

Spend and Tax: Why and When States Underprovide Public Goods

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January 2015

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The following contains some ideas that may eventually be the foundation of a book; to call it a rough draft would be a gross overstatement. Most of the bits and pieces of it are currently incomplete (assertions and placeholders for arguments instead of actual arguments) and do not fit together very well. The direction this will eventually take is still unclear. Any and all criticisms and suggestions will be appreciated.

Very few states are either rapacious leviathans or founts of abundant public goods; most are unable to provide all the goods and services their citizens want from them, be it because of fiscal constraints or philosophies of government. The variation in the definition of appropriate publicly provided goods varies not only across countries but also in the same countries over time. Late 20th and early 21st century Britain, the U.S. and Sweden exemplify how quickly the definition and provision of public goods can change.

Two analytically distinct issues affect the content and amount of public spending. The first is what states are able to do, that is their state capacity (Besley and Persson 2011) or their infrastructural power (Mann 1984), particularly in relationship to revenue production. The resources available partially define state activity, but perhaps as important is the administrative effectiveness of government. The second is what rulers¹ choose to do, within the constraints set by their state capacity, the power of other actors, and the characteristics of policy-making institutions. This question is more difficult to answer because their choices are not just a function of maximization of utility within these constraints, but are also shaped by features of the reigning fiscal culture, a culture that by definition is shared by a given population that has some capacity to hold the ruler to account. To take a contemporary example, rulers who believe in Keynesianism will choose different taxing and spending policies than those who adhere to neoliberal ideas within the same structural conditions, but they can do so only if there is a powerful enough coalition of citizens and politicians who share their beliefs. In another paper (set of chapters) we focus on the determinants of tax rates and types. Here our concern is the extent of what we label the publicness of public goods: What are the reasons some polities commit to more public goods or public goods that reach more of the populous? And why are some polities more restrictive in their definition of appropriate government provision? The preconditions for high publicness are the ability of states to set a high enough tax rate (often difficult, depending on the distribution of power between rulers and elites and the nature of policy-making institutions)² and have the administrative capacity to collect most of the tax (a severe problem for almost all premodern states and many contemporary ones). If those conditions do not exist, state actors have little discretion or capacity to extend the publicness of public goods. If those conditions exist, they can choose that option—but may not.

¹ By 'ruler' we mean any actor with some formal policy-making power. Most polities thus have multiple, partial rulers, determined by the structure of political institutions.

² For example, when rulers are highly dependent on elites to maintain their power, elites can often negotiate very low rates of taxation, making it difficult to adequately fund the state. Feudal aristocrats and capitalists in the contemporary US are two obvious examples. See, for example, Lachmann (2011) and Rueschemeyer, Stephens and Stephens (1992) on the effects of class power on the provision of state policies.

The Relationship between Taxing and Government Provision of Goods and Services

Before turning to the fiscal culture, it is worth considering the relationship between spending and taxing. They might be related in three possible ways. The first is not at all. In some states taxes are compulsory payments, taken by force or the threat of force, without rulers making any claims or promises to provide anything to taxpayers in return (some scholars call this 'tribute' instead of taxation).³ This is often the case in recently conquered territories, but it also characterized extractive relationships between peasants and autocratic rulers in many premodern states.

A tight one-to-one relationship, in which a particular tax payment is made for a particular good or service from the state, is the second possibility. The payroll tax funding social security in the US provides one example. Another comes from medieval England, in which monarchs often collected a particular tax for a particular war, and even in some cases returned the money if the war was not fought (Barzel and Kiser 2002). Prior to the 19th century, most European states budgeted in this manner (Webber and Wildavsky 1986). Taxation came prior to spending but was linked to a particular expenditure. Steinmo (1989, 1993) argues that when policy-making institutions couple decisions about spending and taxation, rates of both taxation and expenditure are higher and more stable.

One variant of this second type is an exchange between powerful taxpayers in government in which goods and services are provided to those who have particular power over or claims on the ruler/government. The power of the state is used to wrest resources from the whole to support the requirements of a relatively few constituents. Patronage systems and crony capitalism both fit in this hybrid category. Earmarking and pork barreling have similar characteristics.

A third type is a loose relationship between spending and taxing. General fund taxation is used to provide a set of public and collective goods, but there is no clear relationship between the amount of tax paid by individuals and the particular benefits they get from spending. In general fund taxation, the temporal order between taxing and spending is often reversed – states spend, then tax. More precisely, they begin by identifying ways they want to spend revenue, then look for ways to collect it. One way of conceptualizing this type of general fund taxation is as communistic in Marx's original sense – taxes come from each according to their abilities and spending goes to each according to their needs (perhaps this is the source of its legitimacy problems in many contemporary capitalist states). To put it differently, the relationship between the state and the taxpayer is one of generalized exchange (Martin et al. 2009, 3).

Systems of taxation cannot be divorced from state expenditures; the demand for tax revenue in part determines its supply. Thus taxation is in part a function of the spending patterns of states: on war, domestic security, education, social insurance and public welfare, religious buildings and ceremonies, disaster relief, and payoffs for political

³ A related situation, even more common historically, is rulers promising to provide some collective or private good in exchange for taxation, but not honoring that promise.

support (bread and circuses). War and security issues are especially important determinants of the demand for tax revenue, because the failure to fund them adequately can result in the demise of the state itself. This is why Tilly's (1990) work on war and state-making has been so important (see also Kiser and Linton 2001).

We also expect the type of public good provided to be an important determinant of tax policy and the effectiveness of tax systems. First, people may be more willing to pay taxes for some types of policies than others. Second, the effects of inefficiency and/or corruption may vary across policy domains. For example, are taxpayers more willing to tolerate inefficiency and corruption in defense spending than in welfare spending? This may also vary by political party: for example, will Republicans in the U.S. increase their tax evasion more if corruption occurs in welfare spending than if it occurs in defense spending?

Tax revenue does not always and directly determine spending; rulers often spend more than they take in taxes. However, this does not mean that tax revenue sets no constraints on spending. Tax revenue sets general, long-term constraints on spending, working via what we call "rubber band" causation – spending can be stretched beyond revenue, but only so far and only for so long, until it is pulled back, in one way or another. We will attempt to explain variations in the elasticity of the rubber band throughout history – how tightly (and by what mechanisms) is state spending tethered to total revenue? In other words, what determines the amount and duration of deficit spending?

We also stress the distinction between taxation and total revenue. In addition to taxation, rulers can get revenue from many independent sources (control of natural resources, conquered or confiscated lands) or they can borrow money to fund their expenses. These non-tax sources of revenue often increase the autonomy of rulers, allowing them to pursue policies in their interests alone.

Determinants of Public Goods Provision

Our theory of expenditure systems contains three general categories of determinants. The first is the structural context. Fiscal policies are made and implemented within particular economies and specific geopolitical relations. The second is cultural, the existing beliefs as shaped by information, values, and habits about government expenditures and taxation. The third is the nature of the political institutions. Sociologists tend to focus primarily on the first and second, political scientists on the second and third; we believe all three are essential to a complete explanation. In this particular paper, however, we are going to focus on the attributes of fiscal culture and its interaction with political institutions. We claim that the variation in the definition of government-provided public goods and their recipients is an effect of three determinants of fiscal culture: 1) the prevailing ideology of government among the key political leadership; 2) the construction (and reconstruction) of communities of fate within the populous; and 3) institutional features that enable and constrain political leadership.. We begin here to build a foundation for a model that identifies the endogenous sources of change in fiscal cultures and the consequences for public good provision.

Economic Structure and Geopolitical Relations

Economic structure affects fiscal policy mainly by setting constraints on taxation. The most foundational level determining the ability of rulers to extract revenue is the size (total output) and structure (type of production and exchange) of the economy.⁴ In other words, the economy sets the ceiling for tax rates, which in turn delimits, *ceeteris paribus*, the amount to be expended on public goods. A resource constraint always exists, but it is more severe in some places and times than in others. For most of recorded history, the size and development of economies was the main limitation, and this is still true in some of the less developed parts of the world (e.g., sub-Saharan Africa).

In most premodern states, limitations of the economy and administrative capacity were generally more important inhibitors of tax revenue than the nature of political institutions, but the situation changes in the modern world. In contemporary developed states the economy provides a sufficient tax base and the (usually bureaucratic) administration collects revenue fairly effectively (contemporary Greece and Italy are notable exceptions), but the nature of policy-making institutions (multiple veto points, for example) often limits tax revenue and spending

Other aspects of economic structure also affect the sources of revenue and its fluctuations. Oil dependence can create a great influx of monies into public coffers, but the steadiness of the stream of revenue depends on world prices and also the speed at which the oil fields are depleted. Taxes on trade are only possible if a sufficient volume of trade exists.

Geopolitics further affects taxation, primarily by shaping the demand for revenue. In premodern states, the main reason for taxation was to fund war (Tilly 1985, 1990). In the contemporary world, countries that depend on a superpower for defense may have to spend less of their budgets on defense, leaving governments the discretion to spend on other public goods or to reduce public expenditures altogether.⁵

MORE COMING

The Role of Fiscal Culture

Fiscal systems are not simply a function of existing economic and geopolitical conditions, but also of how those conditions are understood by actors. The fiscal culture of a particular polity comprises two major sets of beliefs: 1) the general conception of

⁴ The distribution of economic resources is important as well, as the breadth of the distribution of resources determines the potential breadth of the tax base. A broad base is more difficult to tax administratively, but a narrow base (when resources are concentrated in the hands of a small elite) is more difficult to tax politically (as they will have more power relative to rulers).

⁵ Exemplary perhaps is the comparison of defense spending data, all as % of GDP, of the U.S. with countries that spend a higher proportion on welfare: Sweden: 1998 2.5; 2012 1,3%; Denmark: 1998 1.6%; 2012 1.3%; US: 1998 16%; 2012 19%

the state, that is, the definition of what a state should do and for whom; and 2) the composition of the community (or communities) of fate in terms of who is included and who excluded, whether there is one or many, and, if many, whether they have contesting views of the role and legitimacy of government. These two features affect the level and distribution of compliance with revenue extractions, the demands for and expectations of goods and services, and the kinds of government policies selected. Those elements, together, form the fiscal culture.

Beliefs about the responsibilities of government

There are several sources of beliefs about appropriate government expenditure, about what goods and services it is the role of government to provide. Among the most discussed are ideologies, generally based in economic theory, that focus on the role of taxes and expenditures in promoting economic growth and prosperity (see, e.g. Micklethwait and Wooldridge 2014). Related are considerations of market failures and how and when government has a responsibility to address them; contention abounds around the claim that government should step in when markets fail to provide collective goods or when markets produce negative externalities (Keynes 1936).

Relatively universal agreement exists that it is government's responsibility to provide national defense, regulation of social order, basic education, and at least minimal social protection, although disputes continue (and probably will always continue) over the extent to which government purchases relevant services (e.g., mercenary armies, contracted security), regulates private provision (e.g., religious and charter schools, social welfare), or provides such goods and services directly. Even among those who believe government should provide more than the minimum, there is disagreement over which public goods are essential and which not. And there is further disagreement over the priority of different kinds of public goods, especially when economic downturns require reassessment of budget priorities (see, e.g., Kayser and Grafstrom 2014). And yet another source of contention is what level of government should provide what. We, thus, need a typology that disaggregates public goods along various dimensions.

The public also has ideas of what government should be doing, ideas grounded not so much in political theory as in habits and practices often supported by institutional arrangements that become self-reinforcing over time. This is the claim of recent research on the consumer society in the United States (Cohen 2003; Hyman 2011, 2012; Prasad 2012). Prasad (2012) makes a strong case that the U.S. government's emphasis on encouraging consumption results, in a complex causal chain, in a less expansive welfare state and a higher rate of poverty than we see in many other advanced industrial countries. This emphasis pre-dates Keynesianism and lays in the American way of business and citizenship. We will return to the institutional supports for such a predilection later in the paper (book).

Although it is (thankfully) uncommon for rational choice theorists to assume perfect information these days, few provide the systematic analysis of the information available to actors (the contents of their fiscal "toolkit") that is necessary to replace it. Our methodology of tracing the "leading edges" of fiscal systems, the development of new models and their subsequent (potential) diffusion, requires that.

Tax systems are not constructed by actors out of a choice set containing all possible institutions and policies, but out of a set containing only those models known at the time. There is an important historical dimension to this, as information has increased and diffused over time, the choice sets of rulers have expanded. The lack of information about possible alternatives is one of the determinants of the stickiness of tax systems, especially in premodern states.⁶

It is also important to analyze the unequal distribution of information across actors. Rulers generally have better information about their policy options than those they rule, and state officials have better information about the taxes they are supposed to collect than rulers do. As agency theory shows, these informational disparities often have important consequences, allowing agents to act contrary to the interests of principals. Fiscal culture also depends on mental models of how fiscal systems work.⁷ Mental models determine how information is interpreted, and even what counts as useful, important information in the first place. How can we fully understand early modern European tax policy without mercantilism, post-colonial fiscal policy in Africa without modernization theory, or fiscal policy in the late 20th century in Britain and the US without neoliberalism? Mercantilism, modernization theory, and neoliberalism are all mental models that posit certain causal relationships between taxing and particular outcomes such as economic growth and state power. These mental models may be more or less correct, depending on the state of current theories and folk wisdom, and the availability of empirical evidence to correct inaccuracies. The closer they are to correct, the more they converge with a perfect information model, thus the less we have to pay attention to them theoretically. They have probably become more correct over time, but they are still far from irrelevant. For example, there are ongoing disagreements about whether decreasing taxes on the rich spurs economic growth, whether austerity measures help balance budgets, and whether privatizing tax collection makes it more efficient.

Discount rates play a role here as well, because they have two important macro-level effects. First, they are one of the most important causes of deficit spending. Deficits will be common when there are immediate spending needs or when rulers have especially high discount rates (due to insecurity of rule, for example) (Levi 1988). The main problem with deficits is that they increase legitimacy in the short term but decrease it in the long run. As the theory of quasi-voluntary compliance suggests, legitimacy is in part a function of whether people think they are getting benefits commensurate to the costs they pay in taxes. In the short run, deficit spending allows rulers to provide more benefits than costs, because total taxation is less than total

⁶ Of course, knowing that an option exists is not sufficient for it to be included in the feasible choice set of rulers, it must also be deemed appropriate or acceptable. For example, most contemporary states would not view forced labor as an acceptable way to tax.

⁷ For a different interpretation of this, see Webber and Wildavsky (1986) on “budgetary cultures.”

spending. However, as annual deficits accumulate into debt which as to be paid off (at the very least, the interest on the debt must be paid), people will be getting less from state spending than they are paying in taxes (because some of their tax payments go to paying off the debt). This always threatens the legitimacy of states. It also facilitates the rise of anti-tax, anti-state parties, because they can make a compelling argument that the state is inefficient – that it is not providing benefits via spending commensurate to the costs of taxes.

The second main effect of high discount rates is that they decrease spending on goods with high initial costs and delayed benefits, such as infrastructure and education. Therefore, in addition to decreasing the overall provision of public goods, high discount rates will shift the distribution of public goods toward those that provide more immediate benefits.

Communities of Fate

A very different kind of attribute of a society also has a strong influence on the fiscal culture: the issue of who is to be served by government. At one level, this is an institutional question to be addressed later: who has voice and power within the system and by what means can they exercise demands. But it is also a matter of a more general societal commitment; even in polities where most of the populous is disenfranchised, noblesse oblige or fear of rebellion may motivate broad governmental welfare responsibilities. One way to frame this is in terms of the community of fate, that is, “...those with whom individuals come to perceive their own interests as bound and with whom they are willing to act in solidarity” (Ahlquist and Levi 2013)

We argue that: The greater the breadth of communities of fate both spatially and temporally, the greater the provision of public goods. The spatial dimension refers to the inclusiveness/expansiveness of the group (the upper bound being inclusion of all citizens of the country) and the temporal dimension refers to the time horizons of the community (necessary since most public goods require high initial spending that pays over the long term). Our question then becomes: what are the determinants of the spatial and temporal breadth of communities? From this we can derive more specific empirical questions, for example: what has narrowed the spatial and temporal breadth of the US community of fate (or, made it less of a community of fate) in the post WWII era, leading to a decline in the provision of public goods?

An important distinction is necessary here. Interest groups refer to consciously developed coalitions of individuals and corporations that work together to achieve particular political and economic objectives via tools such as votes, lobbying, protest, and other forms of pressure. It is interest groups that were the concern of the pluralists and that inform many important claims about governance (Olson 1982; Fukuyama 2014). Communities of fate, on the other hand, may or may not produce interest groups. Rather, they are the source of the beliefs and norms that are at the base of the fiscal culture and are the source of beliefs about appropriate and possible actions on behalf of the community. The construction of a community of fate is a political and social process, involving leadership and education (or, at least, socialization).

One reason for an initial link between the broadening perception of the community of fate and the increased extensiveness of public goods was the move from a theory that based a ruler's legitimacy in religion to a theory that established legitimacy on the justification "...that they in some sense 'represented' the broader interests of the whole community" (Fukuyama 2014, 50). The expansion of citizenship further institutionalized the requirement of government to be attentive to the demands of its people while expanding the conception of who was in the community of fate.

Being part of a ruler's community of fate brought some additional values into the ruler's decision-making with consequences for the fiscal culture. Here we focus on perceptions of fairness and trustworthiness in the context of Levi's (1988, 1997) model of quasi-voluntary compliance. Throughout history, the belief that government is untrustworthy and/or unjust has affected the extent to which a fiscal system can be based on cooperation or coercion (see, e.g., Daunton 2001, 2002; Sánchez Román 2013).

An effective government is one that protects the population from violence, ensures security of property rights, and provides the infrastructure that makes possible the exchange of goods and delivery of services (Levi 2006, 5). If it is also a trustworthy government, it is, by definition, competent and credible in its commitments to provide services and benefits that enhance citizens' welfare and motivated to implement laws and regulations fairly (Cook et al. 2005; Rothstein 2005). The more a government is effective and trustworthy, the more legitimacy that government is likely to attain, and the more it will possess the potential to elicit compliance without excessive monitoring or punitive action (Tyler 1990; Levi 1997; Tyler 2006). That is, the government can achieve a high degree of quasi-voluntary compliance with the taxation system.

Quasi-voluntary compliance⁸ involves a strategic interaction with government, but it also has an ethical element: An individual who feels it is right to cooperate with government will only do so if he or she feels government is doing its part and if others are also cooperating. Quasi-voluntary compliance is most likely among taxpayers who perceive that government is engaging in serious efforts to meet its fiscal contract with constituents by delivering infrastructure and services or quickly developing the competence to do so. In addition, an increasingly large body of evidence suggests the importance of government also meeting prevailing standards of procedural fairness in its provision of goods and implementation of policies. Individuals are less likely to comply if they feel government is breaking its fiscal contract with them, is exercising favoritism or revenge through its policies, or is unacceptably corrupt. Individuals are also less likely to comply if they perceive a high incidence of evasion by others. Quasi-voluntary compliance is compliance motivated by a willingness to comply but backed up by coercion, particularly coercion that ensures that others will be obeying the law. The achievement of compliance with government extractions and regulations depends on

⁸ This term originated in Levi (1988) but has been elaborated most recently in the context of Afrobarometer data concerning the reasons citizens are willing to pay taxes. See Levi and Sacks (2009), Levi and Sacks (2012), Levi, Sacks and Tyler (2009), Sacks and Levi (2010). Also see Delalande and Huret (2013).

the competent exercise of the coercive capacity of the state, including its ability to detect and punish those who illegally evade their obligations.⁹ When taxpayers perceive that government is relatively effective, competent, and procedurally just, there is the potential for the development of a virtuous circle. The more effective and procedurally just the government, the greater the willingness of citizens to accept governmental authority and therefore the greater the degree of quasi-voluntary compliance, which then improves government's capacity to become more effective and to evoke deference, which in turn increases quasi-voluntary compliance (see Figure 3).

FIGURE 1 ABOUT HERE

The virtuous cycle depicted in Figure 1 is quite rare historically. Governments can easily lose the confidence of taxpayers by failing to deliver promised returns for taxes or by engaging in favoritism, corruption, and clientelism instead. Rulers achieve the quasi-voluntary compliance of the few, often to the detriment of the many.¹⁰ Once quasi-voluntary compliance breaks down, it becomes very difficult to elicit it again. The presence of virtuous and vicious circles of legitimacy is one of the main determinants of the high level of path dependence of fiscal systems.

STILL TO BE DEVELOPED

The Role of Political Institutions

Two kinds of institutions are key to the definition of and provision of public goods. The first are the rules affecting aggregation of interests, including the capacity to stop policies as well as to enable them. The second are the administrative and bureaucratic apparatus and processes that delimit the possible.¹¹

Policy-Making Institutions

In thinking about the aggregation of interests, we rely on selectorate theory and the theory of veto points. Selectorate theory (Buono de Mesquita et al. 2003) begins with the Downsian assumption that rulers want to gain and maintain power. The characteristics of selection institutions (institutions governing the selection of rulers) determine their policy preferences. These institutions specify who is in the selectorate (all actors with some control over choosing rulers, for example registered voters in a democracy) and the size of the winning coalition (the subset of the selectorate whose

⁹ Buono de Mesquita, Smith, Siverson and Morrow (2003) argue that the extent to which the winning coalition is loyal to the ruler (essentially a measure of legitimacy) is greater the smaller the winning coalition and the larger the selectorate (in this situation, disloyal members of the winning coalition can easily be replaced).

¹⁰ Quasi-voluntary compliance can exist at many levels: among all taxpayers, among state officials, or among members of winning coalitions, and has different effects at each of these levels.

¹¹ Fukuyama (2014) offers a recent and compelling account.

support is necessary to get or maintain rule).¹² The size of the selectorate and the size of the winning coalition determine the content of state policy and the degree of loyalty of supporters to the current regime.¹³ *The smaller the winning coalition in any state, the more clientelist the fiscal policy.*

The characteristics of selection institutions determine the policy preferences of rulers, but whether and how those preferences are translated into actual policies depends on the nature of policy-making institutions. There are many arguments about how policy-making institutions affect policies – for our interests in explaining why taxes are often so low, the theory of veto points (Tsebelis 2002) is especially helpful. A veto point is a position in an institution that has the ability to stop any change in the status quo. The greater the number of these veto points, the less likely new legislation will be passed, because for any particular change to become policy, it must be preferred to the status quo by all veto players. Therefore, *the greater the number of veto points, the lower the levels of taxation and spending.*

Public Administration and Bureaucracy

Making policies is only the first part of the process; they must also be implemented. If the economy provides adequate/abundant resources to tax, do rulers have enough effective and trustworthy agents to effectively collect taxes? For most premodern states, the simple answer was no – administrative limitations prevented them from collecting much revenue.

To analyze the implementation of state policies we need a model of the relations between rulers and officials in charge of carrying out state policies and a model of the extent to which taxpayers will be willing to comply. For the former we use a version of agency theory that combines insights from Weber (1978) and contemporary economics (Jensen and Meckling 1976; Kiser 1999), and for the latter we use Levi's (1988) theory of quasi-voluntary compliance.¹⁴

¹² For example, in hereditary monarchies both the selectorate (all aristocrats) and the winning coalition (a majority of aristocrats) are small. In rigged electoral systems (such as the USSR) the selectorate is large (all adult citizens) but the winning coalition is small (all party members).

¹³ This model has two important virtues compared to the autocracy/democracy dichotomy common in the literature: (1) the same model is used to analyze both autocratic and democratic states; and (2) it reveals variations within different types of both democracy and autocracy.

¹⁴ For Weber (1978), 274, the agency relationship between rulers and their administrative staffs is essential to understanding political history: "historical reality involves a continuous, though for the most part latent, conflict between chiefs and their administrative staffs for appropriation and expropriation in relation to one another." Furthermore, Weber (1978), 225, 991-9 realizes that the reason agents are often able to get away with acting contrary to the interests of principals is that they have better information concerning the quality of their performance than principals do. This is a classic statement of an agency problem, delegation of authority leading to problems of control due to conflicting interests of principals and

Agency theory focuses on the ways rulers try to mitigate problems of asymmetric information (their agents know more than they do about tax collection) by the ways they select, monitor, and sanction agents. Agency theory can also give us a clear definition of administrative efficiency to be used as a baseline in measuring state capacity. The most efficient tax administration is the one that produces the highest net revenue within the set of structural constraints present at the time, where net revenue means gross revenue (set by the tax rate and tax structure) minus administrative costs, costs of agent corruption, and costs of taxpayer evasion.

We can illustrate the model with a quick analysis of some of the agency problems in premodern states. One of the main problems premodern states faced in providing adequate policies with high publicness is that they lacked sufficient administrative capacity to collect taxes in areas far from the capital. These problems are only mitigated with the development of technologies of communications, transportation, and information processing (a function of the level of economic development). The costs and effectiveness of monitoring are primarily determined by these technologies of control, since they determine the ease with which principals can acquire information about agents (Weber 1978:224). The higher the level of development of technologies of control, the greater the monitoring capacity of rulers, *ceteris paribus*.¹⁵ When the monitoring capacity of rulers is poor, some decentralized forms of patrimonial administration will be more efficient (i.e., produce more net revenue for rulers) than centralized bureaucracy (Kiser 1994; Kiser and Kane 2001). The only remaining choice they have is what form of decentralization (feudalism, prebendalism, tax farming, etc.) to use. The ideal typical administrative equilibrium for most premodern states and empires was to use tax farming for indirect taxes and some type of decentralized patrimonialism (feudal, prebendal, administration by local notables) for the collection of direct taxes. Rulers will only choose to use centralized bureaucratic hierarchies when their monitoring capacity is good enough to ensure agent compliance.

Agency theory alone is insufficient to understand state policy implementation, it focuses on the relationship between rulers and officials, but undertheorizes the citizens/subjects who are paying taxes and receiving state services. Power also affects tax administration. For example, tax collectors, like other state officials, were often chosen not on the basis of their skills but because of their power relative to rulers. This not only decreased efficiency in the short term, but in the long term it made tax administration very difficult to reform. Once powerful actors became entrenched in lucrative administrative positions, it was difficult to dislodge them even when changes in conditions made other

agents, and informational asymmetries favoring agents. Weber's ideal types of forms of state organization (patrimonialism, bureaucracy) can best be understood as his attempt to model agency problems in different structural contexts. They are essentially typical clusters of recruitment, monitoring, and sanctioning strategies.

¹⁵ Economic development does not always have positive effects on administrative capacity. For example, although rich people have always found ways of hiding taxable assets from states, the globalization of finance has made this easier by increasing opportunities for hiding assets in banks in other countries.

administrative arrangements (such as bureaucracies that hired on the basis of merit) more efficient. This is why the transition to bureaucratic administrations is often caused not just by changes in economic conditions, but by things like revolutions that dislodge the power of entrenched officials.¹⁶

In addition to agency problems and relative power, legitimacy also affects the effectiveness of tax administration. For this we use the theory of quasi-voluntary compliance (Levi 1988, 1997), as discussed above. TO BE WRITTEN

Stability and Change in Fiscal Culture

Where does fiscal culture come from and why does it change? Fiscal culture is primarily a product of lived experience; it is shaped by political institutions and state policies. As Pierson (1994, 2004) argues, in addition to preferences shaping policies, policies shape preferences. This tends to create fairly stable sets of mental models of how fiscal systems do and should work, and accompanying sets of fiscal habits.

Habit is one major source of stability and an important component of the microfoundations of fiscal culture. In terms of contemporary cognitive psychology, much of our fiscal behavior is associational and automatic, not the product of explicit rational calculation (Kahneman 2011). Fiscal habits (always voting for a particular political party regardless of platform changes, always paying taxes regardless of risk of punishment, etc.) develop over time, often persist even after the conditions that created them have changed.

There are many important macro-level consequences of tax habits. Habits are one of the main sources of path dependence, they can partly explain why fiscal systems are often sticky (slow to change when objective conditions change).¹⁷ Habits are also a core part of what Weber called traditional authority. Barzel and Kiser (1997, 2002) elaborate on Weber's insights by showing that much taxation is customary, and very resistant to change. In terms of contemporary cognitive psychology, when tax levels are stable over

¹⁶ See Kiser and Kane (2001) on the effects of the English and French revolutions.

¹⁷ We can also say something about the conditions under which non-instrumental aspects of fiscal culture (deviations from rationality) will be more or less important. The existence of large groups Hechter (1987) is insufficient to weed out these effects, because they are not random individual variations that will thus balance out, but systematic features of particular fiscal cultures. What does weed out the effects of non-instrumental microfoundations to a large extent is formal (especially bureaucratic) organization. People in organizations are no less prone to the effects of values and habits than people outside them, but bureaucratic organizations provide sufficient information-gathering resources and checks on individual behavior to mitigate the effects of individual actions based on them. We expect the actions of bureaucratic organizations will be more rational (less affected by fiscal culture) than the actions of individuals. For example, fiscal culture should affect the actions of voters more than the policies of states, and the policies of kings more than contemporary democratic presidents.

time they come to be taken as a baseline for judgments about appropriate levels of taxation (mixing values and habits).

We are especially interested in exploring the process by which regimes move from one equilibrium to another in terms of public goods provision, that is, why and how the fiscal culture shifts. This transformation will often involve a shock or crisis (see Kiser and Schneider 1994 on conquest; Kiser and Kane 2001 on revolution). It often involves pressure on resource constraints, be they caused by downturns in the economy or changes in population pressure (exploding birth rates in India, immigration to Europe). Another main source of change is diffusion from other states, primarily from “leading edge” states that innovate in political institutions and policies.

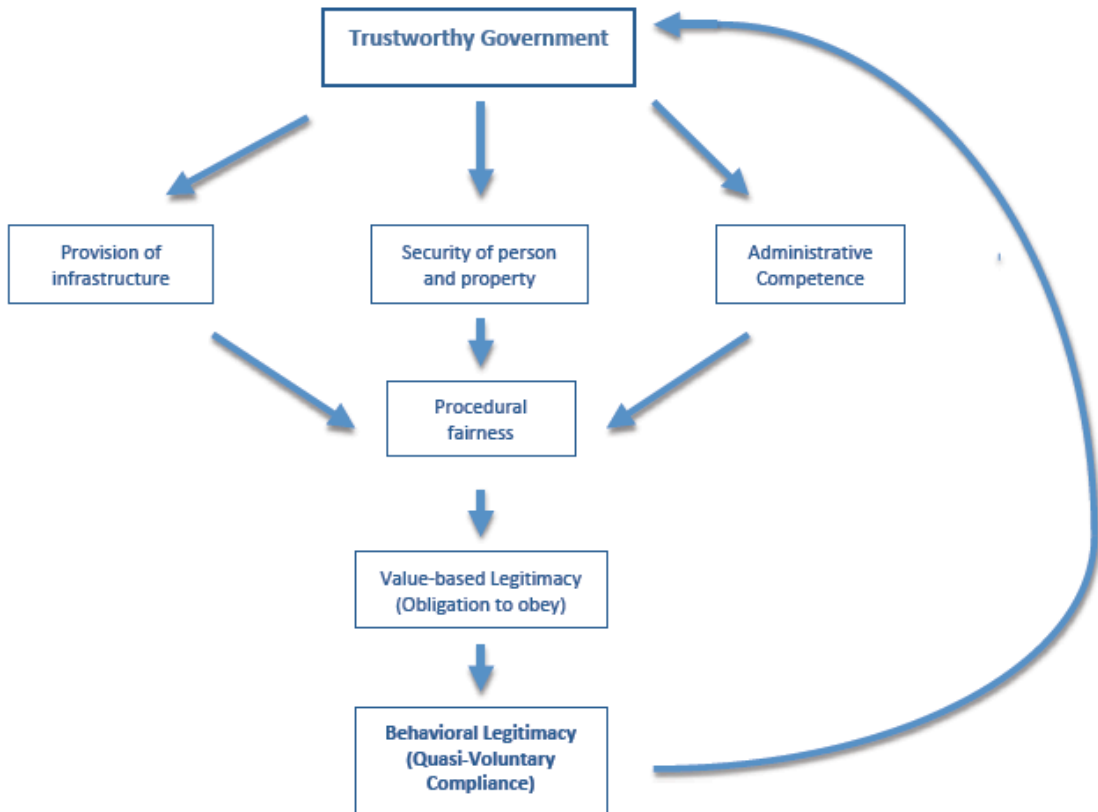
Given these pressures—and sometimes in their absence (to be explored empirically)—endogenous sources of change may come to the fore and be the actual source of transformation of the fiscal culture. In these remaining paragraphs, we are going to mention two with some examples of what we mean. This is a preliminary sampling at best but gives a sense of where we hope to go:

The failure of government to deliver on its promises for goods and services can stimulate a sufficient breakdown in quasi-voluntary compliance and belief in the reigning fiscal culture. The wonderful *Red Plenty* (Spufford 2012) offers a compelling picture of how the Soviet regime’s promise of significant improvement in the material well being of its citizens became a reason for the demise of the regime.

An expansion of the proclaimed community of fate that important groups contest can also lead to a revision of the fiscal culture. The Civil Rights movement led to an expansion not only of citizenship but of the community of moral obligation in 1960s America. Many Americans (and not just southerners) resented this expansion, particularly when it came to inclusion in social insurance and welfare protections. Black mothers on welfare were demonized as welfare queens—thus putting them outside the community of fate. With stagflation, those who delimited the community of fate looked for reasons to justify reductions in expenditure; they demonized Keynesianism and sought a new ideological grounding for the fiscal culture.

A more positive story (although the ending is not yet written) is unified Germany when the government’s community of fate came to include the East as well as the West. Despite the economic costs, the commitment to the larger Germany held.

Figure 1: How Quasi-Voluntary Compliance Creates A Virtuous Circle



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