The Incidence of Taxes and the Burden of Proof

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We would like to assure Professor McCloskey that we did remember that the economic incidence of taxes depends upon a complex of elasticities and market forms, so that the point of initial, or legal, impact is not necessarily the final resting place of a tax. In case semantic confusion arises from Professor McCloskey's claim that we assumed economic incidence can be completely assumed from legal incidence we should point out that legal incidence defines the parties responsible for paying taxes.

In our article we do remark (p. 627) that "the incidence of taxation can only be properly evaluated on the basis of estimates that reveal the proportion of total tax revenue paid to the state by the different groups in society classified in terms of the share of national income that accrued to these groups at specified levels of family and personal income". We of course agree that the real incidence of taxes depends on the extent to which the burden can be passed on by the persons having the initial obligation for paying the taxes — whether landowners paying land tax seeking to modify rentals, merchants paying import duties making price adjustments, manufacturers doing the same in the case of excise taxes, or workers claiming that wages should be higher because of the higher costs of commodities occasioned by indirect taxes. We certainly assumed such tax shifting occurred and propose to interpret his comments as a critique of our assumptions about the economic incidence of taxes. Broadly we believe that indirect taxes shifted forward to consumers and that direct taxes were "paid" by those upon whom they were levied.

The central purpose of our article, however, was to quantify the levels of public revenue in the two countries and then to compare in the very broadest terms the economic and social effects of taxation in Britain and France. We did not seek to *measure* the economic and social incidence of taxes precisely; but to argue that in France the burden of taxation was less than in Britain and to maintain (pp. 629-30) that "we were not prepared to accept as obvious the proposition that taxes in France could be described as socially more regressive than British taxation".

It may well be that, in the abstract, economic theory concerning taxation allows nothing at all to be said about who actually pays what in relation to any tax whatever (although one wonders if the same accademics actually hold such an agnostic position about their own tax returns). Theoretical possibilities for tax shifting are as numerous as the taxes devisable by politicians. However, looking at such relationships retrospectively, with the advantages of hindsight, we do not feel quite so helpless as Professor McCloskey. Judged *ex post facto,* it is surely unnecessary to be quite so non-committal: the facts may help even if the voice of theory is silent.

In considering the major sources of tax revenue contemporaries assumed (as we did) that, broadly speaking and over the longer run, such commodities were produced under competitive conditions and that the demand for goods and services which consistently yielded significant shares of revenue as well as the supply of resources engaged in their production were relatively inelastic. These assumptions (set out here in the parlance of a modern economist) describe the kind of commodities and services that the statesmen of Hanoverian Britain and Bourbon France singled out for indirect taxation precisely because of their awareness of the problems of social and economic incidence. Governments of the day were, after all, under no illusions about the facts of tax shifting and tax avoidance; and also had to face acute problems of political power and incipient opposition inseparable from their political problems.

Even over the question of minimum wage rates being set to incorporate the tax element in the price of necessities, this assumption (to be generally valid) requires adherence to the subsistence theory of wages. And does Professor McCloskey hold with this? Wage rates varied greatly, as he knows, regionally and by sector of the economy in eighteenth-century England. Neither their levels nor their trends have close correlations with changes in indirect taxation. We also know that it was usual to make allowances in rent levels where tenant farmers accepted liability for the land tax — and, apart from that, changes in rent levels do not coincide with changes in the land tax.

Professor McCloskey's example of the brewing industry seems ill-chosen to sustain his assertions. For this, and other industries, it is of course difficult to identify all movements of elasticities, costs, profits and prices (even in retrospect) and specify what caused what in all the variables. But some facts are clear. The duty on strong beer was raised in 1760 from 5s. (where it had stood since the end of the seventeenth century) to 8s. per barrel, and the malt duty from 6¾d. to 9¼d. per bushel. The total net yield of the excise in 1761 was £ 4.61m. from being £ 3.59m. in 1760. The price of beer in London was raised in the aftermath of the tax increase from 3d. per quart to 3½d. per quart — the first increase since 1722. Beer output paying duty in the whole kingdom was 4.019m. barrels (strong) and 2.121m. barrels (small) in 1760; 4.31m. barrels (strong) and 2.1m. barrels (small) in 1761. Doubtless costs and profits in the trade were also affected, but it is clear that the increases in duty were not *principally* absorbed by such variations in profits and costs. The government gained extra income from the brewing industry because of these increased prices; beer remained a product in mass demand at ale houses and those who drank beer paid. It is still, alas, true with increases in taxes upon alcoholic drinks at the present time. Exactly because of the limited elasticity of demand in relation to price, eighteenth century governments could extract greater resources by indirect taxation when wars had to be paid for; and because there were no significant trends in substitution for other drinks, and beer remained a product in mass demand, we argued in our article (and still maintain) that this tax, and other similar levies, were socially regressive in their incidence. Contemporaries argued all this out in sophisticated terms.*

Finally, while we agree with Professor McCloskey that to transform our tables into tables of economic and social incidence would require a difficult enquiry into the nature of the British economy in the eighteenth century, we must draw his attention to our carefully specified purpose, which was to *compare* incidence in Britain with Britain in very broad terms. Since we made similar assumptions about incidence for both kingdoms our tentative conclusion that it was difficult to see the taxes of the *ancien régime* in France as less regressive than taxes in Britain, could only be overturned if patterns of forward shifting of taxes to commodity prices or backward shifting to the returns of factors of production turned out, on detailed investigation, to be very different in the two countries. Theoretically that is possible, but, we believe, highly improbable in fact. In short we remain unrepentant in adopting the heuristic device of assuming that, in broad terms, the burden of taxation fell where contemporaries thought it fell and where we believe the facts and the logic also suggest it fell. We do not intend to recant until it is demonstrated to us that the facts contradict our assumptions and our arguments. The incidence and also the burden of proof should fall squarely, we maintain, upon Professor McCloskey.

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* For example, see A. Smith, *Wealth of Nations* (1976 edn.) vol. III, pp. 359-71. The negotiations before the increase in the duty in 1760 are outlined in P. Mathias, *The Brewing Industry in England, 1700-1830* (1959), pp. 355-61.