.” Such incentives are ubiquitous in our current system. Asking taxpayers to objectively assess their own tax liability employing a complex set of rules is therefore enabling tax cheating and fostering disrespect for the rule of law. When the complexity of these rules provides no reason to think the end-product will be a taxpayer's fair share, hoping patriotism and civic duty will carry the day amounts to congressional negligence.

John Stuart Mill observed, regarding voluntary tax systems, “[t]he main reliance must be placed, and always has been placed, on the returns made by the person himself. The tax, therefore, on whatever principles of equality it may be imposed, is in practice unequal in one of the worst ways, falling heaviest on the most conscientious” (1884, 556). According to Mill, those most concerned with paying their fair share will invariably end up paying more than they should, resulting in an unfortunate paradox. If we believe we are being asked to pay more than our fair share—though we can never be sure what that share is because of the code's complexity—and the means for adjusting our share is left within reach through self-assessment, even the most conscientious taxpayers may eventually succumb. As a result, if it is impossible to know whether each of us is paying our fair share, any civic duty to comply with the income tax laws based on the fair-share principle is doomed.

According to the IRS, “[a] wide range of factors influence voluntary compliance, although there is little empirical confirmation as to the most important of these factors or their magnitudes” (IRS 2007, 17). Among the assumed factors, the IRS lists the economy, demographics and socio-political factors such as swings in patriotic sentiment. As to the IRS’s own level of influence, it admits, “[i]t is very difficult to determine the impact that any IRS activity has on voluntary compliance” (IRS 2007, 17). It is my experience that fear and intimidation are generally its greatest weapons.

“There seems to be a problem,” Torgler advises, “with a tax system that the majority of the public consider as complicated and unfair.” (2007, 75). While the arithmetic involved is generally not complex, the reasons for many of the calculations are inexplicable: Why are apartment buildings depreciated over 27.5 years? Why are criminals permitted to deduct the cost of their tools and their travel? Such serial arbitrariness leads to unanswerable questions of fairness. In the end, the code is a black box: We process our tax data through the system and our tax liability is the end result.

It could be argued that in a democracy, tax laws passed by duly elected representatives are fair by definition and therefore each taxpayer’s computed tax must be his or her fair share. For Webber and Wildavsky (1986, 534), this notion is tautological and the tax process is “an accurate reflection of public opinion” by definition. This claimed outcome is countered by the practical effects of special-interest lobbying which greatly impacts our tax laws: While lawmakers represent those who vote for them they also represent those who support their campaigns financially. According to Scholz (1989, 19), “members of tax-writing committees, and particularly the chairmen, receive considerably greater contributions than the average congressman.” Although there is ancient wisdom advising that no one can serve two masters, our congressional representatives appear un-dissuaded.

Some of what are popularly called earmarks are tax laws affecting a few or only one taxpayer. Though special-interest tax legislation is nothing new, the closet where the bodies are hidden was opened for a brief period in the late 1990s. The *Taxpayer Relief Act of 1997* contained 79 items that applied to 100 or fewer taxpayers (Title XVII sec. 1701). The reason we know this is the result of a short-lived law aimed at bringing some transparency to the tax-legislation process. The *Line Item Veto Act* (P. L. 104–130), subsequently ruled unconstitutional by the Supreme Court in *Clinton v. City of New*

York,¹¹ required the Congressional Joint Committee on Taxation to prepare a statement identifying each “limited tax benefit”—earmark directed at 100 or fewer taxpayers—“contained in a bill or resolution.” One of these measures, and a target of the President’s veto, affected only one taxpayer. Its cost was estimated at “\$84 million over five years, allowing for deferral of taxes on the sale of a sugar beet processing facility owned by Dallas businessman Harold Simmons to a farmer-owned cooperative” (Dallas Morning News 8/8/97).¹² The inclusion of this narrow rule and others like it—what one writer calls “‘special interest’ provisions buried within the arcane language of the income tax code” (Pollack 1996, 4)—weakens the force of a civic duty to pay our fair share. To engender a civic duty, laws must be general. A law designed to apply to anyone in a particular class—but where that class has been so narrowly defined as to circumscribe a very few taxpayers—abuses the spirit of the principle of generality. This principle—that like cases be treated alike—depends on the moral relevancy of the criteria used to determine likeness. Congress has frequently violated this requirement; without it, however, the civic duty to the tax law is eroded. If the sugar beet plant noted earlier were an isolated incident, it might be excused. But the fact that we had a law requiring disclosure of tax items affecting 100 or fewer taxpayers indicates a general problem with the tax code and its ability to foster a civic duty.

Tax-Accounting Income vs. Spendable Income

In the previous section I described why the complexity of the tax code clouds a taxpayer’s vision of what a fair share might be. The civic duty problem is

¹¹ *Clinton v. City of New York*, 524 U.S. 417. In its syllabus of the case, the Supreme Court writes, “[t]he President exercised his authority under the [*Line Item Veto Act*, 2 U.S.C. §691 *et seq.*] by canceling §4722(c) of the Balanced Budget Act of 1997, which waived the Federal Government’s statutory right to recoupment of as much as \$2.6 million in taxes that the State of New York had levied against Medicaid providers, and §968 of the Taxpayer Relief Act of 1997, which permitted the owners of certain food refiners and processors to defer recognition of capital gains if they sold their stock to eligible farmers’ cooperatives.”

¹² Act Section 1175. This provision was subject to the President’s line item veto and was in fact vetoed. However the veto was subject to a constitutional challenge to the Line Item Veto Act itself in *Clinton v. City of New York*, 524 U.S. 417.

due in part to the inability of any taxpayer to know with any assurance that what he or she is paying represents a fair share of the national tax burden. This problem is exacerbated by the fact that the very notion of income—the base to which the income tax is applied—is not intuitively clear and excludes almost as much spendable income as it includes. With a real estate tax, for example, we understand generally how our house is valued and also that if our house is smaller than our neighbor's we should be paying less tax. But our income tax system allows two people (or ten or a hundred) with the same spendable income to pay different amounts of tax. An individual who collects Social Security and invests in municipal bonds, for example, may have the same number of dollars coming in as her neighbor who works a full-time job for \$12 an hour. Yet the first may pay no tax and the second may pay a 15 percent tax or pay nothing and receive the Earned Income Tax Credit. In this limited example, each component (limiting the tax on Social Security, exempting municipal bond interest from taxation, graduated tax rates and the Earned Income Tax Credit) may have been introduced originally to ensure each taxpayer pays his or her fair share. But in combination with one another—and multiplied by the vast array of other special provisions, each also designed to make some aspect fairer to some constituency—the sum precludes taxpayers' recognition of what amount of tax represents their fair share.

Adam Smith expressed a moral intuition regarding the fairness of taxation. He wrote that “[t]he subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state” (bk. 5, chap. 2, pt. 2). In general terms, a tax on income could accomplish this, though Smith's words do not necessitate the countless refinements inserted in the code to ensure “even greater fairness” for specific constituencies. These modifications to Smith's fundamental insight attempt to redefine fairness from opposing perspectives. To counterbalance an item designed to please small-business, for example, another measure is inserted to benefit the working poor.

While I do not believe that complexity alone is the reason for our lack of a civic duty to pay our taxes, one aspect of our system's complexity, as noted, is its obfuscation of the fair-share calculation. A major source of this problem is the congressional decision to bifurcate income into what is

taxed and what is not, rather than taxing all income “from whatever source derived” as permitted by the Sixteenth Amendment.

In a book entitled, *If Americans Really Understood the Income Tax*, Fox (2001) explores the relation between tax rates and the percentage of income available for taxation: “Because the tax laws currently allow massive amounts of income to be siphoned away from taxable income”—approximately 46 percent of the total available—“[p]rogressive tax rates ... apply only against the remaining 54 percent” (49). Part of Fox’s point is that while government authorities may spend time and resources chasing the untaxed-unreported income—comprising the tax gap—the amount of income legally excluded from taxation for various political reasons is almost equal to the amount available to be taxed. This produces a distortion of the progressive tax rate régime. While those benefiting from this distortion may not care, the integrity of the system is compromised if its intended effect is easily circumvented by propitious tax planning. “[S]pecial income exclusions and deductions, as drafted by Congress,” Fox reports, “are anti-egalitarian. They operate regressively: The great bulk of the tax savings from special social and economic programs in the tax laws redound to the benefit of more able taxpayers” (40). Further:

[T]he link between tax rates and the rules determining taxable income is undeniable. Tax rates can produce tax revenue only from income within their reach. Having placed so much income beyond the government’s reach, Congress adopts much higher tax rates than would otherwise be necessary to raise a given amount of tax revenue (12).

This phenomenon occurs through the use of what economists refer to as “tax expenditures.” As Burman explains, “[t]he term ‘tax expenditure’ refers to departures from the normal tax structure designed to favor a particular industry, activity, or class of persons” (2003). Effectively, these represent the cost in lost tax revenue from deductions or items excluded from taxation for special groups of taxpayers. According to Fox, “Congress undermines the effectiveness of progressive tax rates by allowing so much income of middle and upper-income taxpayers ... to escape status as taxable income” (2001, 39). More than 45 percent of the income potentially available for taxation is legally excluded, although this untaxed income is not spread proportionately among taxpayers in relation to their taxable incomes

(Fox 2001, 49).¹³ Income which illegally escapes taxation is also concentrated among certain taxpayers as well, further distancing the tax system from Adam Smith's goal noted earlier.

Credits and deductions are peppered throughout the Code in an attempt to encourage certain activities and discourage others, though this further blurs our vision of a fair share. The result, as noted, is that any two taxpayers with the same amount of economic income will rarely pay the same amount of tax. Thus, there is little reason to believe the end-result of the code's machinations is our fair share. Only if we possessed a uniform and all-inclusive definition of income and knew that everyone was paying a certain percentage of their income into the Treasury, could we even know what share we were paying, and possibly whether it was also our fair share. The use of tax expenditures greatly complicates the tax code and, combined with our knowledge of the growing tax gap, makes the notion of a fair share and thus a civic duty to pay our share a distant dream.

Conclusion

This article is a response to and evaluation of the results of a survey question reported by the IRS Oversight Board indicating that the vast majority of taxpayers feel a civic duty to pay their fair share of the national tax burden. The article focuses primarily on two aspects of this question. One aspect involves the contrast of the widespread claim of a civic duty to pay taxes (95 percent of respondents) against the growing problem of tax non-compliance and the resulting \$450 billion annual tax gap. The second is the difficulty encountered in ascertaining the basis for a civic duty by determining what is meant by a taxpayer's fair share, given the complexity of the current tax code and its piecemeal approach to achieving fairness based on isolated constituent needs without the benefit of an overall vision. Thus, while the IRS Oversight Board may take comfort that 95 percent of the taxpaying public believes that they have a civic duty to pay their fair share, this finding should give pause for sober reflection. As noted, any consensus that broad regarding an otherwise contentious issue should be met with skepticism. The near-unanimous response may mean no more than that people recognize that

¹³ For a full explanation of this feature of our income tax system see Fox (2001).

the functions of government must be paid for and that each person should pay a certain part. Understood in these terms, the survey findings should be seen as hollow and primarily a function of how the question was framed. I believe tougher and more probing questions would serve the IRS Oversight Board's mission more effectively by seeking to uncover authentic areas of concern upon which the Board could then make recommendations.

As noted at the outset, the problems faced by the U. S. income tax system are fundamentally problems of moral and social philosophy. Understanding how citizens view their connection to the state and to other citizens is central to dealing with problems of tax compliance and tax cheating. Recognizing this connection is critical to modifying the existing system or designing a more effective tax system.

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