



Uniwersytet
ŁÓDZKI



**WYDZIAŁ PRAWA
I ADMINISTRACJI**

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Streszczenie rozprawy doktorskiej

Zasada równości a progresywne opodatkowanie dochodu

Summary of Ph.D. dissertation

The Equality Principle and Progressive Taxation of Income

Dissertation prepared

at Material Tax Law Department

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Łódź 2017

The Ph.D. dissertation regards a problem of compliance of progressive income tax with the equality principle. There are two elements of analysed matter: first - the equality principle and second – progressive taxation of income.

In Polish legal system the principle of equality is stipulated in art. 32 sec. 1 of the Constitution of the Republic of Poland: "All persons shall be equal before the law. All persons shall have the right to equal treatment by public authorities". The examination of the principle of equality should be carried out with reference to the of the Constitution of the Republic of Poland, but above all based on the jurisprudence of the Polish Constitutional Court, which is of universal significance because of identity of the equality principle meaning in various legal systems.

Equality has two aspects: horizontal and vertical. Horizontal equality implies that we give the same treatment to people in an identical situation. On the other hand, vertical equality means that people in different situations should be treated differently. This is why the equality principle in general can be described as different treatment of unequal situations and equal treatment of equal.

On the ground of tax law equality can be described more precisely by different theories. There are two groups of such theories: the benefit theory and theories including the ability-to-pay principle. First is the theory where taxes should be considered as payments for services rendered by the state to the taxpayers and so proportioned. Second theories consider taxes as an obligation that is not connected with the provision of services by the state but with taxpayers' possibility to pay them. The ability-to-pay approach treats government revenue and expenditures separately. Taxes paid are seen as a sacrifice by taxpayers, which raises the issues of what the sacrifice of each taxpayer should be and how it should be measured. In this matter the most well-known theory that includes ability-to-pay principle is the equal sacrifice theory that has three alternative variants of interpretation (alternative theories):

- a) equal absolute sacrifice - the total loss of utility from income as a result of taxation should be equal for all taxpayers,
- b) equal proportional sacrifice - the proportional loss of utility from income as a result of taxation should be equal for all taxpayers,
- c) equal marginal sacrifice - the instantaneous loss of utility from income (as measured by the derivative of the utility function) as a result of taxation should be equal for all taxpayers. This therefore will entail the least aggregate sacrifice (the total sacrifice will be the least).

Having interpreted the principle of equality at both the general, as well as the tax law, we could focus on the second component of the subject matter of this dissertation, that is, the progression in income tax.

First of all we should clarify the concept of progression in tax law in general and the progression in income taxation, while taking into account the history of the development of this form of tax burden distribution. Although narrowly covered in this dissertation is the subject of personal income tax, the conclusions of the study will also refer to corporate income tax.

A progressive tax is a tax in which the tax rate increases as the taxable amount increases. The term "progressive" refers to the way the tax rate progresses from low to high, with the result that a taxpayer's average tax rate is less than the person's marginal tax rate.

Progression in taxation has long history. Its sources, on which we have knowledge, reach back to ancient Athens and Solon's time, when progression was determined to belong to one of the four social classes. On the other hand progression, as indicated above, in the form of progressive tax rates appeared already around 380 B.C. during the administration of Nausinicus. The beginnings of progressive income tax as we know it nowadays date back to the end of the 18th century, when a progressive personal income tax was introduced in the United Kingdom. In Poland, the income tax was introduced by the Act of July 16, 1920 on the state property tax and income tax. It was also the first progressive income tax in Poland.

Despite its long history there is no undisputed way of justifying such form of taxation of income. In this regard, particular emphasis should be placed on the abovementioned equal sacrifice theory as the theory of broadest impact, taking into account all three variants of its interpretation (alternative theories), i.e. the equal absolute, proportionate and marginal sacrifice. In order to fully illustrate the existing forms of justification for progression, we should mention also that there are other methods of argumentation based on the other modes of interpretation of the principle of equality. I mean here those that were built on the benefit theory and other than theory of sacrifice theories that include the ability-to-pay principle. We could also find justification for progressive income tax in theories separated from the notion of the principle of equality, i.e. socialist and compensatory theory. Despite that other theories than the equal sacrifice theory which try to justify progression, are nowadays denied as unacceptable.

The sacrifice theory can be interpreted in quite different ways depending on the configuration of the appropriate conditions: (i) the three alternative variants of interpretation of the sacrifice theory in the form of equal absolute, proportional or marginal sacrifice, (ii) concept of distribution of tax burden among taxpayers, i.e. the concept of income or its utility and (iii) depending on the function of utility in one of the two possible growth variants, i.e. accelerated and linear growth. Depending on the way we interpret the sacrifice theory, we can get a justification for how to distribute the tax burden on fixed tax rates independent of the tax base, through progressive, degressive and regressive rates.

Taking into account the multiplicity of factors influencing the interpretation of the sacrifice theory, it is worth pointing out that the search for justification for progression in income taxation only in the alternative theory of the sacrifice theory in the form of equal absolute sacrifice, taking into account the utility of income as the basis for determining the distribution of tax burden and only if the total utility value obtained with income increases slower than the increase in the value of income, one could point to the justification of progressive tax scale. It cannot be left alone, in terms of determining the utility function, only on the statement that it increases in a delayed variant but that it increases in that variant in a strictly defined manner that does not justify either the proportionality of taxation or its regressivity. Also the alternative theory of equal proportional sacrifice, taking into account the utility of income as the basis for determining the distribution of tax burden, and only on the basis of increasing the value of total utility of income in a delayed way, the increase in the value of income may be indicative of a justification for a progressive tax scale.

Only after explaining the significance of the principle of equality and variants of its interpretation and by presenting the characteristics of progression in income tax and the proposed ways of justifying this form of tax burden distribution, we can focus on compliance of the quality principle with progressive income tax.

The effect of the analysis of the principle of equality for progressive income tax and the justification of this method of taxation of income shall be the assessment of the compliance of progression in income tax with the principle of equality. This assessment should first be carried out at the level of analysis of theoretical considerations, taking into account the principle of equality. Then, taking into account the previously explained explanation of the importance of the principle of equality and its possible interpretation as well as the characteristics of progression in income tax and the

permissible means of justifying this form of tax burden distribution, a comparison of the abovementioned matters shall be carried out in practical terms.

What is important is the fact that the abovementioned way of justifying progression in income tax, in practice, raises serious doubts that make this theory unacceptable. The weaknesses focus on the proper distribution of tax burdens among taxpayers according to the utility of income, as the uncertainty surrounding the definition of utility, marginal utility and the unidentified utility function, which is absolutely essential for the distribution of tax burden among the taxpayers. That is way we cannot implement this theory.

Irrespective of the lack of justification for progression in income taxation on the ground of existing theories as presented above, these considerations should be completed by attempting to verify the admissibility of the theoretical justification for practical solutions in the form of progressive taxation of income based on the premise of its differentiation, by analysing selected practical solutions.

After analysing practical solutions, also by designating a function of utility, concerning income taxation in Poland, Estonia, United States and Netherlands (group of representative states and legal systems), there was no possibility to accept progression as described in those legal systems as consistent with the equality principle as described above.

Inconsistency with the alternative theories of sacrifice theory resulted from the following premises:

- a) unjustified change in the rate of decline in marginal utility in respect of income corresponding to the tax thresholds (Poland, United States, Netherlands);
- b) the increase in the marginal utility value for income corresponding to the tax thresholds (Netherlands);
- c) from an arbitrarily determined range of income exempted from taxation (tax-exempt amount) (Poland, Estonia, United States, Netherlands);
- d) the most intense decline in marginal utility of income in the range of low income (Poland, Estonia, United States, Netherlands).

In conclusion, there is no justification for the progression in income taxation, based solely on the premise of differentiation of taxpayers' income, while taking into account the equality principle. Independently whether we are trying to study the theories developed in this field, taking into account their practical application, or analysing practical solutions, we are looking for a concept that best fits in with the progression but

there is none. Thus progression, in its pure form based on the premise of income differentiation, is contrary to the principle of equality, as there is no theoretical justification based on the concept of equality as well practical based on the solutions used in this matter.

The effect of such an interpretation of the principle of equality is proportional taxation, which, contrary to progression, is the most appropriate way of taxing income, which is not based on an intuitive conception of equality that could justify that kind of taxation, but logically coincides with the accepted and practically applicable interpretation of the principle of equality.

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