An interpretation of fairness (equity) based on the equal sacrifice principle is not clear; three taxation rules can be derived from it. Instead of searching for a fair tax system, the ethical behavior of taxpayers should be set as target and expected. Ethical taxation can be encouraged and propensity to pay taxes could be reinforced by abolishing the secrecy of individual and family tax returns, setting restrictions on cash operations which are associated with corruption, and gradually eliminating the tax havens and offshore areas.

1. Brief theoretical history

Literature studying the general government and tax system in the narrow sense essentially describes the basic characteristics of the tax system in identical, but at least similar terms. Any differences are related perhaps to the order and the narrower or broader expression of the various criteria. Stiglitz (2000) lists five basic characteristics. A tax system must be economically efficient, simple and cheap, flexible, politically responsive and fair.

Of the characteristics of the tax system, probably equity, or fairness was the oldest requirement ever raised. Two authors are frequently opposed to Adam Smith: Montesquieu (1833) and Say (1803), who argued for progressive tax on the grounds of fairness. Adam Smith’s position divides the opinions depending on whether they intend to justify a pro or contra progressive taxation stance; contradictory ideas have formed about him. A typical position is the French author traditionally seen as a classic of the theory of finances (Leroy-Beaulieu, 1879) who categorically rejects any interpretation of Adam Smith as a promoter of progressive taxation. In Hungarian economic literature, the first to raise a demand for the fair distribution of the tax burden was Károly Balás, albeit he always used the term fair in quotation marks.

During the last two decades of the 20th century, the key personalities in public finances and
tax theory, Musgrave (1984) and Stiglitz (2000) used the requirement of equity and fairness as a criterion of the tax system as synonyms. There is a broad consensus that fairness, one of the basic characteristics, is not clear even theoretically and this is not corrected by distinguishing a horizontal and a vertical fairness either. The fact that the problem is not solved is reflected in Stiglitz's opinion who “lightly chats” through nearly a whole page when ending the sub-chapter “What economists can contribute to discussions of fairness”, stating that “we can attempt to distinguish those cases where the term “fairness” is used simply to cover up a group’s pursuit of self-interest from those cases where some reasonable ethical or philosophical position underlies individuals’ claims.” (Stiglitz, 2000. p. 420)

Is it possible that fairness, equity, righteousness (all the three terms used with a similar meaning, as synonyms) are terms which cannot be associated with any category in market economy and instead, the social interest should be approached from another direction, with another concept?

2. Equal sacrifice principle - three different interpretations

Justice and equity are probably among the most beautiful terms and every human can be assumed to have an emotional attitude towards them. Their meaning and substance according to the dictionaries can be various; but the interpretation based on the individual’s emotional approach can be diverse even within the same linguistic meaning. There is no proof to this extent, but we can cautiously state that the concept of equity cannot be extended to the functioning of economy and the elements of the economic system, or, as you choose, extending it to them is not advisable.

A traditional starting point in defining the fair tax (system) could be the ability to bear public burden. According to a claim phrased after a review of theoretical history, “the only globally applicable criterion of fairness is the principle of the ability to bear public burden (equal sacrifice)” (Balogh, 2013). True, but after this concise finding we should also bring up the opinion of the German economist Brümmerhoff, who suggests that three taxation rules could be derived from the principle of equal sacrifice. The three different rules affect taxpayers to

1 Brümmerhoff finds three different acceptable taxation solutions based on the equal sacrifice principle, assuming the same usefulness function. Brümmerhoff’s merit lies in describing the problem accurately. The
extremely different extents. Take

\[ U(Y) - \text{utility of income} \]

\[ U(Y-T) - \text{utility of income after taxes} \]

According to the equal *absolute sacrifice*

\[ U(Y) - U(Y - T) = \text{constant} \]

then the lump-sum tax or the single-rate tax is advised;

According to the equal *relative sacrifice*

\[ \frac{U(Y) - U(Y-T)}{U(Y)} = \text{constant} \]

then the single-rate or progressive tax is the reasonable approach (Cullis John-Jones, 2003).

According to the equal *marginal sacrifice*

\[ U'(Y - T) = \text{constant} \]

then the better approach is progressive tax.

Clearly the principle of equal sacrifice can be interpreted in three different ways which allow at least three different taxation techniques.

This causes the principle of equity to be meaningless in the case of a concrete tax. It could be assumed that the interpretation is possible taking taxes as a whole, albeit not in the case of individual tax types i.e. the concrete tax system of a concrete country could meet the equity criterion. This assumption must be rejected as well, because the liability of taxpayers by tax type is known when the tax system is established and it is not a rare thing to have one tax type associated with one taxpayer. (In 2014, Hungary used 55 tax types, duties not included.) The equity criterion based on the principle of equal sacrifice could refer to a certain tax type or the tax system as a whole (all the tax types), but the possibility of multiple interpretations offers us no clear answer.

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various possibilities of interpretation had been suggested by several authors discussing the theoretical aspects of taxation.
If three different interpretations are possible, a decision should be made on which direction is the equitable (or more equitable) one. A theoretical decision is impossible, and in lack of one, the individual and group interests are the rules of the game in practice.

If a concrete tax type and the tax system as a whole cannot be judged based on the equity principle, in lack of other possibilities, the criterion which expresses the social interests and follows them can and should be defined for the taxpayers.

The taxpayer can be the individual (the citizen), the family (household) and the various forms of associations. In practice, tax liability is stipulated by law\textsuperscript{2}. It is not unrealistic to assume that the whole of statutory taxes (the tax system) is a clear instruction to the taxpayer to assess the tax liability, to declare it and to pay it. To put it briefly and more simply: the taxpayer or its representative can calculate the amount of the tax liability. It can also be assumed that as part of governmental planning, the state budget is prepared based on the sufficiency of funds principle i.e. considering the size of the targeted balance, the tax laws proposed, then adopted by the Parliament ensure the revenue necessary for financing the costs.

If real economy, income and consumption forecasts are close to the factual data within the acceptable margin of error, then the actual size of revenue and the real position of public finance will depend on the “willingness” of individuals, households and businesses obligated to pay tax to actually pay the tax.

Can the tax “willingness” be shaped? If yes, then strengthening it can be designated as the key financial policy goal for society’s and economy’s sake. If not, a new system based on new concepts must be invented. The possibility that “willingness” variable by country can be observed does not rule out that it can be changed and, in particular, strengthened, but rather allows it. If there is a possibility, then the tools facilitating the strengthening of the taxpayers’ “willingness” to pay tax must be found and applied.

\textsuperscript{2} A counterargument at hand is that the Islamic religion imposes a tax representing mandatory alms-giving, customarily 2.5\% of the value of land owned, wealth and income, if the Muslim believer has no debt for at least one year. The counterargument is questionable, as Islam postulates the identity of the Muslim community and the state, and the so-called sharia is a state and religious code at the same time.
3. Seek ethical taxpayers instead of seeking a fair tax system

After the lengthy introduction and before recommending the incentive tools, it is essential to tackle the aspect which is assumed to be secondary for practical purposes i.e. how the “acceptable taxpaying willingness” can be approached and interpreted. As the ethical approach gains more ground in economy, including finances as a whole, it would be unjustified to leave out taxation from its scope. The definition rephrased according to the bygone ethical philosophers, especially Kant, is applicable to taxpayers, too: an ethical action is a solidarity and rational action of the free man’s will, considering the limited nature of goods and time (A. Bánfi, 2013). Two attributes of the ethical taxpayer should be highlighted in this definition. Solidarity means solidarity with taxpayers who pay less tax from their lower income (unemployed, unable to work) than would result from the share in the common social consumption (especially health and education consumption). Rationality is the consideration and acceptance of long-term aspects which point beyond the momentary interests (redistribution attenuating poverty helps maintain public safety, so extra funds for increasing safety are not necessary).

An ethical taxpayer thinks according to the legislator’s intention and acts upon the law. The ethical taxpayer concept rules out tax avoidance and tax optimization. Employing tax consultants may be justified by a complex tax system, but there can be no argument for tax consultants’ aiding the tax evaders and tax optimizers instead of the ethical taxpayers.

Improving the taxpayers’ tax morale and changing them into ethical taxpayers is not a simple tax, but it is not impossible either. A few general aspects:

- The simplest possible tax system should be established. Existing tax systems are not only complicated, but unnecessarily complicated. The government intends to achieve its purposes, or at least part of them, through the tax system, so other goals besides having sufficient funds are integrated as well (Kürthy, 2010). All this is not necessary, because the ethical, the fairness, and economic growth aspects can be approached

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3 A long list of Greek, British, French, and German moral philosophers attests to the age-long scientific history of ethics. Plato (The Republic, 370 BC), Aristotle (Nicomachean Ethics, after 322 BC) were the beginning, followed later by the British Joseph Butler, with particular emphasis on Adam Smith (Theory of Moral Sentiments. 1750), Thomas Reid, David Hume (A Treatise of Human Nature. 1740) John Stuart Mill (On Liberty. 1859; Utilitarianism. 1862), Jeremy Bentham (An Introduction to the Principles of Morals and Legislation. 1789), the French Rousseau, Voltaire, Holbach, the German Immanuel Kant (The Critique of Practical Reason. 1788), the German Johann Fichte (The System of Ethics. 1798), and the list could go on.
through expenditure too.

- Simplifying the accounting system must limit the possibilities for creative accounting; the accounting obligations of micro and small enterprises could be minimized by expanding the lump-sum tax so that it ensures only tax control.

- The international harmonization of national tax systems would limit the possibility of tax arbitrage. If various countries had simplified their national tax systems, the determination of the tax base of the fewer tax types, the size of tax rates, the scope of facilities and exemptions could be approximated so that the sufficient funds principle is enforced and tax competition is attenuated.

4. Specific recommendations for stimulating ethical tax-paying

4.1 The taxpayers’ tax morale depends primarily on the tax-paying willingness of the other taxpayers, therefore eliminating the secrecy of individual and family tax returns (tax payment) would improve tax-paying willingness.

Generally, individuals (citizens) can finance their own and their families’ consumption from their labor-income after taxes and/or capital income after taxes and/or tax-exempt government subsidies (family allowance) or pension. The part of the population’s income in a given period not spent on consumption forms the population’s savings which can be used later also for consumption.

The scope of taxpayers and paid tax volume increase:

- if employment contracts are signed with the illegal (undeclared) employees in existing jobs (whitening);
- the entire income of legal employees in existing jobs (wage + other income) is legalized;
- payment in sales transactions is executed based on an invoice (receipt).

All three cases can be improved by stricter control, but that would increase the cost of control; ethical taxpayers are inconvenienced by more frequent controls.

It can be assumed – and after implementation, it can be confirmed or refuted – that the strongest and least costly means to increasing tax-paying willingness would be publicity,
which should be achieved by disclosing the confidential tax returns and tax payments of individual taxpayers. Declassifying tax secrets and the public disclosure of the annual tax payments of taxpayers would not be a new thing; tax secret has not been around for long in our country. Until 1945, the ‘virilists’ (the largest taxpayers) had been the representatives of local governments elected from a certain group of taxpayers paying the highest rate of direct tax (Vörös, 1979). Of course, declassifying tax secrets would not imply the restoration of virilism. Wealth-based privileges rooted in noble privileges cannot be sustained, but public tax returns should not be replaced by confidential tax declaration.

Legal wealth may be acquired by inheritance and the unconsumed part of income after taxes. If the income after taxes is known, the source of the individuals’ and families’ wealth accretion would be known. Such a system would leave no room for arguments for wealth and property tax as a subsequent tax on wealth accrued from untaxed income.

4.2 Ethical taxation and corruption

The concept of ethical taxation is most closely related to corruption in the sense that they are mutually exclusive terms. Corruption in the Hungarian language means bribery; “An official, public, political, moral state in which the practice of bribery and the spirit of bribability are widespread.” (A magyar nyelv értelmező szótára, IV. kötet, p. 344 / Dictionary of the Hungarian Language, Volume IV, p. 344) As corruption can be associated with official, public or political personalities who are bribed, their actions are criminal cases requiring no consideration; consequently, corruption is always tax fraud, too, as the income derived from corruption cannot be part of the tax base. This means corruption is always a double crime of fraud and tax evasion. Without discovering and proving the fraud, the tax evasion cannot be discovered, therefore corruption must be limited with all the means possible.

Numerous opinions, both written and verbal, have been and are still voiced on fighting corruption. All governments, governmental control institutions, politicians, governmental officials fight corruption at least verbally; the results, according to the experts’ opinions, are feeble, which suggests the lack of action or inefficiency of action. If bribery cannot be eliminated completely or to a satisfactory level with legal means, then the circumstances which allow the possibility of bribery must be inactivated or at least diminished.
Corruption is an illegal activity generally involving cash operations. It is the interest of the participants of the corruption case to pay cash instead of bank transfers which can prove that the financial transaction has been executed. The demand for cash for the movement of funds and the significant volume of cash within the volume of funds can probably be explained by the demand for cash in corrupt practices (Raciborski-Kürthy, 2010).

Today, there are no technical limits to the broad expansion of cashless payment. Individuals (could) receive their income into bank accounts, can make transfers from their bank accounts to others’ (individuals’, public utilities’, institutions’) accounts from the bank branch or even from home electronically, and can pay by card for goods and services. Cashless payment is widely spread if there are no technical limits to its exclusivity; maintaining cash payments in a narrow scope is justified by practical reasons only. What is the cause and explanation for the volume of cash in circulation significantly in excess of the “normal” cash demand of economy? A certain part of the “excess” cash volume is required by shadow economy associated with tax evasion and corrupt or “non-corrupt” tax evasion, while the other part can be explained by the sales of common delinquent illegal markets (prostitution, drug or arms trade).

If there is an upper limit of payment in cash per transaction in trade (both on the goods and services markets), the cash withdrawals and payments at the bank cash desks are limited per transaction, they would result in a cash deficit compared to the volume of cash necessary for “financing” corruption, which would hinder i.e. limit corruption, as absurd as this conclusion may sound.

Of course, cash demand can be satisfied with foreign currencies, as well; but the conversion involved in the substitution would make the transactions related to the corrupt practice more complicated and dangerous, so at least it can have a deterrent effect. The ideal version would be to restrict cash payments to a wide scope of countries, or at least to the stable currencies of “more reliable” countries.

Cash payment limits can be set based on practical considerations, changed based on experience and occasionally indexed according to the inflation rate. In Hungary, to use an example, minimum wage could be a recommended limit.
4.3 Gradual limitation of tax havens and offshore areas

If the taxpayers were obligated to satisfy part or all of the tax liability arisen from their economic activity at the real site of the activity, the scope of taxpayers would widen and government revenues would increase. Ideally, the companies registered in tax havens or offshore areas would pay tax in the countries where the economic activity actually takes place. This is conditioned by a wider (complete) international agreement, followed by decision and action. The time between the start of the action and completion of the process cannot be too big, because the enforcement of a fast-paced movement of the immense (almost impossible to estimate) cash volume associated with the tax havens and offshore areas could cause unpredictable foreign exchange fluctuations (Péli, 2010). In the less ideal case, at least the difference between the tax liability according to the national rates and the tax paid abroad should be paid by the taxpayer at the real site of the activity. According to tax experts, taxpayers can be compelled to do this even under the current regulations (Brother Layman, 2011).

5. Summary

It is society’s common interest to have as many ethical taxpayers and as few tax evaders as possible. The goal, albeit not easily and quickly, can be achieved. The strongest and least costly means to increasing tax-paying willingness would be publicity, which should be achieved by eliminating the confidentiality of tax returns. A least simple and fast means would be restricting corruption, fraud and tax evasion. The money movement associated with the corrupt practice is executed in cash instead of transfer between bank accounts; therefore restricting the amounts which can be paid in cash hinders corruption. A third recommended step affects a well-known area. The existence of tax havens and offshores is disadvantageous to many countries; eliminating them or at least gradually diminishing them would attenuate the disadvantages. If significant results cannot be obtained in the foreseeable future, financing the common expenses in the long term becomes impossible. The consequences are impossible to predict.
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