

Tax Filing in the U.K.: A Guide for the U.S. When Eliminating the Marriage Penalty

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ABSTRACT

The United States is one of the last countries to use the joint return for married couples' tax filing; most other countries have adopted individual filing. In 1990, the United Kingdom completed its transition from a tax system that required husbands and wives to file as a marital unit to one that requires individual filing, and so it has two decades of experience with the new regime. Although the U.K. ought to be a rather obvious example for the U.S. to consider if the U.S. government decides to change its filing requirements, little research has been done on the British change in policy. Examining first what makes a valuable international comparison, this paper then reviews the origins and development of the mandatory joint return and the forces that drove the change to individual filing in the U.K. Perhaps most importantly, the paper also appraises the consequences of this revision of British law. Evaluating the change in the U.K., including the improved economic position of many wives and the increased incidence of tax avoidance, this paper explores its implications as a model for the U.S. In doing so, it urges consideration of the costs as well as the benefits of changing tax units.

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INTRODUCTION

While few would dispute that “reinventing the wheel” is generally a waste of time and resources, Americans often do just that when considering changes to fiscal, and other, policies. As a nation, we are more inclined to explore what has already been tried in the United States than examining what has been undertaken abroad. It is rare for U.S. policymakers or scholars to consider the experiences of other countries. This is unfortunate because some reforms currently being proposed in the U.S. are similar to those that have already been adopted abroad. For example, the U.S. is one of the last countries to have a marriage penalty in its tax code that results from a joint filing system with a separate rate bracket for married couples. For decades there has been a worldwide movement, which many American academics now join, in favor of individual tax filing as a means of promoting gender equality and eliminating that marriage penalty.² Surprisingly, virtually all of the American scholars who agree with this conclusion do so without examining the numerous real world examples of this change in policy.

Before 1970, only six OECD countries taxed spouses separately; the others shared the American system of taxing married couples as a unit. By 1980, seven of those countries had adopted individual taxation and three more did so in 1989 and 1990. In the same period, no country moved to joint taxation.³ In Europe alone, Austria, Belgium, Denmark, Finland, Italy, the Netherlands, Spain, Sweden, and the United Kingdom have moved from primarily joint taxation to individual taxation.⁴ Because so many countries in recent years have changed how

² See OECD, FUNDAMENTAL REFORM OF THE PERSONAL INCOME TAX 54-56, 114-26 (2006); *The EC Commission on Income Taxation and Equal Treatment for Men and Women*, 39 BULL. INT’L FISCAL DOCUMENTATION 252 (1985); Norma Briggs, *Individual Income Taxation and Social Benefits in Sweden, the United Kingdom, and the U.S.A.*, 39 BULL. INT’L FISCAL DOCUMENTATION 243 (1985). See also note * below. Among the dozens of articles by American scholars on this topic, see ALICE KESSLER-HARRIS, IN PURSUIT OF EQUITY 170-202 (2001); EDWARD McCAFFERY, TAXING WOMEN (1997); Lily Kahng, *One is the Loneliest Number: The Single Taxpayer in a Joint Return World*, 61 HASTINGS L.J. (forthcoming, 2010); Wendy Richards, *An Analysis of Recent Tax Reforms from a Marital-Bias Perspective*, 2008 WIS. L. REV. 611 (2008); Lora Cicconi, *Competing Goals Amidst the Opt-Out Revolution*, 42 GONZ. L. REV. 257 (2007); Shari Motro, *A New ‘I Do’: Towards a Marriage-Neutral Income Tax*, 91 IOWA L. REV. 1509 (2006); Amy C. Christian, *The Joint Return Rate Structure: Identifying and Addressing the Gendered Nature of the Tax Law*, 13 J.L. & POL. 241 (1997); Lawrence Zelenak, *Marriage and the Income Tax*, 67 S. CAL. L. REV. 339 (1994); James Edward Maule, *Tax and Marriage: Unhitching the Horse and the Carriage*, 67 TAX NOTES 539 (1994); Marjorie E. Kornhauser, *Love, Money, and the IRS: Family, Income-Sharing, and the Joint Income Tax Return*, 45 HASTINGS L.J. 63 (1993); Bea Ann Smith, *The Partnership Theory of Marriage: A Borrowed Solution Fails*, 68 TEX. L. REV. 689 (1990); Carolyn C. Jones, *Split Income and Separate Spheres: Tax Law and Gender Roles in the 1940s*, 6 LAW & HIST. REV. 259 (1988); Pamela B. Gann, *Abandoning Marital Status as a Factor in Allocating Income Tax Burdens*, 59 TEX. L. REV. 1 (1980); Alicia Munnell, *The Couple versus the Individual*, in THE ECONOMICS OF TAXATION 247 (Henry J. Aaron & Michael J. Boskin ed.s, 1980); Wendy Gerzog, *The Marriage Penalty: The Working Couple’s Dilemma*, 47 FORDHAM L. REV. 27 (1978); Michael J. McIntyre and Oliver Oldman, *Taxation of the Family in a Comprehensive and Simplified Income Tax*, 90 HARV. L. REV. 1573 (1977); Boris Bittker, *Federal Income Taxation and the Family*, 27 STAN. L. REV. 1389 (1975); Grace Ganz Blumberg, *Sexism in the Code: A Comparative Study of Income Taxation of Working Wives and Mothers*, 21 BUFF. L. REV. 21 (1971): 49-98.

³ CONGRESSIONAL BUDGET OFFICE, FOR BETTER OR FOR WORSE: MARRIAGE AND THE FEDERAL INCOME TAX, Appendix A (1997). Individual taxation often applies only to earnings. In 1993, of 27 countries in the OECD, 19 countries taxed earned income separately but taxed couples’ investment earnings collectively. *Id.*

⁴ Cathal O’Donoghue and Holly Sutherland, *Accounting for the Family: The Treatment of Marriage and Children in European Income Tax Systems*, Innocenti Occasional Papers, Economic and Social Policy Series (1998), at 12.

they tax married couples, there are many opportunities for the U.S. to learn from these nations' experiences as it considers undertaking a similar change in policy.

The U.K. switched from a system that required husbands and wives to file tax returns as a marital unit to one that requires individual filing. It completed this transition in 1990 and so has two decades experience with the new regime. Although the U.K. ought to be an obvious example for the U.S. if the U.S. government decides to change its filing requirements, little research has been done in the U.S., or made widely available to U.S. legal scholars, on the British transition.⁵ This paper fills in this gap in knowledge as it evaluates the potential costs and benefits of changing tax units using the U.K. as a case study. It looks at the forces that drove this change in British law and the consequences of the change, and discusses its implications for the U.S.

The paper begins in Part I by setting forth general guidelines for assessing the usefulness of international comparisons. Because not all countries share the same objectives for their income tax or apply it in the same way, it is important to evaluate whether a particular country makes a good subject for comparison with the U.S. This part first examines baseline questions for when an international comparison will be useful. Concluding that the U.K. is a good subject of comparison, despite significant differences in the structure of the two nations' taxing regimes, it then develops a framework for evaluating particular changes in the law. In order to make an effective comparison of similar policy changes in different countries, evaluations must be made as to whether or not the stated goals of the policy would differ between the countries, whether the policy change would likely have a different impact on tax compliance in the two countries, and whether we should expect the unintended consequences of the change (both the good and the bad) to be different.

With those differences in taxing regimes in mind, Part II explores the early development of the British income tax and why Parliament initially adopted the joint return. Focusing on the tax system's impact on women and its interaction with the women's movement, this section examines the evolution of how wives were treated by the tax regime. Part III then evaluates how and why the British parliament adopted individual filing, or as they would call it "independent taxation," in the Finance Act of 1988, which became effective in 1990.⁶ The transition began in 1972 when Parliament introduced optional separate filing, permitting wives to file individual returns for their earned income and for their resulting tax obligations to be calculated as though

Ireland has been gradually switching from joint to individual assessment to improve secondary earner's incentives to enter work. *Id.* The Netherlands is the only country whose tax law treats unmarried persons living together as married couples. Joseph A. Pechman and Gary V. Engelhardt, *The Income Tax Treatment of the Family: An International Perspective*, 43 NATIONAL TAX J. 1, 7 (1990).

⁵ Economists have looked at its impact on transfers of property within the family but not the legal developments. See Melvin Stephens, Jr. and Jennifer Ward-Batts, *The Impact of Separate Taxation on the Intra-Household Allocation of Assets: Evidence from the UK*, 88 J. PUB. ECON. 1989 (2004). Ann Mumford will have a chapter on the tax unit in her forthcoming book on British taxation and its impact on women. Ann Mumford, draft, "Chapter 5: Tax, Law and the Idea of the Family," at 2 (on file with author). However, Mumford takes as her baseline the move to individual taxation and argues that a subsequent shift to a child-centered focus now hurts women.

⁶ Individual filing is more commonly referred to as "independent filing" in British writing. I have retained the phrase individual filing for the ease of my largely American audience.

they were single persons. In 1988, Parliament went further and denied married couples the option to file jointly by adopting mandatory separate filing.

Part IV of the paper appraises the consequences, some of which were unintended, of the U.K.'s adoption of individual filing and considers what guidance the U.K.'s experience can provide American policymakers. It examines how the incentives created by individual filing have influenced couples' legitimate economic activity as well as how they avoid taxes. Because the wife is typically the lower-earning (or non-earning) member of a couple and so will be taxed at a lower rate than her husband, individual filing gives couples an incentive to shift more of the family's income to wives. Among law-abiding couples, this will typically encourage more wives to enter the paid labor market and encourage couples to shift income-producing property to wives. This paper explores whether British couples made either of these responses when joint filing was adopted, and to what extent they reduced couples' total income tax burdens and improved wives' economic situations and relative power within marriage. Individual filing may also encourage tax avoidance when higher-income spouses seek to shift income to lower-income spouses for tax purposes without losing control over the income-producing property. This paper examines whether a significant number of higher-income spouses use avoidance devices to transfer tax ownership of properties, but no other substantive rights to the properties, to their lower-income spouses, and what new pressures this form of tax avoidance puts on the British tax system.

The paper concludes that the effects of Britain's adoption of individual filing should provide a warning to the U.S. Adopting individual filing has caused serious complications in the U.K., and U.S. policymakers must consider these consequences before the tax unit is changed. Even if adopting individual filing ultimately proves to be the best choice, the costs as well as the benefits need to be included in the political calculation, and looking carefully at the British experience with individual filing can offer us meaningful guidance as we try to predict what these costs will be.

PART I: WHY THE U.K.? RULES AND REASON

We have all heard about the dubious value of comparing apples to oranges; likewise, inapt or ill-considered comparisons of policies across legal systems will teach us little and may prove misleading. On the other hand, careful, informed comparisons between legal systems that have sufficient common ground can be highly instructive. By looking at similar legal systems that have already adopted policies that are being considered in the U.S., American policymakers can gain valuable insight into practical consequences of such policies. In order to benefit from such comparisons, we must answer the questions: What characteristics must two nations' legal systems share to make comparisons between them meaningful and under what circumstances can one nation's policymaking experience help predict the effects of legal change in another?

These are difficult questions, particularly when the policies under consideration involve two nations' tax regimes. The tax systems of most developed countries have grown incredibly complex, and when comparing the effects of different nations' tax policies, it is vital to

understand how the policies under consideration fit into these complex systems. Indeed, even for taxes that appear facially very similar, both their purpose within the overall national systems and the nations' broader goals for their revenue systems can vary so greatly as to make a comparison virtually meaningless. This Part examines the questions that should be asked to ensure that the U.S. and the U.K. share enough legal, social, and cultural common ground that these two tax systems provide useful information and examples to the each other about the costs and benefits of various income tax policies. In order for us to determine whether the U.K.'s experience in adopting individual filing can offer meaningful insight and guidance to U.S. policymakers, we must establish two things. First, we must determine that good comparisons can generally be made between the U.K.'s income tax system and that of the U.S. Second, we must, for both countries, be able to isolate the effects of a change in the tax unit and to identify what variables determine how the choice of tax unit will affect taxpayers and the revenue system generally.

A. GOOD COMPARISONS

Not everyone accepts the value of comparative research. Mary Ann Glendon once wrote, "To many American lawyers, an interest in other legal systems is a something like an interest in wines: a little knowledge about them is a sign of good taste and sophistication, but a serious dedication may be evidence of waste, or luxury, or even worse."⁷ This attitude is likely caused by the fact that the probative value of comparisons between legal systems is often dubious: While a fairly broad range of comparisons between nations may be interesting for survey or theoretical purposes, relatively few international comparisons will offer policymakers meaningful practical insights into a particular issue, and finding the right nations for such a comparison requires hard work. Possibly for that reason, some comparative studies shy away from applying concrete, specific lessons from one country to the other.⁸

Policymakers that want to take such concrete, practical lessons from comparative legal studies, and particularly those that will use such studies to help predict the consequences of undertaking a particular legislative change, need make sure that they choose a nation whose legal and revenue systems are similar to their own in certain fundamental ways. Otherwise it is unlikely that even identical policy choices will have similar consequences. Moreover, they need to understand these legal and revenue systems well enough to be able to identify what factors are likely to cause the results of similar policy changes to produce different results in the two nations.

This paper employs a comparative methodology in order to help U.S. lawmakers assess the likely consequences of a specific policy change. Because it allows legislators to learn by studying the experiences of another nation when it made this same policy change, American policymakers can avoid starting from scratch as they consider the policy and may be able to shape a final policy that avoids the negative unintended consequences that the other nation experienced.⁹ For such a comparison to offer U.S. lawmakers meaningful practical insight about the policy under consideration, this paper must be sensitive to differences in the culture, politics,

⁷ Mary Ann Glendon, *Why Cross Boundaries?* 53 WASH & LEE L. REV. 971 (1996).

⁸ For example, despite its title, see William Gale, *What Can America Learn from the British Tax System?* 18 FISCAL STUDIES 341 (1997).

⁹ Thuronyi, *supra* note *, at 4.

and economies of the two countries. This requires a careful, nuanced investigation of differences between the two countries that goes well beyond the nations' tax systems themselves and warns us that in all such research that there is no perfect comparison. Indeed, there will be important differences between any two countries, and so, at some level, using international comparative work for policy purposes will always require us to make the leap of faith that, despite these differences, the knowledge we gain from looking at another country will be useful in ours.

The information gained from a such a comparison is most likely to be useful to policymakers if the comparison employs countries with certain key factors in common and if it clearly acknowledges where the countries differ. When studying income tax regimes, broad threshold questions of politics and economics can eliminate many nations from consideration. Is there a genuine rule of law in both countries and how strong are the legal institutions that regulate their income taxes? What are their relative levels of economic development and are these levels so different that one can expect their income systems to differ accordingly? Is one or both of the nations constrained by supranational organizations that limit its individual sovereignty?

These threshold questions are easily answered in this paper for the nations under review. The U.K. and the U.S. are both wealthy, industrialized democracies with common law backgrounds and robust, effective legal institutions, albeit with important variances in their law and politics that will be discussed below. Although the U.K. is a member of the European Union, it retains substantial freedom in devising its own tax system as, of course, the U.S. has. Therefore, while there are important differences between the U.K. and the U.S., the initial threshold questions do not suggest that the comparison should be abandoned.

Nevertheless, both to determine whether the comparison is genuinely worthwhile and to understand its limitations, we must look more specifically at the American and British income tax systems. This examination focuses on five sets questions. First, to what extent are both countries dependent upon the revenue generated by the income tax so that they have vested interests in protecting its revenue-raising potential? Because the U.S. is reliant upon the income tax as a source of revenue, if the second country is not similarly dependent upon the income tax, the two nations are likely to have different concerns, and, consequently, make different choices when they alter the tax. Like the U.S., the U.K. relies heavily on its income tax, although the U.K. raises comparatively more revenue from internal taxes. Despite its value-added tax (VAT), the British income tax has fluctuated between 11.7% and 10.1% of the U.K.'s GDP and 39% and 30.9% of its tax revenue between 1976 and 1990. In the U.S., the percentage was always lower but shared a similar trend, from 8.2% to 8.3% of GDP and 46.6% to 46.1% of tax revenue.¹⁰ Clearly, both nations rely on the income tax as a vital source of revenue, and so both have a strong incentive to consider very carefully how any proposed change to the income tax will improve or worsen the tax's effectiveness.¹¹

¹⁰ INTERNATIONAL MONETARY FUND, TAX POLICY HANDBOOK 289-94 (1995). In the U.K., by 2005 the income tax was down to 28% of revenue. OFFICE FOR NATIONAL STATISTICS, UK 2005, THE OFFICIAL YEARBOOK OF THE UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND 365 (2005).

¹¹ Isabelle Joumard, "Tax Systems in European Union Countries," Economics Department Working Papers, No. 301, OECD, Jun. 29, 2001, at 10.

Second, to what extent does the political process behind the creation and evolution of the income tax differ between the two countries? How much do taxpayers and their interest groups participate in the political dialogue that shapes tax policy? After the tax policy is determined, how aware are people of taxation and how compliant are they with the paying the tax? There are substantial differences between the two countries under review in terms of the overall process of tax policy creation and the public's interest and involvement in that process. As discussed in more detail below, unlike in the U.S., where tax policy typically develops as a result of a complex drafting and negotiation process that is largely public and involves both the executive and legislative branches of government, British tax policy is more of a closed process where a substantially final, complete policy is designed by the administration and then only voted on, rather than negotiated or "marked up," by Parliament.¹² Not only does this result in less public awareness of the process and less overt interest group pressure, but it has allowed the British government to design a simpler regime than exists in the U.S. In part as a result of the simplicity and structural features of the British tax, British taxpayers are less aware of the income tax and yet are also less compliant than their American counterparts.¹³ These differences in how the income tax is legislatively modified and how the public perceives of the tax will impact the validity of comparisons between the countries. Throughout this paper, the potential impact of these differences has been highlighted.

Third, to what extent does the structure and practical administration of the two income taxes differ? Are these differences substantial enough that we should expect similar policies to produce different results in practice? Answering these questions requires considering not only the general degree of complexity of the tax codes but also far-ranging and very specific details of their operation. For example, how do the countries define income, do the variety and purpose of deductions differ, and to what extent are the taxes collected at the source of income? The answers to these questions reveal substantial differences in the administration of these two income taxes.

The U.K. has a schedular system of defining income whereby the income and deductions of different sources of income are separately assessed, whereas the United States uses a global definition that combines all income and deductions in a single calculation. One consequence that has evolved from these two approaches is that the U.K. has a more limited, source-based concept of income as opposed to the broader, American concept that any realized increase in wealth is taxable income.¹⁴ Furthermore, the British system has a pay-as-you-earn (PAYE) system instead of the American withholding and self-assessment system, although the U.K. has been moving in the direction of more self-assessment since 1996.¹⁵ Not only does the PAYE system tell taxpayers how much they owe, but it calibrates the amounts withheld to ensure that neither refunds nor payments are due at the end of the taxable year. Even under the post-1996 system, only about 9.3 million people, typically those with higher incomes, those who are self-employed,

¹² See note * below.

¹³ Kay and King.

¹⁴ Thuronyi, *supra* note *, at 26, 236.

¹⁵ Gale, *What Can America Learn*; Victoria Curzon Price, "The British Tax System: Opposing Trends", http://www.irefeurope.org/col_docs/doc_9_fr.pdf, at 3.

or those with investment income, are required to file a tax return in the U.K.¹⁶ Thus, only about 35% of British taxpayers, and only 20% of wage earners, as opposed to more than 100% of all American taxpayers, are required to file income tax returns.¹⁷

The PAYE system works, in part, because the British income tax is simpler than the American system, which makes self-assessment unnecessary in most cases.¹⁸ For example, there are many fewer deductions in the British tax than in the traditional American tax, although the American alternative minimum tax (AMT) with its flat tax features eliminates many of these deductions. Simplicity in operation is an important goal in the U.K., even if the statutes themselves are not always simple.¹⁹ While the U.S. claims to have such a goal, little has been done to make it so in practice. Similarly, there are currently fewer rate brackets in the U.K., although the number was once extensive and it is growing again. Before 2010 there were three brackets, with 10%, 20%, and 40% rates, but in 2010 a 50% bracket was added. There are also special rates for savings income or ordinary dividends. There are an estimated 29.9 million individual taxpayers, of which only 3.4 million, or 11.4% in the highest bracket in 2004, the latest year for which we have numbers.²⁰ These structural differences between the U.K. and the U.S. are significant and will likely affect the impact of individual filing; however, the two regimes share sufficient similarities that the impact of the differences can be discussed in the remainder of this paper.

Fourth, to what extent does the enforcement of the taxes in the two nations differ? Seeking to maintain its simplicity, unlike in the American system, the British income tax has no general anti-avoidance rule.²¹ Instead of the common law doctrines and broad anti-avoidance legislation and regulations that U.S. regulators use to pursue tax avoiders whose actions breach the spirit, but not the letter, of the law, the British tax system demands that Parliament clearly define the income it wants to tax. As discussed in Part IV below, the British regime largely

¹⁶ OFFICE FOR NATIONAL STATISTICS, UK 2005, THE OFFICIAL YEARBOOK OF THE UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND 372 (2005).

¹⁷ Approximately 17 out of 26 million individual taxpayers had no need to file tax returns and 50% of those who do are self-employed. William J. Turnier, *PAYE as an Alternative to an Alternative Tax System*, 23 VA. TAX REV. 205, 224 (2003). Americans who are not taxpayers have to file income tax returns because the system is also used to distribute government aid, such as the Earned Income Tax Credit.

¹⁸ Gale, *What Can America Learn*.

¹⁹ See discussion at * below. This is true despite the fact the British tax is still relatively complex. THURONYI, *supra* note *, at 17.

²⁰ OFFICE FOR NATIONAL STATISTICS, UK 2005, THE OFFICIAL YEARBOOK OF THE UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND 372-73 (2005).

²¹ This is discussed more fully in part IV below. For a discussion of how tax statutes are interpreted, see HUGH AULT AND BRIAN ARNOLD, *COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS* 132-34 (2004); VICTOR THURONYI, *COMPARATIVE TAX LAW* (2003); David W. Williams, *Taxing Statutes are Taxing Statutes*, 41 MODERN L. REV. 404 (1978). In *Duke of Westminster*, [1936] A.C. 1, the House of Lords refused to look at the substance of a transaction to determine if a “real” change has occurred that warrants special tax treatment. As a result, rules are very narrowly drafted to prevent individual avoidance devices. Even after the landmark *W.T. Ramsay Ltd. v. CIR*, [1982] A.C. 300 (1981), in which the House of Lords effectively adopted a step transaction doctrine, allowing the courts to disregard elaborate planning steps by taxpayers that have no individual substance, “[t]his does not mean that strategic tax planning is impossible; far from it. However, it is not advisable unless you can afford good advice, are prepared to take time to understand the details of how and why tax can be avoided, and appreciate fully the risks you are taking.” Granham, *supra* note *. The use of legislative history in judicial interpretation was only accepted since 1993 and not in all cases. THURONYI, *COMPARATIVE TAX LAW*, 136.

protects taxpayers who can make the formal case that their income falls outside the precise definition. Although it has been moving to a more American-style system, the traditional policy dates back to William Pitt, who complained in 1798, if the people were “right in supposing that conscientious men would think themselves justified in taking every advantage to evade the law, it was the more incumbent on him to make the letter of the law so strict that the spirit should not be evaded.”²² British Tax avoidance is largely a test of statutory construction, and to a certain extent, form over substance; taxpayers generally succeed in avoiding taxes if they structure their transactions to gain favorable tax treatment under the literal language, if not the purpose, of the various revenue statutes. This difference in systems will have a definite effect on the effectiveness of policing sham transfers between spouses, discussed more fully in Part IV below.

Finally, to what extent is the income tax meant to further social goals, or goals other than to simply raise revenue, in each nation? More specific questions regarding the nature of the goals pursued through the adoption of individual filing will be discussed in the next section. As for general social policy, the U.S. has long incorporated social policy goals in its tax code, for example through the numerous deductions and credits that have been developed in an attempt to shape behavior, such as deductions that encourage charitable donations, home ownership, and secondary education. While the U.K. shares an understanding that the income tax can be used to implement social policy, it has never attempted to do so to the extent that the U.S. does. The U.K. has many fewer deductions and tax credits, and, while the lack of these deductions and credits helps to preserve the simplicity of the U.K.’s system, it may do so at the cost of making individuals’ tax liabilities less closely tied to their ability to pay than in the U.S. system.

Nevertheless, both nations generally share, and attempt to advance, the larger social policy goal of taxing people according to their ability to pay taxes and both seek, within broad limits, to advance policies the dominant political party finds important. For example, the adoption of individual filing in the U.K. was driven not by revenue objectives but by social ones.²³ The U.K. did so to help particular family structures, namely single-earner families, by reducing their tax obligations. In the same decade, the U.S. shared many of these same goals and sympathy for single-earner families; however, the U.S. did not change its taxable unit to assist them and there was no adoption of the British rhetoric in the U.S. Why those means to the same social ends did not cross the pond is curious. Similarly, why the U.S. generally regards, and uses, the tax system as a more effective vehicle for serving social goals than does the U.K. is unclear. Nonetheless, both nations clearly regard the tax system as an appropriate and effective means of furthering governmental and societal objectives.

Based on these questions, it is clear that the most important differences between the British and American tax systems are in their structure and administration, and it is primarily these differences that will make comparisons between the U.K. and the U.S. less than perfect. These two nations have sufficiently different approaches to the mechanical details of income taxation that it is likely that making the same change in policy in the two countries will produce somewhat different results. That does not mean, however, that these results will be radically different or that one nation’s experience with a particular policy will not be instructive to the other. However, if the comparison is to be practically useful, it is important to identify and

²² The Parliamentary History of England, vol. 34 (1819), at col. 132.

²³ This issue is discussed in more detail in Part III.

understand the factors that are likely to weaken it. The British system's streamlined structure and administrative simplicity compared to the much more complex Americans system will definitely alter the consequences of a change in the taxable unit.

We then must consider how these differences are likely to affect the results of the comparison. With respect to the issue of the tax unit, one should expect that, because the system in the U.K. is so simple, problems created by a change in policy might be harder to eliminate through the use of additional regulation, whereas in the United States, the complexity of the system is likely to increase and aggravate the unintended consequences of policy change. While these factors may not come into play in every change in policy, they should be kept in mind in any comparative study of U.S. and U.K. tax policy. If we do so, and understand how they are likely to influence our comparisons, the U.K. is generally a good country to use for tax policy comparisons with the U.S., and these comparisons can produce valuable insights as we try to predict the effects of regulatory change.

B. ISSUES OF POLICY

This project adds a second layer of complexity to the international comparison because it is not merely comparing revenue systems as a whole but, instead, is isolating the effect of a policy change to one particular aspect of one part of the system, the taxable unit used in the national income tax. That aspect has been changed relatively recently in the U.K. but, so far, held constant in the U.S. Because modern tax systems are so complex and because so many variables are likely to shape the results of a change within a given income tax system, attempting to isolate the effects of a single policy change in a single country can be difficult, and doing so in two countries is even more challenging. Consequently, comparative studies of the effects of legal change require a close examination of the variables influencing these policies and how these variables differ between the two countries. In other words, it is important to know whether or not we can expect similar results from similar policy changes in the U.S. and in the U.K. and what may cause the results to differ.

The income tax is made up of thousands of small policy choices, each one shaping in some way how effectively the entire tax operates. Some of those smaller choices do not excite the public and do not appear to even interest most policymakers.²⁴ Despite legislators' lack of interest in the small details of policy formation, an international comparison of a particular policy decision must consider how these small details differ between the two countries in much the same way it considers the broader similarities and differences between the two nations' legal and tax systems. As with the larger, structural comparison, the purpose of this evaluation is to highlight factors that might cause the comparison to produce faulty advice and inaccurate predictions. The three general factors this evaluation should consider are the stated goals of the policy change, the impact of the policy on the operation of and compliance with the tax, and the unintended consequences of the policy change. This section lays out a framework of questions and concerns that should be addressed in this evaluation, and Parts III and IV of this paper addresses them specifically. Because only the U.K. has changed its tax unit to date, this paper

²⁴ The public might be rational as to the big picture but not fully informed or, alternatively, institutions might not fully represent their interests. See, John Mark Hansen, "Individuals, Institutions, and Public Preferences over Public Finance," *American Political Science Review* 92 (1998): 513-31.

addresses these questions by focusing on the actual experience in the U.K. and then considering the ways in which the U.S.'s experience would differ if it made a similar change.

First, what were the stated goals of the policy change, as articulated by both the government itself and the various affected interest groups (recognizing that there are likely to be inconsistencies, if not outright conflict, between the various constituencies' statements) and to what extent do the stated goals differ between the countries? In the case of this paper, the questions must be reframed to reflect the fact that the U.S. has not yet adopted individual filing: What were the stated goals of the change in the U.K. and how would we expect them to differ if the policy change was adopted in the U.S.? As a corollary to these larger questions, to what extent has the change achieved its stated goals? Whether one agrees with the stated goals is a political assessment that should be made after this preliminary evaluation has been made. Although it is important to consider the subaltern impact of legal changes, the first step is not to analyze or prioritize these often competing underlying results but, instead, to take the measure and its stated goals at face value.

Second, what impact has the change had on the operation of, and compliance with, the income tax? Has the change proven to be economically efficient or, alternatively, has it produced inefficiencies in the form of tax planning and tax avoidance? If a change in law significantly increases administrative costs or causes a substantial amount of tax avoidance, those considering a similar policy change should weigh that externality heavily against the change's other benefits, both because governments are loathe to spend money on tax enforcement and because the creation of tax avoidance, particularly to the extent it is visible to other taxpayers, might decrease compliance overall.²⁵ This latter concern is likely to be particularly important because many social scientists have moved away from the assumption that taxpayers make independent, rational choices about whether or not to pay their taxes but, instead, have a "bounded rationality" based on their assumptions of the trustworthiness of others within the taxing regime.²⁶ "Taxpayers have little incentive to pay their taxes in the absence of a high degree of 'trust' that other taxpayers and the government were fulfilling their obligations."²⁷ If there are factors that are likely to cause the administrative and compliance affects of a policy change to differ in the two nations under consideration, the comparison should identify them and take them into account.

Third, what unintended consequences has the policy been shown to have? These consequences can be either good or bad; the label of good or bad itself is to some degree subjective. While there are some goals that all of society can agree on, many more divide the public. Nonetheless, while different people may draw different normative conclusions about such consequences, identifying the consequences of a policy change is useful when evaluating the overall success of the measure. Indeed, the unintended consequences of a policy change can be so large or so numerous that they can outweigh the intended consequences of the policy as we evaluate it in hindsight. Included in this group of concerns are the incentive effects of a change

²⁵ See *infra* note *.

²⁶ See, for example, KENNETH BINMORE, *GAME THEORY: A VERY SHORT INTRODUCTION* (2007). A classic statement of public choice is JAMES BUCHANAN AND GORDON TULLOCK, *THE CALCULUS OF CONSENT: LOGICAL FOUNDATIONS OF CONSTITUTIONAL DEMOCRACY* (1962).

²⁷ Daunton, *Trusting Leviathan*, *supra* note *, at 11.

in policy. What does the change in legislation actually cause people to do? Although some new incentives might be intended, that will not always be the case, and it should never be assumed that all policymakers and advocates intended to create these incentives or even understood them.

The remainder of this paper explores the answers to these three groups of questions in the case of the U.K.'s adoption of individual filing and what it is likely to tell us about the consequences of a similar policy change in the U.S. Although there are clear instances where the adoption of individual filing by the U.S. would produce different results than it has in the U.K., the U.K.'s experience still provides some sense of what the U.S. can expect. The U.K.'s change in tax unit should help American policymakers evaluate the costs and benefits of following in its footsteps. Once we know what legal changes actually do, even in a different country, we can evaluate whether, on the whole, the policy is a success and one the U.S. ought to adopt.

PART II. THE TIME THAT WAS

The U.K. adopted the income tax in the midst of the nation's wars with revolutionary France.²⁸ It did so in order to finance the fight. Because the tax was intended to raise revenue, at a time when tax administration was rudimentary, administration was a significant concern; what the tax's impact on wives would be was not. This tax, enacted in 1798, adopted the mandatory joint return so that husbands were required to file tax returns reporting not only their income but also that of their wives.²⁹ This would increase the tax burdens of couples in which the wife had a significant amount of her own property compared to if she were allowed to report and pay tax on her income separately. Although Parliament did enact some changes that granted wives' minimal rights and privileges within the tax system, through the first century of the tax's operation the income tax all but ignored the existence of British wives.

A. HISTORY OF THE TAX

Before 1688, tax revenue in England normally ranged from a scant 1.3 to 4.4% of national income.³⁰ As a result, there was little need for the government to resort to the politically-unpopular sale of offices, the granting of tax exemptions, or the use of tax farms to raise revenue as was prevalent in continental Europe. Most certainly the English did not need to invent new taxes. Even as the demand for revenue rose, the normal level of taxation remained between 8 and 10% of national income throughout the eighteenth century.³¹ Sufficient revenue could be raised by excise and import taxes until the nation experienced massive new revenue demands during the Napoleonic Wars. Taxes spiked to 23% of national income by 1810.

²⁸ For good descriptions of the early British income tax, see A. HOPE-JONES, *INCOME TAX IN THE NAPOLEONIC WARS* (1939); MARTIN DAUNTON, *TRUSTING LEVIATHAN, THE POLITICS OF TAXATION IN BRITAIN, 1799-1914*, AT 32-57 (2001); B.E.V. SABINE, *A HISTORY OF INCOME TAX* (1966); Meade Emory, *The Early English Income Tax: A Heritage for the Contemporary*, 9 AM. J. LEGAL HIST. 286 (1965).

²⁹ U.K. Act of 1799, 39 Geo. 3, c. 13 (repealed). For example, husbands had to be part of suits against wives, so in order to sue to collect taxes against a wife, the government would have had to sue her husband.

³⁰ MARTIN DAUNTON, *TRUSTING LEVIATHAN, THE POLITICS OF TAXATION IN BRITAIN, 1799-1914*, at 5 (2001).

³¹ DAUNTON, *TRUSTING LEVIATHAN*, *supra* note *, at 5, 22.

Revenue demands then fell back to around 8% by 1815 at war's end.³² These fluctuating demands for government revenue put enormous strains on the capacity of the British government to expropriate sufficient funds, as government expenditures surged in periods of conflict when business and trade was depressed. Increasing taxes during these periods came with great difficulty and political danger. Much as would occur in the U.S. during the Civil War, this wartime need opened the door for an income tax.³³

By the end of the seventeenth century, the House of Commons had taken from the king his prerogative of economic regulation; and new political leaders, men like William Pitt, gained and held power on the ground of their financial acumen.³⁴ They were entrusted with the task of raising money even as war with France highlighted the incapacities of the British fiscal system.³⁵ There were many tax experiments during this period, some of which were found to hurt the affected industries. For example, a 1795 tax on hair powder only hastened the decline of the fashion as caricaturists seemed to have particular fun at its expense.³⁶ Among the numerous new taxes, in 1796 a tax on dogs was introduced and then one on clocks and watches – with rates different for gold and silver.³⁷ A 1785 tax on female servants lasted only six years and was “widely supposed to be due to Pitt’s aversion to the female sex.”³⁸ The primary direct tax of the period was a land tax that produced diminishing returns since land and other property had not been revalued over the preceding century.³⁹

In the face of national need, Pitt took a provocative step in 1797 by implementing the triple assessment for 1798, an early form of a graduated income tax.⁴⁰ Those who owed tax on coaches, carriages, male servants, dogs, clocks, or watches were to pay additional taxes if their incomes were above a threshold of £60.⁴¹ The additional taxes were never less than three times the amount of the existing rate.⁴² Taxpayers were given an assessment, that many evaded, and were also invited, if their incomes were above £200, to make additional voluntary contributions

³² DAUTON, TRUSTING LEVIATHAN, *supra* note *, at 22.

³³ For the U.S., see Stephanie Hunter McMahon, *A Law with a Life of its Own: The Development of the Federal Income Tax Statutes Through World War I*, Pittsburgh Tax Rev. (forthcoming); STEVEN A BANK, ET AL., WAR AND TAXES (2008); W. ELLIOTT BROWNLEE, FEDERAL TAXATION IN AMERICA: A SHORT HISTORY (2d ed., 2004); RICHARD J. JOSEPH, THE ORIGINS OF THE AMERICAN INCOME TAX: THE REVENUE ACT OF 1894 AND ITS AFTERMATH (2004); STEVEN R. WEISMAN, THE GREAT TAX WARS: LINCOLN TO WILSON – THE FIERCE BATTLES OVER MONEY AND POWER THAT TRANSFORMED THE NATION (2002); ROBERT STANLEY, DIMENSIONS OF LAW IN THE SERVICE OF ORDER: ORIGINS OF THE FEDERAL INCOME TAX, 1861-1913 (1993); JOHN F. WITTE, THE POLITICS AND DEVELOPMENT OF THE FEDERAL INCOME TAX (1985); D. BUENKER, THE INCOME TAX AND THE PROGRESSIVE ERA (1985).

³⁴ B.E.V. SABINE, A HISTORY OF INCOME TAX 14 (1966).

³⁵ Three percent consols, which had been around par in 1792 and fluctuated around 70 during the next three years, fell to 55 in January 1797 and 47 3/8 before the end of May. The Bank of England suspended species payments. Investors were losing faith in their economy. EWIN R. A. SELIGMAN, THE INCOME TAX 62 (1911).

³⁶ SABINE, *supra* note *, at 20.

³⁷ SABINE, *supra* note *, at 20.

³⁸ SABINE, *supra* note *, at 20.

³⁹ DAUTON, TRUSTING LEVIATHAN, *supra* note *, at 33; ARTHUR HOPE-JONES, INCOME TAX IN THE NAPOLEONIC WARS 10-11 (1939).

⁴⁰ DAUTON, TRUSTING LEVIATHAN, *supra* note *, at 44; HOPE-JONES, *supra* note *, at 14-15; MEADE EMORY, “THE EARLY ENGLISH INCOME TAX,” 9 AM. J. LEGAL HIS. 286, 292-5 (1965).

⁴¹ DICTIONARY OF POLITICAL ECONOMY 3:582, edited by R.H. Inglis Palgrave (1901).

⁴² *Id.*

to ensure that they paid 10% of their income to the government. As voluntary contributions could not be permanently depended upon, Pitt was soon forced to propose a new tax levied directly on income.⁴³ So, on December 8, 1798, Pitt introduced the income tax in his annual budget. It aroused significant opposition but Pitt was able to push the tax through Parliament.

One reason for his success was the relatively closed system of British tax policy. The British revenue system is framed with much less interest-group influence than in the U.S. In the U.K., there remained an emphasis on secrecy in policy development, with Parliament voting the government's proposals up or down.⁴⁴ [DEVELOP]

A significant concern for those drafting this income tax was how to minimize its avoidance.⁴⁵ They recognized that there would always be some avoidance and evasion, but they sought to contain the limits of abuse.⁴⁶ Pitt, a Tory, concluded the need for precise statutory language that would remove all opportunity for abuse. He argued that:

persons, who probably would have shrunk from a direct fraud, have been able by different pretenses to disguise the fair and adequate proportion which they ought to have contributed, [so] it becomes more than ever necessary to render every case of exemption precise, and to guard every title to deduction from the danger of being abused.⁴⁷

In Parliament, some members objected that to draw too fine a line around the tax would create inequity. For example, Sir John Sinclair, a Scottish Whig, complained, "For my part, I think it infinitely preferable that we should lose some money, than run the risk of establishing principles abhorrent to that free constitution which this country has hitherto boasted of."⁴⁸ Mr. George Tierney, a prominent Whig opponent of Pitt's, agreed, "[I]t was a common saying, that tricks which were fair in love, were also fair in taxation; that was, that every advantage which could, might be taken."⁴⁹ Despite these concerns, the bill and its emphasis on precise legislative drafting passed handily.⁵⁰ Later, as shown in Part IV of this paper, the adherence to strict construction can also work in taxpayers' favor.

This original income tax was a comprehensive bill of 124 sections, covering 152 pages in the statute books.⁵¹ It imposed taxation on a person's entire income, whether a resident of Britain or non-resident merely with property in the isles.⁵² The person was not every individual,

⁴³ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 4-5.

⁴⁴ This form of policy development regarding taxation remains. See David W. Williams, *Taxing Statutes are Taxing Statutes*, 41 MODERN L. REV. 404 (1978).

⁴⁵ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 1152. See also SABINE, *supra* note *, at 22-32.

⁴⁶ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 5.

⁴⁷ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 7.

⁴⁸ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 84.

⁴⁹ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 132.

⁵⁰ THE PARLIAMENTARY HISTORY OF ENGLAND, vol. 34 (1819), at col. 148.

⁵¹ The tax imposed an income tax at the rate of 2s in the £ on individuals with total incomes over £200. As with the triple assessment, abatements were provided for incomes between £60 and £200. There was no tax imposed on incomes under £60. See note * above.

⁵² For all of its comprehensiveness and purported intrusiveness, however, the tax law left each individual to interpret the rules and estimate his or her own income. The exigencies of the period helped inspire compliance.

however, but every non-married person and every husband. The income tax as enacted in 1799 treated unmarried individuals and married couples as equivalent tax units:

That the income of any married woman, living with her husband, shall be treated and accounted for by her husband at the time of delivering his own statement under this act; provided that the Commissioners shall be at liberty to summon the wife, and examine her touching her separate property, under such rules and regulations as any party may by this act be examined.⁵³

Because the income tax was intended to raise revenue at time when public administration was rudimentary, the mandatory joint return was a natural choice of tax units if only because it “afforded a convenient means of collecting the tax, more especially as the husband was a necessary party to any suit against his wife at common law.”⁵⁴ An alternative approach to the tax unit was adopted across the channel, in Germany and France. However, their unit was not the individual. Instead, their taxable unit was the family, including the income of children unless a child’s income was not at the disposal of the father.⁵⁵

At the time of the tax’s enactment, coverture denied British wives legal recognition as separate individuals from their husbands for most legal purposes.⁵⁶ From the early thirteenth century until 1882, English common law held that most of the property a wife owned as *feme sole* came under the control of her husband at the time of their marriage.⁵⁷ A wife’s personal property vested in her husband absolutely. While this was the general law of coverture, it did not apply in practice that way to women of the wealthiest families or, as recent studies have shown, necessarily to any group of women. Women along the income spectrum found means to preserve wives’ separate property, owning and, more importantly, controlling that property.⁵⁸ Emily Erickson has found that at least 10% of non-elite married women had protected some separate property.⁵⁹ Once separate, for example if held in trust, a wife’s property could not be reached by her husband or by her husband’s creditors. Coverture was, therefore, more likely a system for regulating the state vis-à-vis the family than the expected condition within a family. In other words, outsiders, most notably the government, only had to deal with one member of the family even if within the family there were multiple decision-makers. The British income tax

⁵³ U.K. Act of 1799, 39 Geo. 3, c. 13, sec. 41 (repealed). But see reference to “actual receipt” as a requirement for tax in sec. 38, p. 70. COMPARE ACTUAL CHANGE IN 1806. “A woman’s income chargeable to income tax shall...(for any year) during which she is a married women living with her husband be deemed for income tax purposes to be his income and to be her income.” Sec. 37, Income and Corporation Taxes Act 1970, though the wording has been same in substance since 1806.

⁵⁴ Cmd. 9105, at 36.

⁵⁵ EDWIN R. A. SELIGMAN, THE INCOME TAX (252). Seligman concluded that this was the result of the nations’ divergent objectives for the income tax. For example, England wanted revenue, Germany wanted to end class struggle. *Id.*

⁵⁶ WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND: A FACSIMILE OF THE FIRST EDITION OF 1765-1769 1:43 (University of Chicago Press ed., 1979); J.H. BAKER, AN INTRODUCTION TO ENGLISH LEGAL HISTORY 552 (3d ed., 1990); Mary Beth Combs, “A Measure of Legal Independence”: The 1870 Married Women’s Property Act and the Portfolio Allocations of British Wives, 65 J. ECO. HIST. 1028-57 (2005).

⁵⁷ BAKER, AN INTRODUCTION TO ENGLISH LEGAL HISTORY, 3d Ed., 1990, p. 484-7.

⁵⁸ *Id.*; Joanne Bailey, *Favoured or Oppressed? Married Women, Property and “Coverture” in England, 1660-1800*, 17 Continuity and Change 351, 363-66 (2002); Margot Finn, *Women, Consumption and Coverture in England, c.1760-1860*, 39 HISTORICAL J. 703, 705-6 (1996); TIM STRETTON, WOMEN WAGING LAW IN ELIZABETHAN ENGLAND 26-27, 119-23 (1998).

⁵⁹ EMILY ERICKSON, WOMEN AND PROPERTY IN EARLY MODERN ENGLAND 150-1 (1993).

continued with the traditional coverture model, only requiring the Inland Revenue⁶⁰ to collect from husbands, even though husbands who paid significant income tax would likely have had wives with separate income beyond their reach but on which they had to pay tax.⁶¹

Mandatory joint filing, as existed under this early regime, played into the prevailing notions of marriage, even when the notions did not always accurately describe marital relations. Joint filing, technically the reporting by the husband of the couple's income, would have required disclosure of the wife's earnings to him, but it also required that he pay tax on income that he neither owned nor controlled. Moreover, while husbands were legally responsible for reporting all of the income, there was no means for legally compelling a wife to inform her husband of her sources of income.⁶² It is surprising that these wealthy men, likely some in the House of Lords, whose wives might well have had their own income in trust and out of reach, did not frame the tax so that it imposed the tax on each spouse as an individual. This would have decreased their tax burdens and eliminated the situation of being taxed on someone else's property. That they did not likely means either that (1) wives' trusts and other separate property meant little in practice, husbands still felt they owned their wives' separate property, or (2) it nonetheless seemed equitable to tax the couple on its combined income as if a sense of "coupleness" overrode separate economic interests.⁶³ Regardless of which view prevailed, the first modern income tax taxed couples as a unit.

This early experiment with an income tax did not remain long on the books. With the signing of a peace treaty in March 1802, a new Prime Minister, Henry Addington, abolished the income tax. Renewed warfare soon revived the tax.⁶⁴ This new Addington income tax was retained until 1816 when its repeal, one year after the Battle of Waterloo, was capped off with a bonfire of the income tax records.⁶⁵ The tax remained in relative disrepute, despite repeated efforts by a dedicated few for its reintroduction. Great Britain required several attempts before it was decided that the income tax's gains outweighed its costs. Prime Minister Sir Robert Peel was finally able to reinstate the tax in 1842, well before the U.S. enacted its first income tax in 1861.⁶⁶ This tax, with few significant changes from its forebears, remains in effect today. Even this income tax was seen as a temporary measure. It was not until after the return of Benjamin Disraeli as Prime Minister in 1874, when the income tax was somewhat surprisingly retained, that it was seen as a permanent revenue measure.⁶⁷ In each of these taxes, the system continued to use the mandatory joint return.

⁶⁰ Inland Revenue has since been reorganized as HM Revenue and Customs.

⁶¹ Cmd. 9105, at 36.

⁶² EOC, at 22.

⁶³ The latter position might also reflect the fact that tax rates were so low.

⁶⁴ A major different difference in the 1803 income tax was that it imposed the tax on a scheduler basis, as opposed to a unitary definition of income. A good description of these differences is available at HOPE-JONES, *supra* note *, at 20-1; SABINE, *supra* note *, at 33-8.

⁶⁵ SABINE, *supra* note *, at 46.

⁶⁶ SABINE, *supra* note *, at 60-62.

⁶⁷ SABINE, *supra* note *, at 109-11.

The income tax was first adopted in the U.S. during the Civil War as a minor revenue measure and was less developed than its British counterpart as a statutory regime.⁶⁸ It was not until World War I imposed massive demands on the U.S. federal budget and severely limited revenue from other sources, such as the tariff, that legislators began to appreciate the income tax's potential as a revenue-raising measure.⁶⁹ Although policymakers were aware that wealthy couples had used the family as a means of tax avoidance in the Civil War, how to prevent this tax avoidance as well as the relative tax treatments of husbands and wives and their single counterparts went unanalyzed when the tax was reintroduced, first in 1894 and again in 1913.⁷⁰ Cordell Hull (D-TN) contemplated requiring spouses to file jointly, but he ultimately concluded that married women's property acts would make such a law unconstitutional.⁷¹ As a result, in 1913, Congress adopted a system that on its face defaulted to treating the individual as the basic unit for measuring the amount of federal income taxes owed when it taxed the "net income of every individual."⁷² Although its meaning evolved over time, that language remained largely unchanged until the enactment of the Revenue Act of 1948.⁷³

While the U.S. fumbled for a policy on the taxable unit, the U.K. seemed committed to joint filing, if only because of its administrability. In the U.K., in each of the income tax's enactments, one of its greatest benefits in the minds of many Britons was that it reduced dependency on alternative revenue measures generally perceived as more burdensome: The alternatives being a host of direct and indirect taxes. Even with the era's demand for new taxes and a new tax base, the introduction of a major new tax was nonetheless a rarity. Inertia and the political cost of change normally prevent major reform in tax policy.⁷⁴ That inertia did not prevent the repeated enactment of an income tax in the U.K. That inertia did, however, prevent developments in the tax unit.

⁶⁸ Sec. 49, Act of 1861, at 309; sec. 91, Act of 1862, at 473-4. See McMahon, *A Law With a Life*, *supra* note * above.

⁶⁹ For a discussion of World War I financing, see W. Elliott Brownlee, *Wilson and Financing the Modern State: The Revenue Act of 1916*, 129 PROC. OF THE AM. PHIL. SOC'Y 173 (1985); W. Elliott Brownlee, *Social Investigation and Political Learning in the Financing of World War I*, in THE STATE AND SOCIAL INVESTIGATION IN BRITAIN AND THE UNITED STATES (Michael J. Lacey and Mary O. Furner, eds, 1993); JEROLD L. WALTMAN, POLITICAL ORIGINS OF THE U.S. INCOME TAX 32-82 (1985); CHARLES GILBERT, AMERICAN FINANCING OF WORLD WAR I 77-116 (1970).

⁷⁰ See, e.g., Henry Wilson (R-MA), CONG. GLOBE, 37th Cong., 2d Sess. 2515-16 (1864). The concern during the Civil War was income shifting to take advantage of high exemptions.

⁷¹ ROBERT H. MONTGOMERY, FEDERAL TAX HANDBOOK SUPPLEMENT, 1941-1942, § 1016 (1941). Hull likely meant to have husbands file families' returns, as they did in Wisconsin, see *Hoeper v. Wisconsin*, 284 U.S. 206 (1931). This would have required husbands to pay tax on income that their wives owned. This proposal was not widely debated.

⁷² Tariff of 1913, Pub. L. No. 63-16, § 2, 38 Stat. 114, 166 (1913). Except for a brief period, couples could choose to file jointly or separately as they desired. Although no specific guidance was issued, children could presumably file their own tax returns.

⁷³ See Stephanie Hunter McMahon, *To Have and To Hold: What Does Love (of Money) Have to Do With Joint Tax Filing?*

⁷⁴ R. ROSE AND T. KARRAN, TAXATION BY POLITICAL INERTIA: FINANCING THE GROWTH OF GOVERNMENT IN BRITAIN (London, 1986).

B. IMPACT OF THE WOMEN'S MOVEMENT

At the same time that the British income tax was proving that it could raise revenue, the women's movement began to win advances in the law.⁷⁵ Statutory changes were enacted that gave all wives the protections trusts had previously given the wealthy: The Married Woman's Property Acts of 1870 and 1882 gave wives the right to own and control most forms of personal property as well as rights to their earnings.⁷⁶ One scholar has seen these acts as the "greatest transfer of resources from married men to married women which has ever taken place."⁷⁷ As these legal changes were altering the ownership of property within families, husbands continued to be responsible for the tax due on their wives' income. Husbands did not, however, appear to be lobbying to change this system. In the nineteenth century, the principle of aggregation had "raised no issue of major importance."⁷⁸ Then, in the late nineteenth century, women made individual filing an important and recurrent feminist issue. Liberal chancellor and later Prime Minister David Lloyd George later called the question of the tax unit a "hardy perennial."⁷⁹

In 1894, the first concession to married women was granted: their own exemption or an "allowance" as they are called in the U.K.⁸⁰ Previously, Parliament had given some married couples an additional exemption, the Married Man's Allowance (MMA), if the wife engaged in paid employment (after World War I, the husband received the MMA whether or not his wife engaged in paid employment).⁸¹ This meant that husbands had larger exemptions than single taxpayers. In 1894, Parliament enacted a Wife's Earned Income Allowance (WEIA), a separate exemption that could be used to offset wives' wage income, although it was lower than the exemption given to a single taxpayer. This was in addition to the larger MMA. Parliament

⁷⁵ For a discussion of the movement, see JAN PAHL, *MONEY AND MARRIAGE* 19-22 (1989). One study argues that the improvements in wives' rights were the result of larger numbers entering the paid labor force. A. V. DICEY, *LECTURES ON THE RELATION BETWEEN LAW AND PUBLIC OPINION IN ENGLAND DURING THE NINETEENTH CENTURY* (1920), discussed in JAN PAHL, *MONEY AND MARRIAGE* 19- (1989).

⁷⁶ The Married Women's Property Act of 1870 made it possible for wives to hold limited types of property in their own right without marriage settlements. They could hold wages and earnings from employment and money invested in enumerated investments, including government stocks and funds, building and loan societies, and life assurance. They could also hold what they received by inheritance, but only inheritances under £200. The Married Women's Property Act of 1882 removed these restrictions. PAHL, *supra* note *, at 21-2. However, once the U.K. introduced the pay-as-you-earn withholding system in 1944, the tax would be taken directly from a wife's wages. While the legal changes did not increase wives' total wealth, it did affect their investment decisions. Looking at the portfolio allocations of wives following the 1870 Act, one study found that wives shifted their property away from real property to personal property because wives were able to own the latter separately. Mary Beth Combs, "A Measure of Legal Independence": *The 1870 Married Women's Property Act and the Portfolio Allocations of British Wives*, 65 J. ECO. HIST. 1028-57 (2005).

⁷⁷ PAHL, *supra* note *, at 22.

⁷⁸ Cmd. 9105, at 36.

⁷⁹ 1908 II, UK House of Commons Debates, Official reported, cited in Marshall and Wash, *Marital Status and Variations in Income Tax Burdens*, 4 BR. TAX REV. 236, 237 (1970).

⁸⁰ I will call British allowances throughout this paper, unless it is otherwise named, for the convenience of my American audience.

⁸¹ Colwyn Committee, Presented to Parliament by Command of His Majesty, Report of the Royal Commission on the Income Tax (1920), Cmd. 615, at 56-7; Cmd. 9105, at 39. The value of the married woman's allowance was raised to that of a single person in 1942 in order to induce women to enter the job market. EOC, at 7-8. In 1918, widowers were also given an allowance if they employed a female relative. That was extended to widows with children in 1920 and to those without children in 1924. EQUAL OPPORTUNITIES COMMISSION, *INCOME TAX AND SEX DISCRIMINATION* 8 (1979).

recognized that wives who entered the paid labor force incurred extra expenses as a result of working.⁸² Therefore, while a wife lost her personal exemption upon marriage, if she had earned income it was offset by the WEIA. However, any of the wife's earned income in excess of her special exemption was taxed jointly to the husband with other household income, and any of the wife's exemption not used against her earned income was forfeited.⁸³ The WEIA effectively reallocated the tax burden between earned and unearned income as a wife's unearned income could not be offset by the WEIA.⁸⁴

Then, in 1914, the option of separate filing was introduced which allowed wives to file their own, separate returns.⁸⁵ While this gave wives independence vis-à-vis their husbands, even when invoked spouses' incomes were combined and the tax due was calculated on the basis of the unit's total income.⁸⁶ The liability was then divided in proportion to each spouse's respective income. So this option allowed wives the independence of filing, but it did not allow them independence vis-à-vis the government; and couples' collective taxes, if in higher tax brackets and earned by both spouses, were not thereby reduced. This option was apparently not very widely known, and so was rarely used.⁸⁷

British women, unsatisfied with these modest gains, pressured the government to include consideration of individual taxation by a Royal Commission on the Income Tax convened in 1920. The Commission noted, "This contention has been urged upon us by many witnesses, and it forms the burden of the many letters we have received on this subject – mainly written by persons who would themselves benefit by the change proposed."⁸⁸ Recognizing that individual taxation would decrease the effective tax rates of wealthy couples because couples would shift income between spouses to maximize use of personal exemptions and lower rate brackets, the Commission did not find the public's urgings persuasive:

We feel that the demand of those who favour this change is in effect not so much a demand for separate assessment or separate recovery of tax – this they can have under the existing law – as for a diminution in Income Tax liability on the ground that part of the joint income happens to belong to the wife.⁸⁹

The Chancellor of Exchequer testified before the House of Commons that the loss in government revenue from individual filing would be £20,000,000, increasing possibly

⁸² Louise Dulude, *Taxation of the Spouses: A Comparison of Canadian, American, British, French and Swedish Law*, 23 OSGOOD HALL L.J. 67, 76 (1985).

⁸³ If a husband did not use all of the MMA, the remainder could be transferred and used to offset his wife's earned income.

⁸⁴ Oldman and Temple, "Comparative Analysis," at 589; Cmd. 615, at 56-7.

⁸⁵ Income and Corporation Taxes Act 1970, §38, first enacted in 1914. The tax was still calculated on the basis of the unit's total income and the liability was then divided in proportion to the size of their respective incomes. Cmd. 615, *supra* note 12, at 56-7.

⁸⁶ Colwyn Committee, Presented to Parliament by Command of His Majesty, Report of the Royal Commission on the Income Tax (London, 1920), Cmd. 615, at 56-7.

⁸⁷ *Id.*

⁸⁸ Cmd. 615., at 57.

⁸⁹ Cmd. 615, at 58. Some supporters of individual taxation also argued for increases the in wife and child exemptions that is premised on joint responsibilities of husband and wife. The Commission thought this further evidence that advocates were simply trying to shirk their tax obligations. *Id.*

to £45,000,000 if couples shifted their income in order to minimize taxation.⁹⁰ The desire to reduce tax burdens in this way flew in the face of the fact that, according to the Commission, families functioned as units. The Commission concluded that most couples treat their incomes as combined for purposes of expenditures, and so they should be taxed as such.⁹¹ Professor Lillian Knowles, the first female professor of Economic History, as the only woman on the Commission, issued a powerful dissent.⁹²

The progress that did occur in the tax treatment of wives was largely due to market demands, not feminist lobbying. In the 1940s, for example, driven by a need for labor, Parliament raised the WEIA twice, giving a married couple a much greater amount of exempted income than two single individuals with the same total income as long as the wife participated in the paid labor market.⁹³ This push for change stalled, however, once the war was over and the need for wives' labor subsided. Although in the war's aftermath both the Conservative and Labour parties accepted some degree of state intervention to secure the secular ideal of economic growth, the welfare state was fashioned around the idea of the nuclear family.⁹⁴ This imposed its burdens disproportionately on women as they were pushed out of the labor market. In this environment, further equalization in the tax system was not forthcoming.

With conservative social attitudes permeating British society, another Royal Commission convened in the early 1950s. As in 1920, this Commission received a large number of appeals to the effect that the "aggregation of the incomes of husband and wife ought to be abolished."⁹⁵ While more wives had entered the paid labor market, the Commission continued to focus on the family as a unit. "Marriage creates a social unit which is not truly analogous with other associations involving some measure of joint living expenses..."⁹⁶ Because of this relationship, aggregate taxation was thought to more accurately reflect a couple's relative wealth than taxing spouses separately.⁹⁷ The Commission refused to go as far as to conclude that couples shared a "joint purse," but there was a prevailing sense that any potential harm caused by aggregation was offset by the husband and wife's exemptions.⁹⁸

⁹⁰ Cmd. 615, at 58.

⁹¹ Cmd. 615, at 57-8.

⁹² Cmd. 615, at 59.

⁹³ Louise Dulude, *Taxation of the Spouses: A Comparison of Canadian, American, British, French and Swedish Law*, 23 OSGOOD HALL L. J. 67, 77 (1985).

⁹⁴ Miriam E. David, *Family Roles from Dawn to Dusk of the New Elizabethan Era*, in *REWRITING THE SEXUAL CONTRACT* 17, 19 (Geoff Dench ed., 1999).

⁹⁵ Royal Commission on the Taxation of Profits and Income, Second Report (1954), Cmd. 9105, at 36-7.

⁹⁶ Cmd. 9105, at 37.

⁹⁷ Nonetheless, even over published dissent, the Commission felt there were too many arguments in favor of the WEIA to reduce it because it recognized the added expense of a wife working. Cmd. 9105, at 40. The Commission did think the WEIA was too high because there was a larger exemption for a couple with two earners than for two single taxpayers, because this ignored the economies of scale when people live together. *Id.*, at 40-41. The Commissioner first thought to withhold the husband's net marriage allowance to reduce its value progressively in proportion to wife's tax-free earnings but "enquiry satisfied us that any such scheme for a graduated reduction of the marriage allowance is ruled out owing to its administrative complications." Cmd. 9105, at 41 (1954).

⁹⁸ Cmd. 9105, at 36. If a husband had income taxable at the basic tax rate and was married to a woman with investment income and their joint income was below the surtax rate level, their tax bill would only be higher if the wife's separate income was more than 90£, not an insignificant amount in 1954. If a wife's income was earned, their combined tax bill would only be higher if their joint income exceeded the princely sum of 2,215£. *Id.* Oliver

As in 1920, the Commission's prevailing concern was that moving to individual taxation would encourage tax avoidance. Joint taxation should be retained because, otherwise, "[t]here would be a natural tendency for husbands to try to arrange to transfer so much of their incomes to their wives as would produce an equal division," and therefore to minimize their collective taxes.⁹⁹ According to the Commission, this is what had occurred in the U.S. before Congress adopted the income-splitting joint return in 1948.¹⁰⁰ In the U.K., the alternatives that would be created by individual filing were a loss of approximately £143 million in government revenue or the introduction of special legislation to police inter-spousal transfers.¹⁰¹ Neither of these alternatives was acceptable to the Commission.¹⁰²

While the U.K. was resisting change, many other countries were re-evaluating their taxable units. Groups of Americans, in particular the National Woman's Party, would soon note that British women were protesting mandatory joint returns and began to voice a similar opinion.¹⁰³ On the other hand, the German Constitutional Court in 1957 held that joint taxation of married couples that imposed a higher tax on a married couple than if the couple had not married violated their Constitution which protected marriage and the family.¹⁰⁴ This led the German government to adopt income-splitting joint filing which gave married couples favorable treatment compared to their single counterparts. Similarly, while Canada had always had a system of individual taxation since its income tax was first introduced in 1917, both the Royal Commission on Taxation (the Carter Commission) and the Royal Commission on the Status of Women (the Bird Commission) unsuccessfully recommended the family as the tax unit.¹⁰⁵ The Carter Commission, in particular, was troubled by the amount of tax avoidance perpetrated under Canada's individual system, even though the law purportedly prevented transfers between spouses for tax avoidance purposes.¹⁰⁶

Oldman and Ralph Temple, *Comparative Analysis of the Taxation of Married Persons*, 12 STAN. L. REV. 585, 588 (1960).

⁹⁹ Cmd. 9105, at 37.

¹⁰⁰ Cmd. 9105, at 37.

¹⁰¹ Cmd. 9105, at 37. The Commission did not accept that high tax rates would prevent people from getting married. Cmd. 9105, at 36. They did question why aggregation was not extended to children. They split on the issue but ultimately concluded there was not enough evidence it was a big problem. Royal Commission on the Taxation of Profits and Income, Second Report, Cmd. 9105, at 40 (1954).

¹⁰² Cmd. 9105, at 37.

¹⁰³ *British Women Urging Reform on Parliament*, ATLANTA CONSTITUTION, Jan. 26, 1919, p. A10. *Urges Separate Taxation for Married Persons*, EQUAL RIGHTS, May 3, 1924, p. 90; *Wives and Income Taxes*, EQUAL RIGHTS, March 29, 1926, p. 42; *British Income Taxation Unequal*, EQUAL RIGHTS, June 5, 1926, p.130; *An Englishman's Wife's Income*, EQUAL RIGHTS, Jun. 9, 1928, p. 138; *British Women Phrase Demands*, EQUAL RIGHTS, May 25, 1929, p. 124-6; *Britain's Married Women Seek "Single" Tax Rating*, EQUAL RIGHTS, May 1942, p. 39.

¹⁰⁴ 6 BVerfGE 55, discussed in VICTOR THURONYI, *COMPARATIVE TAX LAW* 93 (Kluwer Law Int'l, 2003). Courts in Cyprus, Ireland, Italy, Korea, and Spain have also found joint taxation unconstitutional. *Id.*

¹⁰⁵ See CANADA, REPORT OF THE ROYAL COMMISSION ON TAXATION: TAXATION OF INCOME, vol. 3 (1966), at 12-15, 117-51; CANADA, REPORT OF THE ROYAL COMMISSION ON THE STATUS OF WOMEN (1970), at 291-307; Susan B. Boyd and Claire F. L. Young, *Feminism, Law, and Public Policy: Family Feuds and Taxing Times*, 42 OSGOODE HALL L. J. 545, 549-50 (2004); Harvey E. Brazer, *Report of the Royal Commissioner*, 22 J. OF FIN. 671, 674 (1967). Half of the federal Interdepartmental Committee on the Taxation of Women in 1975-1976 also wanted joint taxation. Dulude, *Taxation of the Spouses*, at 84.

¹⁰⁶ Dulude, *Taxation of the Spouses*, at 84. The Commission also concluded that the family was the "basic economic unit." *Id.*

Thus, countries, including the U.K. and the U.S., were debating the appropriate taxable unit, but that did not mean that change would quickly be legislated. It also did not mean that all countries would agree to the same answer to the question of the best taxable unit. Instead, the adoption of the individual as the tax unit, in the U.K. at least, would require progress within the European woman's movement and changing economic circumstances to provide an environment in which individual taxation could be pushed through Parliament. Until those events transpired, many felt the original system, one that saw the family as a unit, was most fair. Joint filing, and with it the higher taxation of some married couples, was recommended by the two British Royal commissions in 1920 and 1954 largely because it was believed that "their taxable capacity was greater than that of single persons."¹⁰⁷

PART III. THE HOW AND THE WHY OF CHANGE

By 1971, Parliament had given British wives a special exemption that would largely offset their own earned income but none of their unearned income. This exemption should have protected most wives' incentive to enter the paid labor force, if not to acquire investment property. Wives could also file separate tax returns, but doing so would not reduce families' collective tax burdens. Separate filing still used a tax rate calculated on a couple's collective income. Most women did not consider this enough of an advance.

In the 1970s and 1980s, the British system changed further. The individual was adopted as the tax unit, and, in doing so, Parliament reduced many couples' collective taxes. In 1972, Parliament enacted a law that allowed wives to separately report their earned income and for this separately reported income to be taxed as that of a single taxpayer. For couples in higher rate brackets and in which wives had earned income, this would mean a tax reduction. By the 1980s, however, the concern had shifted from the tax treatment of British wives to the tax treatment of single-earner married couples. In a socially conservative era, similar to that experienced in the U.S. in the 1980s, there was a desire to reduce this group's tax burden.¹⁰⁸ To accomplish that goal, the U.K., but not the U.S., adopted individual filing. Thereafter, one-earner couples could enjoy a tax reduction if husbands gave wives investment income; these couples could then separately report, and pay tax on, their income.

A. THE 1970S: THE BEGINNING OF THE END

In the late 1960s and early 1970s, the U.K. joined in a feminist revival that swept across Europe at the same time that the nation enjoyed a period of relatively rapid economic growth.¹⁰⁹

¹⁰⁷ Oldman and Temple, *Comparative Analysis*, at 589.

¹⁰⁸ See note * below. There were claims, discussed below, that Parliament was also concerned for wives' privacy and independence. Kay and King. No longer did people want those few wives who filed tax returns (remembering that 85% of taxpayers did not file returns) to be required to give their economic information to their husbands, because their husbands did not have to give their information to their wives. *Id.*

¹⁰⁹ Miriam E. David, *Family Roles from Dawn to Dusk of the New Elizabethan Era*, in *REWRITING THE SEXUAL CONTRACT* 17, 20 (Geoff Dench ed., 1999); Alexander Cairncross, *Economic Policy and Performance, 1964-1990*, in *THE ECONOMIC HISTORY OF BRITAIN SINCE 1700*, at 3:67, 67-70, 73-80 (Roderick Floud & Donald McCloskey, 2d ed., 1994).

In an earlier period of British feminism, there had developed a sustained critique of the nation's social policies, focusing on education, family planning, preschool childcare, employment opportunities, and equal pay.¹¹⁰ Now was added new demands for financial and legal independence.¹¹¹ There was a sense that the U.K. could afford to provide this to its wives. British demands were reinforced by the European Community.¹¹² The Council of European Communities issued three directives covering equal pay,¹¹³ equal access to employment, vocational training and promotion, and working conditions,¹¹⁴ and progressive implementation of equal treatment for men and women with respect to social security.¹¹⁵ By the 1970s, the E.C. also pushed for countries to adopt individual tax filing. "Equal treatment shall mean that there shall be no discrimination whatsoever on grounds of sex either directly or indirectly by reference in particular to marital or family status."¹¹⁶

Many countries heeded this call, as shown in the introduction to this paper.¹¹⁷ However, some countries had goals other than gender equality. For example, individual taxation was introduced in Sweden in 1971, coupled with the rapid expansion of subsidized child care. Sweden had the goal of incentivizing wives to supply more labor during a national labor shortage when government policy also resisted increased immigration.¹¹⁸ As a result of these changes, Sweden did witness rising labor participation by wives throughout the 1970s; however, it was largely in part-time jobs, and Sweden even experienced a flow of women from full-time to part-time work.¹¹⁹

Similar forces as in Sweden were at play in the U.K., in which advances in women's rights were made but there remained a reluctance to push the advances too far. A significant number of British women entered the paid labor market for the first time, but much of that increased presence was in part-time, insecure, and intermittent jobs.¹²⁰ The seemingly dramatic growth in public approval for women in the workforce remained, and remains today, tied to whether there were pre-school and school age children in the home.¹²¹ Thus, by the 1970s, the

¹¹⁰ David, *Family Roles*, 20.

¹¹¹ David, *Family Roles*, 20.

¹¹² *The EC Commission on Income Taxation and Equal Treatment for Men and Women*, 39 BULL. INT'L FISCAL DOCUMENTATION 262-5 (June 1985).

¹¹³ European Union Legislation, Council Directive 75/117/EEC, Official Journal L 45, 19/2/1975, p.19. Passed in United Kingdom in The Equal Pay Act of 1970.

¹¹⁴ European Union Legislation, Council Directive 76/207/EEC, Official Journal C 39, 14/2/1976, p. 40. Passed in United Kingdom in The Sex Discrimination Act of 1975.

¹¹⁵ European Union Legislation, Council Directive 70/7/EEC, Official Journal L 3, 10/1/1979, p. 24

¹¹⁶ EC Legislation, Council Directive 76/207/EEC, Official Journal C 39, 14/2/1976, at 40.

¹¹⁷ See p. 1.

¹¹⁸ This account of Sweden is derived from Siv Gustafsson, *Separate Taxation and Married Women's Labor Supply*, 5 J. POPUL. ECON. 61, 61-64 (1992); Anders Bjorklund, *Rising Female Labour Force Participation and the Distribution of Income: The Swedish Experience*, 34 ACTA SOCIOLOGICA 299 (1992).

¹¹⁹ Rachel A. Rosenfeld and Gunn Elisabeth Birkelund, *Women's Part-Time Work: A Cross-National Comparison*, 11 EUROPEAN SOCIOLOGICAL REV. 111, 114 (1995).

¹²⁰ Jonathan Gershuny, *Sexual Divisions and the Distribution of Work in the Household*, in REWRITING THE SEXUAL CONTRACT 141, 142 (Geoff Dench ed., 1999).

¹²¹ Gershuny, *Sexual Divisions*, 142. The British Social Attitudes surveys show that women should work before they have children and after the children leave home, but only 1 in 20 think they should work if she has a preschool child, and 1 in 5 if there are school-aged children. Stein Ringen ed., *Family Change and Family Policies: Great Britain*, in FAMILY CHANGE AND FAMILY POLICIES IN GREAT BRITAIN, CANADA, NEW ZEALAND, AND THE UNITED STATES 31,

public and government policies were sensitive to gender issues, but they were tempered by a reluctance to grant real independence to the country's wives.¹²² Politicians appeared to have a difficult time accepting women as equal participants in the labor market when crafting policy. As the postwar bipartisan collaboration was breaking down, the Labour party, which devoted more effort to securing stronger forms of equality than the Conservative Party, nonetheless found it difficult to unify on gender issues.¹²³

Nevertheless, early in the decade, British couples with two-earners, after having "kept up their lobbying," won a right for married women to be taxed as a single person on her labor income.¹²⁴ In 1971, two years before entry into the E.C., Parliament responded to domestic and European pressure and legislated that, if both spouses elected, a wife could file a separate income tax return reporting her separate wages. Wives could then have those wages taxed as a single person.¹²⁵ For some couples, there was an economic cost if a wife elected to file separately that might outweigh the psychological benefit of separate status.¹²⁶ This cost was publicized.¹²⁷ At the time, the MMA, at £600, was larger than the SPA, at £460.¹²⁸ For couples with two earners, the WEIA of £460 was added on top of this larger MMA.¹²⁹ If a couple opted to be taxed separately as two single persons, for example if the wife earned enough income to benefit from double-dipping into the lower tax brackets, the couple would lose the benefit of the difference between the MMA plus the WEIA and two SPAs, or £140 of exempted income. Moreover, all of a wife's unearned income still had to be reported by, and taxed to, her husband.

Shortly after the change of law, the U.K. entered the E.C. and, within the decade, the British economy plummeted. The Single European Act, signed by Margaret Thatcher, allowed the free movement of goods within the E.C. with the anticipated benefit of spurring competition within the local economy and increasing efficiency. However, the U.K. soon faced the declining economic conditions that were prevalent in much of Europe. While between 1969 and 1971, debts to the International Monetary Fund and other monetary authorities were reduced and reserves were increased, by 1972 the nation was again moving toward a deficit.¹³⁰ After a spate of major strikes, a state of emergency was declared and most of British industry was put on a three-day week.¹³¹ Government policies increased public expenditures and cut taxes to increase production.¹³² Nonetheless, between 1973 and 1982, there was little to no economic growth.¹³³

44 (Sheila B. Kamerman & Alfred J. Kahn, editors, 1997). Age is the most important predictor of these views, with those over 60 considerably more likely to think women should stay home. Ringen, *supra* note *, at 44.

¹²² "Thus the Equal Pay Act of 1970 introduced a weak concept of equal pay for equal work, and the Sex Discrimination Act of 1975 also took on board the notion of eliminating forms of sexual discrimination in employment and public services..." David, *Family Roles*, 21.

¹²³ Amy Black and Stephen Brooke, *The Labour Party, Women, and the Problem of Gender, 1951-1966*, 36 J. BRITISH STUDIES 419, 450 (1997); David, *Family Roles*, 20. Conservatives wanted weaker formulations of the definitions but, nonetheless, supported the legislation. David, at 21.

¹²⁴ Dulude, 77.

¹²⁵ Finance Act 1971, c. 68, §23 and schedule 4.

¹²⁶ John Jeffrey-Cook, *Separate Taxation of Wife's Earnings*, 6 BR. TAX REV. 439 (1980).

¹²⁷ *Id.*

¹²⁸ CENTRAL STATISTICAL OFFICE, ANNUAL ABSTRACTS OF STATISTICS 1972 329 (1972).

¹²⁹ *Id.*

¹³⁰ Cairncross, *Economic Policy*, at 3:68-71; 77-80.

¹³¹ *Id.*

¹³² *Id.*, at 79-80.

Inflation ravaged the country with retail prices rising at 27% per annum at its peak in 1975.¹³⁴ Unemployment mounted steadily until 1977 and, although there was a slight respite in unemployment from 1977 to 1979, it continued to rise until 1986.¹³⁵ By mid-1976, the U.K. had to obtain a \$5.3 billion short-term standby credit from European central banks, and repayment required assistance from the International Monetary Fund on terms that mandated cutting expenditures.¹³⁶ By the late 1970s, top tax rates were as high as 98% in order to pay off the loan and, as an unintended consequence, tax avoidance was rampant.¹³⁷

In the midst of this economic downturn, the Equal Opportunities Commission published a booklet entitled *Income Tax and Sex Discrimination*.¹³⁸ This independent, nondepartmental public body, established in 1975 to focus on gender inequality, complained in 1978 that the Inland Revenue did not advertise benefits, such as separate assessment, which would benefit wives.¹³⁹ The system, deeming a wife's income to be her husband's, was regarded, at best, as humiliating, and, at worst, as discriminatory.¹⁴⁰ Using excerpts from letters, the Commission illustrated the discrimination that women were facing. One of the recurring complaints from married women was that the Inland Revenue "persists in treating them as if they do not exist."¹⁴¹ The anger was less the economics of joint filing than the mechanics – wives would often receive letters from the Inland Revenue about their jobs requesting their husbands send in corrected forms. The publication produced a deluge of more than 2,000 letters, 730 of them specifically demanding that the tax system treat married women as separate individuals.¹⁴²

While the Commission promoted individual taxation, it also recognized that couples might use that system to reduce their taxes by "dividing their *unearned* income between them."¹⁴³ Because this could be very costly to the Inland Revenue, the Commission concluded that the income tax should continue to aggregate a married couple's unearned income for the determination of the applicable tax rates, but the amount of tax due should be apportioned and individual assessments issued.¹⁴⁴ The goal was to grant wives independence while preventing tax avoidance.

¹³³ *Id.*, at 70-72, 83-84.

¹³⁴ Larry Neal, *Impact of Europe*, in *THE CAMBRIDGE ECONOMIC HISTORY OF MODERN BRITAIN*, vol. 3, edited by Roderick Floud and Paul Johnson, 267, 286 (2004).

¹³⁵ Cairncross, *Economic Policy*, at 67-72.

¹³⁶ *Id.*, at 83-4.

¹³⁷ Caroline Granham, *Finance and the Family: The Pitfalls in Tax Planning – Care is Needed if You are to Avoid Breaching the Revenue's Rules*, *FINANCIAL TIMES*, Oct. 9, 1993.

¹³⁸ EQUAL OPPORTUNITIES COMMISSION, *INCOME TAX AND SEX DISCRIMINATION* (1979). Private groups were also interested in the issue of family taxation. A committee chaired by Professor J. E. Meade for the Institute for Fiscal Studies explored, and rejected, the idea of individual taxation. While it wanted individual allowances (with a special allowance for women who stayed at home), "[b]ut to treat the individual as the tax unit would lead either to different tax treatments of families with similar total investment income or else to property arrangements between spouses planned in such a way to avoid taxation." IFS, *THE STRUCTURE AND REFORM OF DIRECT TAXATION* 382-84 (1978).

¹³⁹ EOC, 3.

¹⁴⁰ EOC, 4.

¹⁴¹ EOC, 7. For example, the general rule was to address correspondence to the husband and to send rebates and bills to him, since he was legally liable for tax on both spouses' incomes. *Id.*, at 19-20.

¹⁴² Dulude, *supra* note 12, at 78.

¹⁴³ EQUAL OPPORTUNITIES COMMISSION, *INCOME TAX AND SEX DISCRIMINATION* 29 (1979).

¹⁴⁴ EQUAL OPPORTUNITIES COMMISSION, 29-30.

At the same time, in response to attacks from single taxpayers on the higher MMA, the Commission concluded that a married man “should not be penalized where his wife is at home caring for children or other dependants.”¹⁴⁵ Of course the higher MMA benefits all married couples over single taxpayers unless spouses chose to file separately. As a result, the Commission urged the retention of the higher MMA. The Commission understood that few couples had two earners with each earning sufficient wages to cause them to file separately, so most couples would have been hurt by reduction of the MMA. For example, in 1975, in couples where wives did work for wages, their income on average made up only 20.4% of the family’s total income. If they filed separately, only this portion of a couple’s income would enjoy double dipping in the wife’s low tax brackets. Thus, the Commission’s proposal, far from extreme, was to provide as much tax savings as possible for everyone.

In response to the reaction to the Equal Opportunities Commission, the government commissioned a *Green Paper on the Taxation of Husband and Wife*, released in 1980, the beginning of a decade that would focus on cutting tax rates.¹⁴⁶ A green paper is a tentative, open-ended government report, and this one suggested either of two courses of action: Either allow spouses to choose between traditional joint taxation and individual taxation or change to a Canadian-style mandatory individual system. Of thirty-seven organizations that responded to the 1980 Green Paper, four favored retaining joint returns, thirteen supported transferrable exemptions, and twenty used the opportunity to advocate giving additional financial assistance to families with children.¹⁴⁷ Other than publishing this paper, the government took no other action. Couples could choose to file separate returns, each reporting their earned income, with the cost of losing the MMA, but the husband remained prima facie responsible for filing income tax returns for the married couple.¹⁴⁸

While husbands remained primarily liable for couples’ taxes, there were four different possibilities for how the tax system would economically impact married couples after 1972.¹⁴⁹ First, if one person had earned income and the other had no income, the couple would be better off married. For them, aggregation would be irrelevant but they would receive a MMA if the income was earned by the husband and, if it was earned by the wife, they would also receive a WEIA. Second, if a man and woman each had income that collectively would be taxed in the lower tax bracket and the woman’s income was earned, the couple would be better off married. For them, aggregation would not push the couple into higher rate brackets. They would be entitled to the larger MMA and the wife’s loss of the SPA would be exactly counterbalanced by the WEIA. Third, if their incomes would push them collectively into higher rate brackets and the woman’s income was earned, the couple would be in exactly the same position as two single taxpayers because the spouses would opt for separate taxation. Finally, if the woman had investment income and either no earned income or less earned income than her exemption, the couple would be subject to extra tax when married because they would lose the woman’s SPA to

¹⁴⁵ EQUAL OPPORTUNITIES COMMISSION, 33. The withdrawal of the MMA (£1,455), and its replacement by the single person’s allowance at £945, would increase government revenue by approximately £2,200 million per year. *Id.*, at 34. A husband would lose £3.33 per week out of his pay, or £510 in total annual allowance. *Id.* at 34. EQUAL OPPORTUNITIES COMMISSION, 45.

¹⁴⁶ *The Taxation of Husband and Wife* (1980), Cmnd. 8093.

¹⁴⁷ PAHL, *supra* note *, at 163-4.

¹⁴⁸ Roger Kerridge, *Taxation and Marriage*, 47 CAMBRIDGE L. J. 77, 79 (1988).

¹⁴⁹ Kerridge, 80-81.

offset the unearned income. This later scenario would be the only time where a couple was worse off economically with marriage. “In reality, the vast majority of couples are better off—in terms of income tax—married than single.”¹⁵⁰

[discuss US changes / conclusion]

B. THE 1980S: THE TIME IS NOW

As the equal treatment of women slowly gained popular acceptance in the U.K., the public bureaucracies overseeing the enforcement of the laws mandating that equal treatment were steadily losing popular support. When Margaret Thatcher came to power as Prime Minister in 1979, she did so “on a wave of criticism of such public bureaucracies.”¹⁵¹ Thatcher, like her American counterpart, President Ronald Reagan, prioritized the reduction of the role of the state in the economy and re-focused attention on individual rights.¹⁵² The new direction included reducing marginal tax rates and increasing exemptions, and thereby taking many people off of the income tax roles.¹⁵³ The Thatcher administration’s hands-off approach to the economy and social development facilitated, and necessitated, tax cuts. They were part of a radical change from the post-World War II acceptance of government regulation. The new vision of the income tax was less redistributive and sought to stimulate the economy. For a period, the tax cuts accomplished their objective; during Thatcher’s tenure, there was a gradual economic recovery and a boom in 1987 and 1988 that peaked in 1990.¹⁵⁴

¹⁵⁰ Kerridge, 81.

¹⁵¹ David, *Family Roles*, 21.

¹⁵² For example, between 1979 and 1990, the Thatcher administration raised approximately £33 billion for the government through the privatization of public businesses. Leslie Hannah, *the Economic Consequences of the State Ownership of Industry, 1945-1990*, in *THE ECONOMIC HISTORY OF BRITAIN SINCE 1700*, at 3:168, 182 (Roderick Floud & Donald McCloskey, 2d ed., 1994). “The United Kingdom tax system as it is in 1998 reflects the values of the recent age of extreme individualism.” John Tiley, *United Kingdom*, in *FAMILY TAXATION IN EUROPE* 129, 131 (Maria Roch ed., 1999); Paul Gilbert, *Family Values and the Nation-State*, in *CHANGING FAMILY VALUES*, edited by G. Jagger and C. Wright, 136, 138 (1999).

¹⁵³ OECD, *TAXATION, EMPLOYMENT, AND UNEMPLOYMENT* 45, 63-4. Tax rates rose steadily until 1973 and 1979 when rates halted with coming of Maggie, a policy continued under Blair. Victoria Curzon Price, “The British Tax System: Opposing Trends,” http://www.irefeurope.org/col_docs/doc_9_fr.pdf, at 8. Reduction in income taxes “tilted toward the high end of the income distribution.” Gale, *What Can*, 345.

Personal income tax rates, %		
	Basic rate	Upper marginal
1973-1974	30-35	75-83
1979-1980	25-30	60
1983-1984	30	60
1988-1989	25	60
1989-1990	25	40
1993-1999	20	40
2002-2003	20	40

Inland revenue, www.inlandrevenue.gov.uk.

¹⁵⁴ Alexander Cairncross, *Economic Policy and Performance, 1964-1990*, in *THE ECONOMIC HISTORY OF BRITAIN SINCE 1700*, at 3:72-73 (Roderick Floud & Donald McCloskey, 2d ed., 1994).

In the early Thatcher era, the tax treatment of wives continued to gain significant attention as part of the tax-cutting movement.¹⁵⁵ Most responses to the 1980 Green Paper favored individual taxation; they demonstrated a widespread dissatisfaction with joint filing that was thought to deny women independence and privacy in tax matters and to impose a tax penalty on marriage.¹⁵⁶ On the heels of the publicity from the green paper, a widely read survey circulated decrying the extent of sharing (or, more accurately, the lack of sharing) within marriage. Professor Jan Pahl concluded that “there is a considerable amount of evidence to suggest that such sharing of income cannot be taken for granted.”¹⁵⁷ Pahl found three standard patterns of money management, but in each case wives came out the loser—in control, discretion, and freedom.¹⁵⁸

Nonetheless, British proponents of individual tax filing could not win sufficient parliamentary support for change, in part because they could not agree as to how an individual-based system should operate.¹⁵⁹ In particular, they fought over how to reconcile the old exemption system with individual taxation. While many advocated transferable exemptions, so that if a wife had no income of her own her exemption could be used to offset her husband’s income, others worried that this would dampen wives’ incentive to work. Critics argued that if a wife returned to work after a period of working at home, she would have to choose between leaving her exemption with her husband, so paying more tax herself, or taking back her exemption and increasing the tax imposed on her husband.¹⁶⁰ The Institute of Fiscal Studies calculated that as many as 3.5% of wives engaged in paid employment at the time, or 200,000, would leave the labor force if they were given an exemption that they could transfer to their husband.¹⁶¹ It was on that basis that the House of Lords Committee argued against transferrable exemptions.¹⁶²

While trapped in internal debates over the operation of individual filing, the U.K. continued to face pressure from the E.C. to change its taxable unit. The E.C.’s push for greater equality between the sexes and favorable taxation for women was, however, primarily concerned

¹⁵⁵ See PAMELA ABBOTT AND CLAIRE WALLACE, *THE FAMILY AND THE NEW RIGHT* 22-30 (1992); Tony Fitzgerald, *The New Right and the Family*, in *SOCIAL POLICY AND SOCIAL WELFARE: A READER*, edited by Martin Loney, David Boswell, and John Clarke 46 (1983); Lorraine Fox Harding, “*Family Values*” and *Conservative Government Policy: 1979-1997*, in *CHANGING FAMILY VALUES*, edited by G. Jagger and C. Wright, 119, 124 (1999).

¹⁵⁶ Chancellor of the Exchequer, Forward, Green Paper, *The Reform of Personal Taxation*, Cmnd 9756, March 1986; Dulude, 78.

¹⁵⁷ Jan Pahl, *Patterns of Money Management within Marriage*, 9 *J. SOC. POL.* 313, 314 (1980). Pahl published a book on the topic in 1989, *JAN PAHL, MONEY AND MARRIAGE* (1989). Pahl has updated her studies in Jan Paul, *His Money, Her Money: Recent Research on Financial Organization in Marriage*, 16 *J. ECON. PSYCHOLOGY* 361 (1995) (only one-fifth of couples pool marital income and manage it jointly).

¹⁵⁸ First was a whole wage system in which husbands would hand over their salaries to their wives who would manage their financial affairs. Second, an allowance system in which husbands gave wives an allowance in some community norm amount. Third, a pooling system where both were working, but this might only mean that husbands kept more of their earnings for their personal use. Fourth, an individual control system where each spouse controlled the income that they earned, but this system was quite rare.

¹⁵⁹ Dulude, *supra* note *, at 78-9.

¹⁶⁰ PAHL, *supra* note *, 164.

¹⁶¹ PAHL, *supra* note *, 164.

¹⁶² PAHL, *supra* note *, 165. The original plan of transferrable tax exemptions under which a non-earning spouse could transfer his or her exemption to the earning spouse was revived in the Conservative Party’s 1997 Election Manifesto and advocated by Pam Meadows, head of Policy Studies Institute. Lister, *supra* note *, at 189 n. 11.

with women's right to engage in paid labor. The E.C.'s objective was to have countries "correct[] the effects of fiscal legislation on equal treatment in working life, particularly in so far as existing systems in Member States might be the cause of indirect discrimination against women."¹⁶³ A survey undertaken in ten member states of the E.C. asked for confirmation of the following: "Some people say that the way income tax works in your country makes it, in certain families, hardly worthwhile for the wife to work because too much of what she earns is taken away in tax from her or her husband's salary."¹⁶⁴ The highest percentages of agreement were found in countries with joint taxation.¹⁶⁵ In the U.K., 21% of married women thought that income taxes might be discouraging married women from working.¹⁶⁶ The European perception was that taxation was a major deterrent to wives entering the paid labor force.

This renewed concern might have helped women but for changing economic circumstances and a backlash of social conservatism. During the 1980s, the gender pattern of employment changed as businesses sought a more flexible labor market. This benefited women and disadvantaged men, destabilizing traditional labor arrangements.¹⁶⁷ This was not always beneficial to society as a whole. Because of the changed labor patterns and significant, static levels of unemployment, the period was marred by poverty, homelessness, and social discontent. There was significant rioting in inner-city districts, such as in Handsworth, Brixton, Tottenham, Toxteth, and Liverpool in 1981.¹⁶⁸ There was a major Miners' Strike in 1984.¹⁶⁹ The 1980s was a period of tremendous wealth polarization in both the U.K. and the U.S. causing social divisions and strife.¹⁷⁰

As in the U.S., which faced similar pressures from de-industrialization, the troubled working class in the U.K. embraced family values to fend off fear of unrest.¹⁷¹ Many of society's main concerns were "stable marriage and childrearing, a gender division of roles, the

¹⁶³ Action 6, COM(81) 758 final, 9/2/1971, at 18-19. While it did not expressly call for individual taxation, this was its goal. *Id.* at 19. *See also* Office Journal C 50, 3/9/1981, at 35; European Union, Council Resolution of 12 July 1982 on the promotion of equal opportunities for women, Office Journal C 186, 21/07/1982, at 3; Memorandum on Income Taxation and Equal Treatment for Men and Women, COM (84) 695 final. The OECD was likewise active in this area, calling for multi-faceted policy on the role of women in the paid economy, including individual taxation. OECD, *THE INTEGRATION OF WOMEN IN THE ECONOMY* 137-41, 153-59 (1985). Lots of other groups focused on this issue as well: International Labour Organization, the Council of Europe, European Trade Union Confederation, European Youth Forum, Confederation of Family Organizations in the European Community, etc. Bulletin of the European Communities, Supplement 3/86, "Equal Opportunities for Women," COM(85) 801, at 6.

¹⁶⁴ COMMISSION OF THE EUROPEAN COMMUNITIES, *EUROPEAN WOMEN IN PAID EMPLOYMENT 1984* (V/1240/84-FR), at 18.

¹⁶⁵ Namely in Ireland, Luxembourg, and Belgium. *EUROPEAN WOMEN IN PAID EMPLOYMENT*, *supra* note *, at 19.

¹⁶⁶ Namely in Ireland, Luxembourg, and Belgium. *European Women in Paid Employment*, *supra* note *, at 19.

¹⁶⁷ Ros Coward, *Was Feminism Wrong about the Family*, in *REWRITING THE SEXUAL CONTRACT* 64, 65-67 (Geoff Dench ed., 1999).

¹⁶⁸ *Victims of Thatcherism*, 20 *ECO. AND POL. WEEKLY* 1717 (1985); Clive Unsworth, *The Riots of 1981: Popular Violence and the Politics of Law and Order*, 9 *J. OF LAW AND SOC'Y* 63 (1982).

¹⁶⁹ Sheila Rowbotham and Jean McCrindle, *More Than Just a Memory: Some Political Implications of Women's Involvement in the Miners' Strike, 1984-85*, 23 *Fem. Rev.* 109 (1986); Peter Ingram, David Metcalf, and Jonathan Wadsworth, *Strike Incidence in British Manufacturing in the 1980s*, 46 *Industrial and Labor Relations Rev.* 704 (1993).

¹⁷⁰ OECD, *TAXATION, EMPLOYMENT, AND UNEMPLOYMENT* 46 (1995).

¹⁷¹ Lorraine Fox Harding, "Family Values" and Conservative Government Policy: 1979-1997, in *CHANGING FAMILY VALUES*, edited by G. Jagger and C. Wright, 119 (1999); Paul Gilbert, *Family Values and the Nation-State*, in *CHANGING FAMILY VALUES*, edited by G. Jagger and C. Wright, 136 (1999).

confinement of sexuality to the permanent married heterosexual couple, and the support of these patterns through government policy.”¹⁷² By the end of Thatcher’s first administration in 1983, a Cabinet Family Policy Group was formulating policies that would further these goals, plus there were numerous groups pushing similar goals operating outside of the government.¹⁷³ This countered the earlier ideological push to increase working wives’ rights.

In 1985, in the midst of economic growth for some and economic and social turmoil for others, the government commissioned a second green paper on the topic of individual taxation. Explaining that the “Government regard it as of major importance to reduce the burden of the income tax,” to maximize taxpayer’s “freedom of choice,” to give “incentives to effort and enterprise,” the paper proposed individual filing and transferrable exemptions.¹⁷⁴ This 1985 Green Paper recognized that this would create relative winners and losers. “Any major structural reform of income tax is bound to shift the relative burden of tax between individuals. But if that is considered unacceptable, then no tax reform would ever be possible.”¹⁷⁵

Unlike today’s American advocates of individual filing, the British government’s focus was not on easing the tax burdens of two-earner couples.¹⁷⁶ For example, the 1985 Green Paper pointed out that about 400,000 married couples paid more in tax than two single taxpayers because the WEIA could not offset a wife’s *unearned* income.¹⁷⁷ At the same time, the Commission drafting the green paper complained, *two-earner couples* had lower tax obligations than single taxpayers.¹⁷⁸ Focusing on life cycles, the Commission concluded that it was natural that a family would sometimes have one earner and, at others, two. In its opinion, the joint filing system needed to be changed because it disadvantaged couples when they were likely to have only one earner, such as when they had young children. “Couples have high tax allowances (2 ½ times the single allowance) when both are in paid work, but see a sharp reduction (to 1 ½ times the single allowance) if the wife leaves paid work. This is likely to be the time when the couple are under greatest financial pressure...”¹⁷⁹ When the government had increased the WEIA, it had needed to induce wives to enter the labor market, the Commission explained, but in 1985 the rule was that women earn wages, and so “the system needs to be changed to remove the discrimination against couples where only the husband is in paid employment.”¹⁸⁰

¹⁷² Harding, *supra* note *, at 119.

¹⁷³ *Id.*, at 120.

¹⁷⁴ Chancellor of the Exchequer, *The Reform of Personal Taxation*, Cmnd 9756, March 1986, at 1. The government sought to allow all allowances be transferred between spouses in order “to recognize the shared responsibility of a married couple.” Cmnd 9756, at 12.

¹⁷⁵ Cmnd 9756, at 1 (emphasis in original).

¹⁷⁶ *See* note * above.

¹⁷⁷ Cmnd 9756, at 4.

¹⁷⁸ Cmnd 9756, at 5.

¹⁷⁹ Cmnd 9756, at 5. There were, however, no limitations proposed to ensure that favorable treatment would only help couples when they had young children or other care-giving responsibilities.

¹⁸⁰ Cmnd 9756, at 8. Over 60% women under 60 work and the “vast majority” of men. *Id.*, at 26. The structure of the basic personal allowances remained basically unchanged since 1942. Married men’s exemption was approximately 1 ½ times that of a single person. A wife’s earned income exemption was equal to that of a single person but could only be set against her earned income. As a result, a two-earner couple had approximately 2 ½ times the exemption of a single person. On the other hand, if the husband was the only earner, the couple had approximately 1 ½ times the single’s exemption but if the wife was the only earner, the couple retained the 2 ½ times exemption.

Thus, although the government also claimed to want to give wives privacy and independence in their tax matters, it was more focused on targeting tax reduction in a cost effective way.¹⁸¹ The targeted group was one-earner couples, and wealthy couples at that. This was unsurprising to some who thought that “Thatcherism was centrally concerned with sexual counter-revolution and/or the restoration of the patriarchy.”¹⁸² This formula of tax cuts would not reduce the tax burden of low-income taxpayers who had no income to shift between spouses and wives already had a WEIA equal to a SPA to exempt a portion of their wages. The only possible reduction in taxes for these low-income couples would derive from the transferability of the wife’s SPA in single-earner families, and this ultimately failed to win parliamentary support.¹⁸³ Individual taxation allowed the Conservative government to reinforce the traditional family for wealthy couples by cutting taxes and did so without growing the size of the government itself, pleasing both sides of the party.

While the 1986 Green Paper strongly supported individual filing, it did recognize that with individual filing many couples would have an incentive to rearrange their affairs to reduce their collective income taxes. It concluded, however, that “[i]t is very unlikely that all couples would seek to rearrange the ownership of their income-bearing assets in order to take maximum advantage of separate tax rate bands. Many would not be able, or would not want to, make the necessary transfer of assets.”¹⁸⁴ It was estimated that if couples did take advantage of income shifting, it would cost the government £100 million.¹⁸⁵ Consideration of whether Parliament would need to take steps to prevent this tax avoidance was purposefully deferred.¹⁸⁶

The timing of the proposed change was crucial. The Commission knew it must wait until the computerization of the PAYE system in 1988 before it could make such an extensive change. Individual taxation would increase the number of taxpayers and require the coordination of family deductions.¹⁸⁷ Waiting, however, threatened the proposal. There was no assurance the economic boom would continue or that there would not be a change in tax philosophy. Luckily, 1988 was a peak economic year. Although 1988 was the end of post-war economic growth, the last time the government was close to full capacity, the government retained the political capacity to change the tax unit and thereby meet its goal of helping one-earner couples while complying with European directives.¹⁸⁸

The E.C. had once again demanded that “[t]ax discrimination should be examined with a view to arriving at a neutral system which does not act as a disincentive, particularly with regard

¹⁸¹ Cmnd 9756, at 3.

¹⁸² Harding, *supra* note *, at 124.

¹⁸³ Individual taxation, to the extent it lowers the taxation of married couples and necessitates increases in tax rates, will disadvantage those in relatively greater need. One-parent families, largely composed of women and children, constitute one of most rapidly-growing family types. In Britain this group is extremely marginalized. Hilary P.M. Winchester, *Women and Children Last: The Poverty and Marginalization of One-Parent Families*, 15 TRANSACTIONS OF THE INSTITUTE OF BRITISH GEOGRAPHERS 70-86 (1990).

¹⁸⁴ Cmnd 9756, at 26. The government was also concerned about the “great practical difficulties in enforcing such special provisions,” if did try to police intra-spousal giving. *Id.*

¹⁸⁵ Cmnd 9756, at 26.

¹⁸⁶ Cmnd 9756, at 26.

¹⁸⁷ Cmnd 9756, at 1.

¹⁸⁸ Charles Feinstein, *Success and Failure: British Economic Growth Since 1948*, in THE ECONOMIC HISTORY OF BRITAIN SINCE 1700, at 3:95, 95 (Roderick Floud & Donald McCloskey, 2d ed., 1994).

to the taxation of the earnings of married women.”¹⁸⁹ The House of Lords understood that the European Parliament recommended a tax system that was neutral as been married couples where only one spouse was in paid employment and those where both spouses were in paid employment.¹⁹⁰ The commentary provided by the House of Lords noted the seeming inconsistency in the E.C.’s objectives:

“Neutral” is here presumably intended to mean that one-earner and two-earner couples with the same total income should in principle pay the same tax. However, such neutrality can be guaranteed only under an *aggregate* taxation system. With *independent* taxation, the total tax depends on how the earnings are split. There thus appears to be a contradiction between the first part of the recommendation and the second.¹⁹¹

Without reconciling those two objectives, Parliament adopted mandatory individual filing in 1988 to go into effect in 1990, so that all spouses were taxed separately on all income, both earned and unearned.¹⁹² Conservative Chancellor Nigel Lawson pushed hard for this change to the taxable unit.¹⁹³ Margaret Thatcher, on the other hand, did not support individual taxation, believing it would alienate working wives.¹⁹⁴ Because of the British system of exemptions, individual filing would do little for most two-earner couples and provide a lot of tax-planning opportunities for one-earner couples. Lawson was able to win support for individual filing by demonstrating its benefits in terms of the “so-called unemployment trap” for the very reason it would keep wives out of the labor market.¹⁹⁵ This motive flew in the face of European directives even as it appeared to implement European policy. Similarly, when Lawson pushed for larger personal exemptions, he was troubled that couples with two earners would receive a higher

¹⁸⁹ Bulletin of the European Communities, Supplement 3/86, “Equal Opportunities for Women,” COM(85) 801, at 12. A seminar was held on the topic of tax neutrality in the United Kingdom in early 1986. Bulletin of the European Communities, Supplement 3/86, “Equal Opportunities for Women,” COM(85) 801, at 13. The OECD likewise continued to be active in this area. OECD, INTEGRATION OF WOMEN, *supra* note *.

¹⁹⁰ House of Lords 1985, p.15, *quoted in* Cathal O’Donoghue and Holly Sutherland, Accounting for the Family: The Treatment of Marriage and Children in European Income Tax Systems, Innocenti Occasional Papers, Economic and Social Policy Series (1998) at 4.

¹⁹¹ House of Lords 1985, p. 15, *emphasis added, quoted in* Cathal O’Donoghue and Holly Sutherland, Accounting for the Family: The Treatment of Marriage and Children in European Income Tax Systems, Innocenti Occasional Papers, Economic and Social Policy Series (1998) at 4-5.

¹⁹² “Section 279 of the Taxes Act 1988 (which treats the income of a woman living with her husband as his income for income tax purposes) shall not have effect for the year 1990-91 or any subsequent year of assessment.” Finance Act 1988, c. 39, §32. Change was pushed by Nigel Lawson, who was Chancellor in Mrs. Thatcher’s third administration. His predecessor, Sir Geoffrey Howe, also wanted the change (publishing the 1980 Green Paper), but faced resistance from Mrs. Thatcher, perhaps because she thought the idea came from Sir Geoffrey’s wife, Elspeth. John Tiley, *United Kingdom*, in FAMILY TAXATION IN EUROPE 129, 132 n. 17 (Maria Roch ed., 1999). This proposal also allowed for confidentiality between spouses. Before the 1988 Act, a wife had to disclose to her husband her income in order for him to accurately complete the couple’s return but a husband did not have to disclose his information to his wife. Many lamented what this did for women’s bargaining position within marriage. Susan Himmelweit, *Making Visible the Hidden Economy: The Case for Gender-Impact Analysis of Economic Policy*, 8 FEM. ECO. 49 (2002). Since 1990, husbands were only able to find out about their wives’ tax affairs, and vice versa, if they are given written authority. IN3—Confidentiality, Independent Taxation Manual: Main Contents, www.hmrc.gov.uk/manuals/inmanual/in3.thm.

¹⁹³ NIGEL LAWSON, THE VIEW FROM NO. 11, at 814 (2003).

¹⁹⁴ NIGEL LAWSON, THE VIEW FROM NO. 11, at 882-4 (2003).

¹⁹⁵ NIGEL LAWSON, THE VIEW FROM NO. 11, at 884 (2003).

exemption than those with only one earner.¹⁹⁶ As had the 1985 Green Paper, Lawson wanted freely transferable exemptions to help couples with one wage-earning spouse.¹⁹⁷ Lawson had to abandon transferrable exemptions, however, because the Inland Revenue, fresh off the adoption of computerization, did not have the capacity to handle them until 1993, which would have been after another General Election.¹⁹⁸

Parliament recognized that this form of individual filing would cause some married couples to shift income between spouses to reduce their collective tax obligations. There was debate on an amendment proposed by the Labour Party that would deny tax benefits for gifts between spouses that were “undertaken with the sole or main objective of achieving a tax advantage.”¹⁹⁹ The Labour Party was concerned that, with individual filing:

It will be possible to make a gift that will produce income which will be taxed at a lower rate than it would be in other circumstances, especially where one member of the household is in a higher tax bracket and the other member pays tax at the basic rate.²⁰⁰

Norman Lamont, Conservative MP, defeated the measure, claiming that this prohibition: would undermine the very basis of independent taxation. If the amendment were carried, there would be no independence for married couples, nor would people be free to arrange their affairs as they wished...Independent taxation is bound to mean that some couples will transfer assets between them with the result that their total tax bill will be reduced. This is an inevitable and acceptable consequence of taxing husbands and wives separately.²⁰¹

Thus, there was recognition in 1988 that some couples would use individual filing for their own economic advancement and that result was accepted by the Conservative government.

While individual filing was relatively easy to adopt, it was more difficult to adjust exemption levels. This was particularly important in the U.K. because the British government exempts much more income from tax than the U.S. In 1990, almost 25% of the gross earnings of the average single worker and 65% for the average married couple was exempted from tax, which amounted to 2.9, 3.7, and 4.5 times the relief given to single persons, married couples, and heads of households in the U.S.²⁰² When the British government wanted to increase exemptions as part of its 1980s tax-cutting movement, it had to distribute them in a politically acceptable way. Because two-earner families already enjoyed higher exemptions (the MMA plus the WEIA), if exemptions were simply increased across-the-board, two-earner couples would get 45% of the tax relief.²⁰³ This group constituted only 30% of taxpaying families.²⁰⁴ “Such

¹⁹⁶ NIGEL LAWSON, *THE VIEW FROM NO. 11*, at 815, 881 (2003).

¹⁹⁷ Some women thought the transferrable exemption would require couples to compare financial information, which they did not want, but Lawson thought “the wife for whom privacy was important could always purchase it cheaply enough by letting her husband keep the transferable allowance.” NIGEL LAWSON, *THE VIEW FROM NO. 11*, at 885 (2003).

¹⁹⁸ NIGEL LAWSON, *THE VIEW FROM NO. 11*, at 885 (2003).

¹⁹⁹ Standing Committee G, June 13, 1989, quoted in Redston, *supra* note *, at 680.

²⁰⁰ Quoted in Redston, *supra* note *, at 680.

²⁰¹ Quoted in Redston, *supra* note *, at 680.

²⁰² Joseph A. Pechman and Gary V. Engelhardt, *The Income Tax Treatment of the Family: An International Perspective*, 43 NATIONAL TAX J. 1, 3-4 (1990).

²⁰³ It was estimated to cost more than £1 billion in revenue if the government raised personal allowances by 5%. Cmnd 9756, *supra* note 33, at 10.

positive discrimination is neither necessary nor economically desirable at a time of high unemployment, particularly among the young (of both sexes).”²⁰⁵ As a result, Parliament awarded each spouse a Personal Allowance (PA), equal to the former SPA, and the couple was given a Married Couple’s Allowance (MCA) equal to the additional amount previously received under the MMA.²⁰⁶ Consequently, couples were no worse off after 1990 than they had been before.²⁰⁷ To dodge the issue of providing married couples favorable tax treatment compared to single taxpayers, the MCA was not indexed to inflation, so it gradually decreased in real value over the 1990s, and it was eliminated in April 2000.²⁰⁸

[compare to U.S.]

So, at the end of a decade of tax cuts, Parliament adopted individual tax filing but the U.S. did not. The British government did so in a way that was intended to benefit one-earner families, tacitly acknowledging that couples would shift income from higher tax bracket spouses to lower tax bracket spouses. For many in the government helping single-earner families did not mean helping wives for their own sake.²⁰⁹ Despite the fact that individual filing had been a feminist objective for more than a century, there was an attempt to help families’ economically while keeping women in the home.²¹⁰ Women, nonetheless, welcomed individual filing as a victory.²¹¹ Individual filing was deemed to end an “explicit sex discrimination” that was considered by most women to be offensive,²¹²

PART IV. DAYS OF RECKONING

The decade following the enactment of individual filing was not a good time for the British economy. The pound was bound in the E.C.’s European Exchange Rate Mechanism until

²⁰⁴ Cmnd 9745, at 9.

²⁰⁵ Cmnd 9756, at 15.

²⁰⁶ Initially, this special allowance was set against a husband’s income but any unused portion could be transferred to the wife. Finance Act 1988, §257B. Making receipt of the MMA conditional on the wife’s not claiming a SPA against her earnings was acknowledged to create a strong incentive for wives to stop working. A. Zabalza and J. L. Arrufat, *Efficiency and Equity Effects of Reforming the British System of Direct Taxation: A Utility-Based Simulation Methodology*, 55 *ECONOMICA* 21, 44 (1988).

²⁰⁷ Natalie Lee, *The Effect of the Human Rights Act of 1998 on Taxation Policy and Administration*, 2 *EJOURNAL OF TAX RESEARCH* 155 (2004).

²⁰⁸ Finance Act 1999, c. 16, §31.

²⁰⁹ Also showing that this was not the high-point of British social equality, the U.K. did not endorse the E.C. Social Charter in 1988 and did not join the Social Chapter of the Maastricht Treaty in 1991. Stein Ringen ed., *Family Change and Family Policies: Great Britain, in FAMILY CHANGE AND FAMILY POLICIES IN GREAT BRITAIN, CANADA, NEW ZEALAND, AND THE UNITED STATES* 31, 33 (Sheila B. Kamerman & Alfred J. Kahn, editors, 1997).

²¹⁰ Susan B. Boyd and Claire F. L. Young, *Feminism, Law, and Public Policy: Family Feuds and Taxing Times*, 42 *OSGOODE HALL L.J.* 545-82 (2004), argues feminists have little influence over tax policy.

²¹¹ Susan Himmelweit, *Making Visible the Hidden Economy: The Case for Gender-Impact Analysis of Economic Policy*, 8 *FEM. ECON.* 49, 61 (2002).

²¹² J.A. KAY AND M.A. KING, *THE BRITISH TAX SYSTEM* 43 (5th ed., 1990).

the restrictions required led to a run on the pound.²¹³ On Black Wednesday, 1992, Britain liberated the pound, but the Conservative party's credibility for managing the economy was already damaged.²¹⁴ The Conservatives fell from power for 15 years.²¹⁵ Much as the nation had second thoughts about the European exchange rates, it re-debated the value of individual taxation. Nonetheless, the prospect of repeal of the latter has not been seriously entertained.²¹⁶ The new tax unit appears here to stay.

This Part focuses on two types of consequences that have resulted from individual filing. First, it looks at the incentive effects individual filing has had on the country's wives. In theory, the individual filing regime should induce more wives to enter the paid labor market or, alternatively, encourage the shifting of ownership of income-producing property from husbands to wives. These would both result in more of a couple's income being taxed in the lower tax brackets of the wife and improve the economic situation and relative power of wives. Second, this Part looks at how individual filing also encourages tax avoidance by higher-income spouses who do not want to reduce their control over the income they shift for tax purposes. Some higher-income spouses have sought to create new means of transferring tax ownership, but little else, to their lower-income spouses. This tax avoidance, in turn, generates new pressures within the British tax system.

A. POWER TO THE WOMEN

The adoption of individual taxation is expected to produce many significant changes in the behavior of married couples. Long before individual filing, people in higher tax brackets responded to taxes with intra-family planning; similar planning should result from the opportunities presented by individual filing.²¹⁷ Proponents of individual filing argue that the consequences of this planning will be socially desirable. This section focuses on two of those consequences: the increased paid employment of wives and their increased ownership of family property.

²¹³ Neal, *Impact of Europe*, *supra* note *, at 291-2; Matthew Tempest, *Treasury Papers Reveal Cost of Black Wednesday*, THE GUARDIAN, 9 February 2005, at <http://www.guardian.co.uk/politics/2005/feb/09/freedomofinformation.uk1>.

²¹⁴ *Id.*

²¹⁵ Patrick Hennessy, *Gordon Brown Hit by Tory Poll Surge*, TELEGRAPH, 10 October, 2007, at <http://www.telegraph.co.uk/news/newstopics/politics/1566048/Gordon-Brown-hit-by-Tory-poll-surge.html>,

²¹⁶ Mumford.

²¹⁷ Research on the changes in taxpayer behavior following changes in marital deductions found a significant drop in marriages in last month of the tax year and an increase in the summer months indicating that taxes do distort behavior. Alexander M. G. Gelardi, *The Influence of Tax Law Changes on the Timing of Marriages: A Two-Country Analysis*, 49 NAT'L TAX J. 17 (1996). Altruistic parents are also found to avoid taxes by changing the timing of transfers when inter vivos gifts are taxed separately from bequests. Katarina Nordblom and Henry Ohlsson, *Tax Avoidance and Intra-Family Transfers*, 90 J. PUB. ECO. 1669 (2006). In the late 1970s Britain transferred substantial child allowance from husbands to wives. Some scholars found strong evidence shift toward greater expenditures on wives' and children's clothing coincided while others found a less conclusive answer. Shelly J. Lundberg, Robert A. Pollak, and Terence J. Wales, *Do Husbands and Wives Pool Their Resources? Evidence from the United Kingdom Child Benefit*, 32 J. HUM. RES. 463-80 (1997); Julie L. Hotchkiss, *Do Husband and Wives Pool Their Resources? Further Evidence*, 40 J. HUM. RES. 519 (2005).

i. EMPLOYMENT OF WIVES

As illustrated by the 1986 Green Paper, encouraging wives to enter the paid labor market was not the objective of the 1990 change; this group of taxpayers was not the group targeted for tax relief. Instead, Parliament operated with the assumption that wives would leave the market when they had children.²¹⁸ “The Government believe that the tax system should not discriminate against families where the wife wishes to remain at home to care for young children.”²¹⁹ The government wanted to ensure that “[o]ne-earner couples at all income levels...see their tax burden fall substantially.”²²⁰ The British desire to help one-earner families by enacting individual taxation conflicted with the concerns of the E.C. in the 1980s and the U.S. today. In the E.C., the concern was that the traditional joint return “serve[d] as a strong disincentive for the wife to join the labour market.”²²¹

There is an on-going debate about the extent to which individual filing is likely to increase wives’ incentive to engage in paid employment.²²² Studies have sought to resolve whether the income tax has significantly affected women’s decisions on this matter.²²³ One study conducted in Sweden found that individual filing does encourage wives to provide more paid labor.²²⁴ On the other hand, a second study shows that women in countries with joint income taxation exhibit no statistically significant difference in their labor force participation than if the country has individual taxation.²²⁵ A third concludes that a wife’s choice to enter the

²¹⁸ Cmnd 9756, *supra* note *, at 15.

²¹⁹ Cmnd 9756, at 15.

²²⁰ Cmnd 9756, at 17.

²²¹ Commission of the European Communities, Memorandum on Income Taxation and Equal Treatment for Men and Women, COM(84) 695 final, at 3. The E.E.C. went so far as to suggest that husbands should be able to pay their wives in the family business in recognition of their employment services. COM(84) 695 final, at 13.

²²² Grace Ganz Blumberg, *Sexism in the Code: A Comparative Study of Income Taxation of Working Wives and Mothers*, 21 BUFF. L. REV. 21, 51 (1971); EDWARD MCCAFFERY, *TAXING WOMEN* 179-894 (1997); Paul J. Devereux, *Changes in Relative Wages and Family Labor Supply*, 39 J. HUM. RES. 696 (2004); Robert K. Triest, *The Effect of Income Taxation on Labor Supply in the United States*, 25 J. HUM. RES. 491 (1990); Claudia Goldin, *The Quiet Revolution that Transformed Women’s Employment, Education, and Family*, 96 AM. ECO. REV., PAPERS AND PROCEEDINGS 1 (2006). Nada Eissa and Hilary Williamson Hoynes, *Taxes and the Labor Market Participation of Married Couples: The Earned Income Tax Credit*, 88 J. PUB. ECON. 1931 (2004). *But see* Dorothy A. Brown, *Race, Class, and Gender Essentialism in Tax Literature: The Joint Return*, 54 WASH. & LEE L. REV. 1469, 1508-11 (1997); Lora Cicconi, *Competing Goals Amidst the Opt-Out Revolution*, 42 GONZ. L. REV. 257, 263-64 (2007); Nancy C. Staudt, *Taxing Housework*, 84 GEO. L.J. 1571, 1600 (1996); Thomas Mroz, *The Sensitivity of an Empirical Model of Married Women’s Hours of Work to Economic and Statistical Assumptions*, 55 ECNOMOETRICA 765 (1987); Bradley T. Heim, *The Incredible Shrinking Elasticities: Married Female Labor Supply, 1979-2003*, 42 J. HUM. RES. 881 (2007); Francine D. Blau and Lawrence M. Kahn, *Changes in the Labor Supply Behavior of Married Women: 1980-2000*, 25 J. LABOR ECON. 393 (2007); Chinhui Juhn and Kevin M. Murphy, *Wage Inequality and Female Labor Supply*, 15 J. LABOR ECON. 72 (1997).

²²³ Tanja van der Lippe and Liset van Dijk, *Comparative Research on Women’s Employment*, 28 ANN. REV. SOCIOLOGY 221, 233 (2002).

²²⁴ Siv Gustafsson, *Separate Taxation and Married Women’s Labor Supply*, 5 J. POPUL. ECON. 61, 72 (1992). The effect of Swedish tax system has been to make wives’ earnings a higher proportion of couples’ after-tax earnings than before-tax earnings, while Germany has experienced the opposite. *Id.*, at 75.

²²⁵ Shelley A. Phipps and Peter S. Burton, *Social / Institutional Variables and Behavior Within Households*, 1 FEM. ECON. 151-74 (1995).

market at all is more sensitive to taxes than whether she will work full- or part-time.²²⁶ A fourth finds that child care is the most important determinant for family patterns of labor supply.²²⁷ Finally, a fifth study shows that these changes were motivated less by individual filing than from a reduction in tax rates.²²⁸ If nothing else, this sample of studies demonstrate that this issue is more complex than simply the taxable unit.

In the U.K., evidence of wives entering the paid labor force as a result of the change in the tax unit is inconclusive. Because British wives previously had a separate exemption equal to that of a single person and the ability to file separately and have their wages taxed as though they were single, economic disincentives for a wife's paid employment should not have occurred unless wives were unwilling to use the separate filing option.²²⁹ For wives who did not file separately, other disincentives to employment, such as the need to report the income to their husbands so that their husbands could complete their tax returns, might have been great. With the adoption of individual filing, these disincentives were removed. Moreover, because wives' exemptions were not transferrable, couples after 1990 lose them if wives have no income (although, unlike before 1990, they could use their exemptions to offset unearned income). Therefore, there were some new encouragements for wives to enter the paid labor market but the previous system had already been comparatively more conducive to wives working than the American regime.

While between 1980 and 1992, two-thirds of the increase in the labor force was women workers, barely more than 60% of all British couples with children have two earners, and that number is only increased to 67% if there are no children.²³⁰ More troubling, studies find that these numbers hide underlying flaws in the labor market that might have been exacerbated by individual filing. In 1996, just under 75% of British women and 95% of British men were in the paid labor market, but most women were working part-time.²³¹ Thus, for example, while fewer Irish than British women work, Irish women's hours are longer for those that do. In the U.K., men work on average 45 hours per week while women work just over 30. This is the second lowest in Europe after the Netherlands.²³² Of the less than two-thirds of couples with two earners, only 33.8% have both spouses working full time and only 20.5% if they have children under 15.²³³ Married women in the U.K. have relatively small labor supply elasticities that have

²²⁶ Rachel A. Rosenfeld and Gunn Elisabeth Birkelund, *Women's Part-Time Work: A Cross-National Comparison*, 11 EURO. SOCIOLOGICAL REV. 111 (1995).

²²⁷ Irene Dingeldey, *European Tax Systems and their Impact on Family Employment Patterns*, 30 J. SOCIAL POL'Y 653-72 (2001).

²²⁸ Nina Smith, Shirley Dex, Jan Dirk Vlasblom, and Tim Callan, *The Effects of Taxation on Married Women's Labour Supply Across Four Countries*, 55 OXFORD ECON. PAPERS 417, 434 (2003).

²²⁹ They would also lose the extra MMA.

²³⁰ Irene Dingeldey, *European Tax Systems and their Impact on Family Employment Patterns*, 30 J. SOCIAL POL'Y 653, 663 (2001); Carole Pateman, *Beyond the Sexual Contract*, in REWRITING THE SEXUAL CONTRACT 1, 7 (Geoff Dench ed., 1999).

²³¹ Smith, Dex, Vlasblom, and Callan, at 419. While the payoff of increasing employment experience has risen a little in the wages of a wife who works fulltime, the pay penalty of part-time work has worsened. Davies, Joshi, and Peronaci, at 294. Women make up 80% of part-time workers. Carole Pateman, *Beyond the Sexual Contract*, in REWRITING THE SEXUAL CONTRACT 1, 7 (Geoff Dench ed., 1999).

²³² Smith, Dex, Vlasblom, and Callan, at 420.

²³³ *Id.*

not been substantially changed by individual filing.²³⁴ Therefore, there must be a concern that the combination of individual filing and the flattening of the tax brackets might have encouraged wives to enter into less well-paid, less-secure, part-time employment when, and if, they need additional income. It does not seem to have created the opportunities or motivation to seek out better-paid, more-secure, full-time alternatives.

As these numbers show, studies in the U.K. find a substantial loss of earnings associated with motherhood.²³⁵ That loss composes about half of a woman's earning potential in less qualified employment sectors, but the loss is becoming smaller for highly qualified women.²³⁶ This is an area where Parliament could significantly aid women, if it chose, to enable them to continue to work. There has been an increase in the number of British women with children under age five working: 28% in 1979, 30% in 1985, 43% in 1991, and 49% in 1995.²³⁷ Their full time employment has risen from 6% in 1979 to 16% in 1995.²³⁸ The exact causes, and how taxes affect these decisions and the loss of earnings in particular, remain unknown.

While British wives were entering predominately part-time paid employment in the last two decades, there has nonetheless been a reaction against the perception of government-created incentives for wives to enter the paid labor force. Some blame the tax system for either recognizing or even creating changing family structures:

Many see the new state libertarianism which has replaced [institutional support for conventional family life] not as a withdrawal of interference in private lives so much as the exercise of a new set of rules privileging a powerful interest group. This perceived new elite, which has definite "meritocratic" features, consists of professional "two-earner" couples, who are better off when taxed as independent workers, plus a growing entourage of fellow-travelling adult "singles" whose relative affluence is similarly promoted by fiscal policies treating "family life" as an individual lifestyle choice.²³⁹

This backlash blames state policy for the fact that the nature of the family unit has changed. Twenty-nine percent of all children born in 1991, a year after individual-filing became effective, were outside of marriage and, in 1991, 26% of households comprised just one person, compared with 17% in 1971, and only 24% of households were married couples with dependent children.²⁴⁰ We will have to wait and see the extent to which individual taxation is blamed for the change in family structures in the U.K.

²³⁴ Melvin and Ward-Batts, *supra* note *, at 1995.

²³⁵ Hugh Davies, Heather Joshi, and Romana Peronaci, *Forgone Income and Motherhood: What do Recent British Data Tell Us?* 54 POPULATION STUDIES 293, 294 (2000).

²³⁶ *Id.*

²³⁷ Davies, Joshi, and Peronaci, at 293. There has been an upward shift in the propensity of British women to be in paid work, even with young children. However, the least skilled are the least likely, and the labor force attachment might even have deteriorated since 1980. Davis, Joshi, and Peronaci, at 299.

²³⁸ *Id.*

²³⁹ Geoff Dench, *Nearing Full Circle in the Sexual Revolution*, in REWRITING THE SEXUAL CONTRACT 40, 41 (Geoff Dench ed., 1999).

²⁴⁰ Stein Ringen ed., *Family Change and Family Policies: Great Britain*, in Family Change and Family Policies in Great Britain, Canada, New Zealand, and the United States 31, 39 (Sheila B. Kamerman & Alfred J. Kahn, editors, 1997). Nonetheless, 41% of the population in 1991 lived in households that were composed of married couples with dependent children and only about 1 in 10 lives alone. Ringen, at 40. See also, Harry Wallop, "Death of the Traditional Family," at www.telegraph.co.uk/family/5160567/Death-of-the-traditional-family.html.

In the post-World War II era, the U.S. has similarly witnessed a growth in the percentage of wives entering paid employment. [need stats]. With individual taxation, one would expect a greater degree of responsiveness in the U.S. because American wives have no earned income deduction equivalent to the WEIA or the British right to separately report earned income, although there is a capped childcare credit subject to a phase-out.²⁴¹ Of course, other conditions, and other tax implications, might counteract its incentives. A Congressional Budget Office report found that joint taxation leads the lower-earning spouse to work between 4 and 7% less than he or she otherwise would, but that this reduces family earnings by only 0.7 and 1.2% because the higher-earning spouse works more.²⁴² Therefore, the amount of increase in the U.S. is not likely to be much greater than in the U.K.

[conclusion]

ii. FAMILY PROPERTY HOLDINGS

Before 1985, it was estimated that over half of all British wives owned some investment property, held independently or jointly with their husbands.²⁴³ With the adoption of individual filing, that percentage of wives and the value of what wives owned was expected to increase. Even Parliament expected families to react to individual filing through the shifting of income between spouses, recognizing that individual filing gives couples economic incentives for the wealthier spouse to transfer income to the lower-income spouse.²⁴⁴ In practice this means that wealthier husbands should transfer investment property to their wives so that their wives can first offset the income it generates with their exemption and, second, report its income in their lower tax brackets.

This shifting of the ownership of family property was expected to occur despite obvious drawbacks for the wealthier spouse. To be an effective transfer for British tax purposes, the transfer to the lower-income spouse must immediately divest the transferor's beneficial interest and vest that interest in the transferee or in a valid trust for the benefit of the lower-income spouse. As in the U.S., whether a person has sufficiently "given" property to another is a matter of intention and a question of fact.²⁴⁵ Unlike in the U.S., however, couples in the U.K. hold fewer easily transferred income-producing assets; more of a British family's wealth is held in their homes, as opposed to, for example, stocks or bonds.²⁴⁶ This should increase the relative impact on the higher-income British spouse of any transfer of assets and fewer British couples than their American counterparts can engage in this income-shifting behavior.

²⁴¹ CITES.

²⁴² CBO, FOR BETTER OR FOR WORSE: MARRIAGE AND THE FEDERAL INCOME TAX 12 (1997).

²⁴³ Chancellor of the Exchequer, Green Paper, The Reform of Personal Taxation, Cmnd 9756, March 1986, at 25.

²⁴⁴ See above. Not until 1991 could interest income be set against the personal exemption. So, for the first year, shifting of investment income would not have produced tax savings. Melvin Stephens, Jr. and Jennifer Ward-Batts, *The Impact of Separate Taxation on the Intra-Household Allocation of Assets: Evidence from the UK*, 88 J. PUB. ECO. 1989, 1990 (2004).

²⁴⁵ *Brennan Minors' Trustees v. Scanlan*, 9 T.C. 427 (1925); Halsbury's Laws of England (4th Ed., 2002), § 23(2) Income Taxation, para. 1294, at 365-66.

²⁴⁶ The most striking differences between the household wealth of couples in the U.K. and the U.S. in the upper middle of wealth distribution was in the nature of their assets. James Banks, Richard Blundell, James P. Smith, *Understanding Differences in Household Financial Wealth between the United States and Great Britain*, 38 J. HUM. RES. 241, 243 (2003).

The potential tax savings from income shifting is widely known and can be executed with no tax costs, although administrative costs will almost certainly be incurred. In its manual on capital gains, the Inland Revenue explains that a husband and wife or civil partners who are living together can transfer assets between themselves without triggering a capital gain or capital loss.²⁴⁷ Spouses can transfer assets to each other tax-free simply by completing, signing, and submitting a form indicating that there is a new owner. Thereafter, spouses can use both of their annual exemptions and also have more income taxed in lower rate brackets. With some planning and the right kinds of assets, couples can minimize their collective tax obligations. These benefits are explained to couples in the popular press as “[t]he last remaining area where there is tax-favourable treatment for those who are married...”²⁴⁸

One study has examined the post-individual filing shifting of family assets between spouses with different marginal tax rates.²⁴⁹ This study found a sizeable shift in the incidence of taxable income; however, it also found that few couples shifted income to the optimal level. In other words, most couples left some tax dollars on the table. Only 18% of couples shifted the optimal amount to the lower-income spouse if the husband’s tax rate was higher than the wife’s, and 30% did so if the wife’s tax rate was higher.²⁵⁰ But while the study found that couples would not shift income to the maximum extent possible to secure a tax reduction, it did find an increase in three outcomes: the proportion of wives having any asset income; the fraction of household investment income held by wives; and the fraction of households in which the wife held all their asset income.²⁵¹ The authors concluded that a 10% differential in spouses’ marginal rates led to a 2.6 to 3.1% increase in the share of investment income allocated to the spouse with the lower marginal tax rate.²⁵² This occurred despite the transaction costs of such re-allocations. Based on this study, individual filing does increase the wealth, if not the earning power, of British wives.

While this transfer appears to benefit women, there are instances when that is not the case. It is possible for British husbands to transfer not a simple interest but an interest with restrictions attached that will secure income tax savings without transferring control. Similarly, it is possible to give an interest in property that creates a joint ownership that is not an equal ownership. This can accomplish the same tax reduction objectives but without significantly increasing the wife’s real wealth. As to the latter, the Inland Revenue has created a default rule allowing spouses each to report 50% of the income of an asset held jointly, regardless of their

²⁴⁷ For this exception to apply, these individuals must not fall within any of the exceptions for nonresident spouses in the Income Tax Act 1988. Before 1990 couples were treated less generously with respect to the capital gains tax. They lost their second annual exemption for capital gains, lost their second exemption for their main residence, and they had no ability to elect whether to elect step-up-in-basis for inter-spousal gifts. Roger Kerridge, *Taxation and Marriage*, 47 CAMBRIDGE L. J. 77, 82 (1988). Moreover, despite the limitation that spouses can not transfer losses between themselves to offset the other’s gains, spouses can transfer depreciated property to one another, before triggering the loss, and then use the loss to offset gains. Finance Act 1988, 1988 Chapter 39, Section 104; CGTA 1979, s. 4(2); Taxation of Chargeable Gains Act 1992, §3, §58. Transfers between spouses are treated as taking effect at a value so that neither gain nor loss accrues.

²⁴⁸ Chas Roy-Chowdhury, “Would Getting Married Save You Tax?” at newsvote.bbc.co.uk/mpapps/pagetools/print/ews.bbc.co.uk/1/hi/business/3472573.stm.

²⁴⁹ Melvin and Ward-Batts, *supra* note 4, at 1989-2007.

²⁵⁰ *Id.*, at 2004.

²⁵¹ *Id.*, at 1990.

²⁵² *Id.*

relative ownership interests.²⁵³ Tax advisors understand the value of this for wealthy spouses: “This 50:50 rule is very useful if you wish to reduce you and your spouse’s overall tax liability, but also retain much of the control over underlying assets. You could put the assets in joint name, but only give away a 5% share of the investments.”²⁵⁴ This can, of course, create situations where wives are taxed on income they do not own and over which they have no control, even as it produces lower collective tax obligations. Although I have found no cases to date, it seems only a matter of time before a British marriage deteriorates to the point where a spouse with a 5% ownership interest but a 50% tax bill objects.²⁵⁵ At that point, at least this aspect of individual filing might not seem so wife-friendly.

The U.S. is likely to experience similar, if not greater, instances of income shifting than have been witnessed in the U.K. The U.S. will also create default rules that might produce troubling results. Ownership and control issues within marriage are complex, and tax laws producing possible tax reduction are unlikely sources of true spousal equality in property ownership. More information about the actual shifting of property needs to be obtained before we can count this consequence a success.

B. TAX AVOIDANCE

The ability to shift income between people in different tax rate brackets would not only increase the relative economic position of British wives but could generate significant policing problems for the government. To the extent the government desires that only real changes in ownership produce favorable tax results, it would need to review the substance of these transactions. The policing of these transfers requires costly effort and creates inequities between those caught and those who manage to avoid detection. British courts have already begun hearing cases in which the Inland Revenue contends that family income shifting constitutes tax avoidance and, therefore, the desired tax reduction should be denied. This section examines these costs associated with inter-spousal income shifting.

i. UNAVOIDABLE COMPLEXITY

In the years leading up to the adoption of individual filing, tax avoidance in Britain was on the increase.²⁵⁶ The Inland Revenue clawed back over £2 billion in unpaid taxes in 1988,

²⁵³ IN6—Separating the Couple’s Affairs, www.hmrc.gov.uk/manuals/inmanual/in6.thm. They will only be taxed based on their actual interests if they file Form 17 indicating that desire. Couples may also elect to have their mortgage interest relief divided between them on any basis they choose, regardless of who is legally responsible for paying the mortgage. IN6—Separating the Couple’s Affairs, www.hmrc.gov.uk/manuals/inmanual/in6.thm.

²⁵⁴ “Save Tax as a Married Couple,” at www.iii.co.uk/tax/howto_display.jsp?howto_id=2267. This does not apply to family companies, in which case ownership is by interest.

²⁵⁵ There will be times when one spouse is unwilling to shift income or resists being taxed on a larger-than-owned share of income, even in the hope of winning tax reduction. J.A. Kay and M.A. King, *The British Tax System* (5th ed. Oxford), 44.

²⁵⁶ For example, the Rossminster group of companies marketed complex tax plans to the rich in the late 1970s but came to agreement with Inland Revenue in March 1989. Peter Rodgers, *Taxing Times for Fiddlers on the Hoof: Convictions for Dodging the Inland Revenue are Increasing but Could Tax Avoidance Here take on US Proportions?* THE GUARDIAN (London), Sept. 1, 1989.

compared to £1.68 billion in 1987.²⁵⁷ Experts also concluded that the Inland Revenue was only catching the tip of a large tax-avoidance iceberg.²⁵⁸ As with most tax systems, the British government recognizes that it has a tax gap between what people pay in taxes and what the government thinks they should pay, estimated by the Inland Revenue at £10 billion annually.²⁵⁹ It is difficult for the Inland Revenue to find this lost revenue because there are substantially fewer audits in the U.K. than in the U.S., and it will require a substantial infusion of money to make this auditing possible, in part because the British system is less efficient than its American counterpart.²⁶⁰ The Inland Revenue's administrative costs, for example, are about 2% of revenue collected, which is three or four times the comparable figure for the IRS.²⁶¹

While the U.K. recognizes that tax avoidance costs the government significant revenue, Parliament has nevertheless been slow to act. As with most treasuries, the Inland Revenue is not required to recover every penny of tax that may be due, but it should, instead, "act with administrative common sense."²⁶² The possibility of introducing a statutory general anti-avoidance rule has been discussed, but no action taken, because many in the British government are unsure if this new complexity would be an improvement over current avoidance.²⁶³ As a result, if there is increased tax avoidance as couples develop new ways to shift income for tax purposes, the U.K. will have a choice, either to devote more resources to define and then police avoidance behavior or to ignore the tax-avoidance behavior, potentially on the ground that some amount of the income will find its way into wives' hands.

It is hard to see how the treasury can retain its common sense and yet police inter-spousal divisions of assets and income. If the government attempts to police marital income shifting in order to differentiate true transfers from sham ones or the amount of an interest actually transferred, there will need to be a significant revision of the currently simple regime. In the place of the current British system will need to be a more American-style, complex tax enforcement system. This flies in the face of current British theory.²⁶⁴ As discussed in part I, as

²⁵⁷ Peter Rodgers, *Taxing Times for Fiddlers on the Hoof: Convictions for Dodging the Inland Revenue are Increasing but Could Tax Avoidance Here take on US Proportions?* THE GUARDIAN (London), Sept. 1, 1989. For example, the Rosminster group of companies marketed complex tax plans to the rich in the late 1970s but came to agreement with Inland Revenue in March 1989. Peter Rodgers, *Taxing Times for Fiddlers on the Hoof: Convictions for Dodging the Inland Revenue are Increasing but Could Tax Avoidance Here take on US Proportions?* THE GUARDIAN (London), Sept. 1, 1989.

²⁵⁸ Peter Rodgers, *Taxing Times for Fiddlers on the Hoof: Convictions for Dodging the Inland Revenue are Increasing but Could Tax Avoidance Here take on US Proportions?* THE GUARDIAN Revenue are Increasing but Could Tax Avoidance Here take on US Proportions?" The Guardian (London), Sept. 1, 1989.

²⁵⁹ HM Revenue & Customs Anti-Avoidance Strategy, <http://hmrc.gov.uk/avoidance/vision-strategy.htm>. Those accused "say they are doing nothing illegal and argue they are merely better at using the tax system than the HMRC is." "Billions 'lost to tax avoidance,'" at newsvote.bbc.co.uk/mpapps/pagetools/print/news.bbc.co.uk/2/hi/business/4765030.stm. See also, *The Informal Economy*, A Report By Lord Grabiner QC, March 2000.

²⁶⁰ THURONYI, *supra* note 62, at 213.

²⁶¹ William Gale, *What Can America Learn from the British Tax System?* 18 FISCAL STUDIES 341, 343 (1997).

²⁶² *Vestey v. Inland Revenue Commissioners*, [1980] A.C. 1148, at 1173.

²⁶³ THURONYI, *COMPARATIVE TAX LAW*, 185.

²⁶⁴ The government generally relies on taxpayers to self-report tax advantages, imposing on taxpayers part of the cost of reducing avoidance behavior, but Parliament did not significantly increase the funds available for investigating those self-made reports. In 2004 Parliament introduced a direct tax disclosure regime must report tax advantage that will result from a scheme. Lynne Oates and David Salter, *Finance Act Notes: Disclosure of Tax*

it currently operates the British income tax has compromised in favor of simplicity even when it frustrates the goals of accurately measuring income or the ability to pay taxes.²⁶⁵ At a time when the Inland Revenue already spends £55 million per year answering more than 12 million enquiries on how to file taxes, despite the fact that less than 35% of British taxpayers have to file tax returns, the adoption of a more complex regime might very well be too high of a price to pay.²⁶⁶

The government has tried to use existing law to prevent the inter-spousal income shifting that occurs through family businesses, but it has failed.²⁶⁷ The most notable case to date, *Arctic Systems*, resulted in a victory for married couples and a substantial loss for the Inland Revenue.²⁶⁸ The final decision ended a seven-year standoff between the government and Geoff and Diana Jones, the husband and wife owners of a small IT consulting firm, Arctic Systems Ltd. After being let go from one employer, Geoff decided to go into business for himself in 1992, two years after individual taxation was established. The new company, owned equally by Geoff and Diana, produced £78,355 in income one year from Geoff's consulting work. On the advice of his accountants, Geoff was paid a salary of £6,520, which was less than he would have earned in the market, and Diana was paid £3,600 for four or five hours per week of administrative and bookkeeping work.²⁶⁹ After expenses and the corporate tax were deducted, the couple received the remaining income as dividends, minimizing their exposure to income taxes and national insurance contributions. The government challenged this tax plan, arguing that Geoff would never have consented to transfer half of his business to a stranger under the same terms.²⁷⁰ Attempting to apply a provision of a 1930 law intended to prevent transfers to minor children,

Avoidance Schemes – Section 116 and Schedule 38, 5 BRIT. TAX REV. 505 (2008). It first was limited to employment or certain financial products but has since been widened to the individual and corporate income taxes and the capital gains tax. HM Revenue & Customs Anti-Avoidance Strategy, <http://hmrc.gov.uk/aiu/summary-disclosure-rules.htm>. Family income shifting does not qualify under the rules provided for a reportable tax advantage. HM Revenue & Customs Anti-Avoidance Strategy, <http://hmrc.gov.uk/aiu/summary-disclosure-rules.htm>; HM Revenue & Customs, Guidance, Disclosure of Tax Avoidance Schemes (October 2008).

²⁶⁵ Gale, *What Can*, *supra* note *, at 348.

²⁶⁶ Turnier, *supra* note *. Those that do tend to be largely high-income taxpayers with asset income with withholding at lower tax rates, those with capital gains above the exemption amount, and those with self-employment income. Gale, *What Can America Learn*, 348.

²⁶⁷ In another case, a husband and wife established a corporation as part of a tax-planning device, but their device was upheld because, although one of their objects was tax reduction, they also used the new corporation to ensure that liabilities would not pass. Mr. P. A. Snell and Mrs. M. Snell versus Majesty's Commissioners of Revenue and Customs, Richard Barlow Special Commissioner, Spc 00699, July 2008, appeal dismissed. In another case, a husband transferred to his wife a discounted security and she then triggered a loss used to offset gains on options the husband received when his company was bought out. David Lachlan Campbell and Commissioners of Inland Revenue, Theodore Wallace and Julian Ghosh Special Commissioners, SC 3060/03. The court did find that the "main purpose" of this exchange was "to obtain tax relief." Par. 66.

²⁶⁸ Jones v. Garnett, [2007] UKHL 35.

²⁶⁹ Lord Hoffman, Jones v. Garnett, [2007] UKHL 35. Mrs. Jones never argued that she was paid in recognition of services performed in the home.

²⁷⁰ One commentator pointed out that if Mr. and Mrs. Jones became involved in a matrimonial dispute, Mrs. Jones's claim to half of the business would be respected. Roger Kerridge, Jones v. Garnett (*Arctic Systems*): *Another Way of Getting to the Same Result*, 5 BRITISH TAX REV. 591 (2007).

the Inland Revenue sought to tax all of the income generated by the business to Geoff individually.²⁷¹

The lower courts agreed with Inland Revenue, disallowing the tax advantage from this planning.²⁷² However, on appeal, although the Law Lords believed that “the decisions were tax driven and not commercially driven,” they concluded that the inter-spousal arrangement fell within the exemption provided for gifts between spouses.²⁷³ This secured the Joneses a 16% tax reduction.²⁷⁴ This benefit was widely-shared. During one hearing, the taxpayer argued that at least 200,000 families were potentially at risk of having their tax-planning devices invalidated; the government countered that the number was really closer to 30,000.²⁷⁵ Regardless of how many couples stood to benefit, gifts between spouses in the U.K., so the Law Lords held, are not taxed and these arrangements were given tax effect. Small businesses rejoiced. The chairman of a group of such businesses hailed the decision as “the best Christmas present for the U.K.’s small family businesses.”²⁷⁶

Inland Revenue was not satisfied with this result. The government sought its only recourse—to change the law. One high-ranking Treasury official gave a written statement to Parliament on July 26, 2007, proposing wide-ranging rules that would affect many limited companies and partnerships.²⁷⁷ He proposed that if two or more “connected persons,” which includes spouses, were engaged in a business and the income the business produced was divided in a manner that produced a tax advantage, the division could be recharacterized.²⁷⁸

The government believes it is unfair for one person to arrange their affairs so that their income is diverted to a second person, subject to a lower tax rate, to obtain a tax advantage (income shifting). The vast majority of individuals cannot shift their income and income shifting runs counter to the principle of independent taxation.²⁷⁹

While the government indicated that it had no intention of attacking actual transfers between spouses, for example transfers of income-producing property, it found

²⁷¹ *Id.*; Taxes Act 1988, §660A. The Revenue asserted that the policy had been in place since the early 1990s, but the announcement was not made until April 2003 in Tax Bulletin 65 that settlements legislation would apply to small business. Loutzenhiser, *Jones v. Garnett*, *supra* note *.

²⁷² Loutzenhiser, *Jones v. Garnett*, *supra* note *. When first heard by two Special Commissioners, both women, there was a division, but with the Special Commissioner giving a second, swing vote. *Id.*

²⁷³ *Jones v. Garnett*, [2007] UKHL 35.

²⁷⁴ Robert Lee, *Lords Rules in Favour of Arctic Systems*, Tax-News.Com, July 27, 2007.

²⁷⁵ Glen Loutzenhiser, *Jones v. Garnett: High Court Gives Taxpayer the Cold Shower*, 4 BRITISH TAX REV. 401 (2005); Roger Kerridge, *Jones v. Garnett (Arctic Systems): Another Way of Getting to the Same Result*, 5 BRITISH TAX REV. 591 (2007).

²⁷⁶ The group was the Professional Contractors Group. Alex Hawkes, *Arctic Systems: Timeline and Background on the Case*, ACCOUNTANCY AGE (Nov. 8, 2007) at www.accountancyage.com/accountancyage/specials/2149834/arctic-systems-georf-diana.

²⁷⁷ HM Treasury, *Income Shifting: A Consultation on Draft Legislation*, December 2007, at http://www.hm-treasury.gov.uk/d/consult_income_shifting.pdf.

²⁷⁸ HM Treasury, *Income Shifting*. Discussed in Anne Redston, *Income Sharing: The Nelsonian Option*, 6 BR. TAX REV. 680 (2007); Glen Loutzenhiser, *Income Splitting and Settlements: Further Observations on Jones v. Garnett*, 6 BR. TAX REV. 693 (2007).

²⁷⁹ PBR 2007 Press Notice PN02, quoted in Redston, *supra* note *, at 680.

something fundamentally different in the business relationship of the Joneses.²⁸⁰ These arrangements, it felt, “minimises their tax liability, and results in an unfair outcome, increasing the tax burden on other taxpayers and putting businesses that compete with these individuals at a competitive disadvantage.”²⁸¹ The Treasury then identified 85,000 small family-run companies and partnerships with arrangements similar to the Joneses. It estimated that the elimination of these arrangements would raise £200 million in revenue and prevent a tax loss by 2010-2011 of £350 million.²⁸² With the “continuing growth of small businesses using the corporate or partnership form, there are greater opportunities to shift income.”²⁸³

Drafting a workable solution proved difficult, however. There were many attacks on the Treasury proposal as business groups allied for its defeat. Arguing that it would disadvantage family-run businesses and discourage people from entering into business with anyone, spouses or not, pro-business groups sought to protect the financial advantages individual filing could provide.²⁸⁴ The Professional Contractors Group, who helped fund the *Arctic Systems* litigation, would not accept the “income shifting” label, arguing that for some years the government’s advice website, Business Link, recommended that businesses be set up jointly.²⁸⁵ The Group even used the opportunity to argue for the addition of transferrable exemptions.²⁸⁶ At least one organization, the Institute of Directors, “recognize[d] the Government’s concern, and we accept that income-shifting is a legitimate area in which to seek policy changes where there is clear abuse...” however, they doubted that there is any “principled way of drawing a boundary between abusive and non-abusive tax planning in this area... There is no point at all in

²⁸⁰ “The legislation is not intended to apply to genuine commercial arrangements, broadly where the share of overall income received by each individual is a fair and reasonable reflection of what they would be entitled to in a normal commercial arrangement, or where there is no overall tax advantage as a result of income shifting.” HM Treasury, *Income Shifting*. See also, Redston, *supra* note *, at 680.

²⁸¹ *Arctic Systems Ltd (Jones v. Garnett)*: HMRC Guidance, at www.hmrc.gov.uk/practitioners/sba.htm.

²⁸² HM Treasury, *Income Shifting*; Richard Tyler, “Arctic Systems and income shifting a year on,” at blogs.telegraph.co.uk/finance/richardtyler/4678027/Arctic_Systems_and_income_shifting_a_year_on/.

²⁸³ HM Treasury, *Income Shifting*; Richard Tyler, “Arctic Systems and income shifting a year on,” at blogs.telegraph.co.uk/finance/richardtyler/4678027/Arctic_Systems_and_income_shifting_a_year_on/.

²⁸⁴ PFK (UK) LLP, Accountants and Business Advisers, *Income Shifting: a Consultation on Draft Legislation Response by PKF (UK) LLP*, at

[http://www.pkf.co.uk/web/pkf.nsf/afb7e018aedc6fd88025725e0051f241/2e826cb8c9d1a42a802573f0005da9fa/\\$FILE/Income_shifting_representations_PKF.pdf](http://www.pkf.co.uk/web/pkf.nsf/afb7e018aedc6fd88025725e0051f241/2e826cb8c9d1a42a802573f0005da9fa/$FILE/Income_shifting_representations_PKF.pdf); Professional Contractors Group, *Response to the Consultation on ‘Income Shifting’ Draft Legislation*, February 2008, at

http://www.pcg.org.uk/cms/documents/POLICY_AND_CAMPAIGNS/taxation/income%20shifting/PCG%20Response%20to%20the%20consultation%20on%20Income%20Shifting.pdf; Institute of Directors, *Income Shifting: A Consultation on Draft Legislation*, January 22, 2008, at

http://www.iod.com/intershoproot/eCS/Store/en/pdfs/policy_consultation_income_shifting_response.pdf. See also, Tax Faculty, *Income Shifting: Guidance on Draft Legislation*, TaxGuide 6/07, at

http://www.icaew.com/index.cfm/route/153289/icaew_ga/Technical_and_Business_Topics/Faculties/Publications_and_technical_guidance/TAXGUIDE_6_07_Income_shifting_guidance_on_draft_legislation/pdf; The Chartered Institute of Taxation, *Income Shifting: A Consultation on Draft Legislation*, at

<http://www.tax.org.uk/showarticle.pl?ft=id=6578;n=0;p=1>.

²⁸⁵ Professional Contractors Group, *Response to the Consultation*.

²⁸⁶ Professional Contractors Group, *Response to the Consultation*.

asking the owners of small businesses to self-assess whether arrangements of the type with which this proposed legislation is concerned are arm's-length.²⁸⁷

Last minute lobbying prompted the Chancellor to postpone the rule changes in favor of more extensive consultation. As a result, what will be the final result after *Arctic Systems* remains uncertain.²⁸⁸ As it stands, these arrangements effectively reduce a couple's collective income taxes and Inland Revenue understands the difficulty of stopping this tax avoidance without creating a paperwork nightmare. Nonetheless, the government continues to consult on this issue. Given the current economic challenges facing the U.K., the Treasury is unlikely to take action. It did not bring forward legislation on this topic in the 2009 Finance Bill. "The Government will instead keep this issue under review."²⁸⁹ The alternatives remain open: Parliament can pass a law moving to a more American-type, complex tax regime allowing the Inland Revenue to devote the resources to police this behavior in order to evaluate, on a case-by-case basis, whether income has been forgone by one individual in favor of another, or Parliament can allow *Arctic Systems* to stand and concede income shifting as taxpayers desire.²⁹⁰

[compare to US / conclude]

ii. IGNORING BAD BEHAVIOR

Thus, the British government retains a choice, but one that it does not want to make. It can police inter-spousal income shifting, but with the costs discussed above, or it can grant tax reduction to all, even incomplete, transfers of property, either by issuing a directive to that effect or by simply ignoring the behavior. This latter option would likely be based on the hope that the rules, namely that spouses remain connected persons and so are prohibited from certain obvious tax avoidance transactions, are enough to police most avoidance behavior.²⁹¹ Parliament should be aware that if income shifting is permitted as a result of either of these actions, it will have certain negative unintended consequences.

The first consequence will be, of course, a reduction in government revenue. Even if the British population concludes that the beneficial consequences of income shifting should override all else, the behavior will decrease the taxes owed by those engaging in income shifting by decreasing the collective taxes that married couples owe. The British public is aware of this result, at least on an individual basis. For example, one British resident who had purchased land and later wanted to build a house to sell wrote to the *Financial Times* for tax advice. The reader

²⁸⁷ Institute of Directors, Income Shifting.

²⁸⁸ Richard Tyler, "Arctic Systems and income shifting a year on," at blogs.telegraph.co.uk/finance/richardtyler/4678027/Arctic_Systems_and_income_shifting_a_year_on/.

²⁸⁹ 5.103, HM Treasury, Pre-Budget Report 2008, 24 Nov. 2008, at http://www.hm-treasury.gov.uk/d/pbr08_chapter5_179.pdf. But see, 2009 Budget, <http://www.official-documents.gov.uk/document/hc0809/hc04/0407/0407.pdf>. As in the U.S., the focus has largely moved to offshore tax avoidance.

²⁹⁰ In 2005, Parliament updated its settlement rules between spouses to require an outright gift not subject to conditions in order to secure tax-free treatment. Income Tax (Trading and Other Income) Act 2005, part 5, c. 5, §636.

²⁹¹ IN8—Rules that Do not change, www.hmrc.gov.uk/manuals/inmanual/in8.thm.

was told by the Citizens' Advice Bureau, a charity that provides free and independent tax (and other) advice, that the couple could avoid capital gains tax if the husband gave half of the land and house to his wife as a gift.²⁹² Thus, married couples are being openly advised how to decrease the amount they must contribute to the government by shifting property and the income it generates. Whether people are aware of the combined result of these individual activities, estimated at £350 million, is unknown.²⁹³

That income shifting decreases tax obligations, and hence government revenue, also means that evidence of this behavior, even when the behavior is not undertaken for tax avoidance purposes, might become newsworthy. In fact, the argument that all income shifting constitutes tax avoidance has already proven valuable as political ammunition. In May 1995, Labour leapt on news that leaders of the National Grid, the company that operates the national gas transmission system throughout Great Britain, "had avoided tax by transferring share options to their wives." Tony Blair told the House of Commons, "The only reason why they transfer it to their spouses is because the remuneration is paid by way of share options to avoid income tax. That's why they do it. That's the issue."²⁹⁴ Similarly, when Adam Inram, former Labour defense minister, earning more than £115,000 from outside business interests, failed to declare a family firm that could be used in this manner to avoid tax, Conservatives brought the issue to the public's attention.²⁹⁵ How the public perceives of this form of shifting, and the degree to which they are willing to accept it, will play a part in the amount of damage it might do to the tax system as a whole.

Revenue lost directly from income shifting might not be the largest threat but the publicity it receives tacitly encourages other avoidance. Scholars have warned that it is not desirable that tax avoidance becomes a part of everyday life because the U.K.'s tax-compliant culture would be eroded.²⁹⁶ As studies in other contexts have shown, the perception of tax avoidance often reduces the compliance of taxpayers who were not previously engaging in tax avoidance behavior.²⁹⁷ In the U.S., for example, there is evidence that publicity of wealthy taxpayers' successful attempts to avoid their "fair share" of federal taxes undermines compliance along the income spectrum.²⁹⁸ When people believe that others have manipulated the income tax

²⁹² *Briefcase: Plotting That Tax Labyrinth*, FINANCIAL TIMES (London), Jan. 4, 1997.

²⁹³ HM Treasury, Income Shifting; Richard Tyler, "Arctic Systems and income shifting a year on," at blogs.telegraph.co.uk/finance/richardtyler/4678027/Arctic_Systems_and_income_shifting_a_year_on/

²⁹⁴ Roger Cowe, *Minister's Key Cash Questions: Labour's Tax Crusade Falter*, THE GUARDIAN (London), Dec. 10, 1997.

²⁹⁵ *Ex-minister denies family firm used for tax avoidance*, ACCOUNTANCY AGE (30 Mar. 2009), at www.financialdirector.co.uk/articles/print/2239408.

²⁹⁶ KAY AND KING, 44; Redstone, *Small Business*, *supra* note *.

²⁹⁷ IRS OVERSIGHT BOARD, ANNUAL REPORT TO CONGRESS, 2008, at 19 (2009); Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO STATE L.J. 1453, 1497-9 (2003); Steven M. Sheffrin and Robert K. Triest, *Can Brute Deterrence Backfire? Perceptions and Attitudes in Compliance*, in WHY PEOPLE PAY TAXES: TAX COMPLIANCE AND ENFORCEMENT 193 (Joel Slemrod ed., 1992); Leandra Lederman, *Tax Compliance and the Reformed IRS*, 51 U. KAN. L. REV. 971, 982 (2003); Steve Johnson, *The 1998 Act and the Resources Link Between Tax Compliance and Tax Simplification*, 51 U. KAN. L. REV. 1013 (2003); David Weisbach, *Ten Truths about Tax Shelters*, 55 TAX L. REV. 215, 215 (2002); Eric A. Posner, *Law and Social Norms: The Case of Tax Compliance*, 86 VA. L. REV. 1781 (2000); James Andreoni, Brian Erard, and Jonathan Feinstein, *Tax Compliance*, 36 J. ECO. LIT. 818 (1998).

²⁹⁸ IRS OVERSIGHT BOARD, ANNUAL REPORT, *supra* note 245, at 19; *Olson Testifies on Fairness in IRS Enforcement*, 2007 TNT 44-28; Written Statement of Nina E. Olson, National Taxpayer Advocate, Before the H.

regime, normally compliant taxpayers are tempted to do so as well. The U.K. already has lower tax morale than that in the U.S., so giving taxpayers additional motivation to avoid taxes could prove damaging.²⁹⁹

These potential reductions in revenue, both directly and with the erosion of taxpayer compliance, will damage the government budget if receipt of the tax revenue has been assumed.³⁰⁰ In that case, the money will have to be found somewhere else, either by increasing taxes or borrowing. Neither option is attractive, particularly during this economic downturn. One way to raise revenue that is likely to be considered is to increase income tax rates. These higher rates will disproportionately impact those who choose not to, or are unable to, engage in tax avoidance. Alternatively, Parliament could increase other taxes. The most likely candidates would be increasing the British VAT, already at 17.5%, or excise taxes. These regressive taxes currently raise a quarter of the nation's revenue.³⁰¹ These alternatives will, in turn, produce new behavior of their own as taxpayers respond to the changing tax circumstances.

Of course, this problem is not unique to the U.K. or to individual filing. To the extent that any tax provision provides taxpayers means to reduce their individual burdens, it runs the risk of requiring that the government increase taxes from other sources. The Inland Revenue currently reports that billions are lost every year because taxpayers evade the income tax; only part of that evasion comes from what the Inland Revenue sees as impermissible income shifting.³⁰² Similarly, the U.S., without this opportunity, reports a \$345 billion gross tax gap.³⁰³ Income shifting will likely increase this number. To the extent individual filing does decrease British or American revenue, it has far-reaching and troubling consequences, many of which were not, and are not, considered during debates over the conversion to individual filing. These unintended consequences must also be included in the evaluation of changing the taxable unit.

PART IV. CONCLUSION

The U.K. has often provided an example to the U.S. of progressive development. From its earlier woman's movement to individual filing, the U.S. can look over the pond for a guide to changing many different types of laws. Sometimes, however, the guidance is also a warning.

Subcomm. on Fin. Services and General Govt, Cttee on Appropriations, on Tax Fairness: Policy and Enforcement, Mar. 5, 2007, at 9; Steven M. Sheffrin and Robert K. Triest, *Can Brute Deterrence Backfire? Perceptions and Attitudes in Compliance*, in *WHY PEOPLE PAY TAXES: TAX COMPLIANCE AND ENFORCEMENT* 193 (Joel Slemrod ed., 1992).

²⁹⁹ James Alm and Benno Torgler, Culture Differences and Tax Morale in the United States and Europe, <http://ssrn.com/abstract=562861>, at 12. The U.S. has the highest tax morale. *Id.*

³⁰⁰ The most troubling aspect of this form of inter-spousal income shifting, however, might not be the loss of income tax revenue, but the conversion of wage income to dividends. This conversion allows former employees to minimize their contributions to the health care system. Claire Crawford and Judith Freedman, *Small Business Taxation*, Institute for Fiscal Studies, at www.ifs.org.uk/mirrleesreview, at 1; Anne Redstone, *Small Business in the Eye of the Storm*, 5 BR. TAX REV. 566 (2004).

³⁰¹ UK 2005, Official Yearbook, *supra* note *, at 365.

³⁰² *The Informal Economy*, A Report By Lord Grabiner QC, March 2000.

³⁰³ U.S. DEPT OF THE TREASURY, OFFICE OF TAX POLICY, A COMPREHENSIVE STRATEGY FOR REDUCING THE TAX GAP, Sept. 26, 2006, at 15; Olson, *Tax Fairness*, *supra* note 114, at 2.

The British experience with individual filing provides a cautionary tale for the U.S. There are significant complications and unfulfilled hopes that arise from the individual regime that need to be considered before the American tax unit is changed. This is true even if adopting individual filing ultimately proves to be the best choice. Individual filing might afford a more complete sense of equality between the sexes, including reducing indirect sources of inequality, but it also inadvertently provides a source of tax reduction for an already benefited group.³⁰⁴ Only when these costs are included in calculations with the benefits of the changed taxable unit can governments accurately assess the value of altering the tax regime.

Individual filing does not seem to be getting that sort of reevaluation in either country, quite possibly because there remain strong concerns about wives' positions in each society. For example, in the U.K., the extent of, or lack of, women's political power remains a cause of concern.³⁰⁵ Moreover, women today, as much as in the past, need economic independence.³⁰⁶ Poverty is a women's issue. In 2008 in the U.S., women were 35% more likely to be poor than men, and 37% more likely to be in deep poverty than men.³⁰⁷ Children living in single female-headed families were more than four times as likely to be poor than children living in married couple families.³⁰⁸ In the U.K., the Women's Budget Group has identified women as being disproportionately poor.³⁰⁹ That group advocated an anti-poverty strategy promoting women's paid work to help end this cycle of poverty.³¹⁰ The economic independence women need does not seem to be increasing, and individual taxation has not been shown to be the answer. Although wives do own more of families' assets than in the past, wealthy husbands are learning to give them lesser interests which allows wives to report more taxable income with limited control.

While individual filing has not been proven a panacea to wives' inequality, there are few credible arguments for returning to joint filing as opposed to trying to address these concerns. Most threats to individual filing are, in fact, made by those advocating on other issues. For example, some advocates of tax reduction toss around the idea of joint taxation as a means to lower tax rates.³¹¹ Similarly, the Chancellor has discussed replacing the family credit (which is paid to wives) with an in-work low income tax credit to encourage paid employment but it would also transfer more resources to husbands as the working spouse.³¹² The in-work credit would likely mean a return to joint filing after integrating the welfare and tax systems.³¹³ These other

³⁰⁴ Discussed, for example, in Catherine Barnard and Bob Hepple, *Substantive Equality*, 59 CAMBRIDGE L. J. 562 (2000).

³⁰⁵ For a discussion of women's role in politics, see Joni Lovenduski, *Women and Politics: Minority Representation or Critical Mass?* 54 PARLIAMENTARY AFFAIRS 743 (2001).

³⁰⁶ Lister, 180-91.

³⁰⁷ U.S. Bureau of the Census, *Income, Poverty, and Health Insurance Coverage in the United States 2008*, Report P60.

³⁰⁸ *Id.*

³⁰⁹ Women's Budget Group, *Women's and Children's Poverty: Making the Links*, at <http://www.wbg.org.uk/documents/WBGWomensandchildrenspoverty.pdf>.

³¹⁰ *Id.*, at 10.

³¹¹ Chartered Institute of Taxation, *Income Shifting*.

³¹² Lister, *supra* note *, at 188. Similarly, articles have appeared in the British press proposing the re-adoption of the joint tax return in order to help reduce poverty. See Pateman, *supra* note *, at 8; Glen Loutzenhiser, *Income Splitting and Settlements: Further Observations on Jones v. Garnett*, 6 BR. TAX REV. 693, 713 (2007).

³¹³ Lister, *supra* note *, at 189.

concerns, though by no means unworthy of debate, may someday bring the end of individual filing without vigorous debate over its worth. Much as the adoption of individual filing should only be undertaken considering the system's cons, jettisoning the experiment should occur only after recognizing that its pros will also be lost.

While the U.K. continues its two decade-long experiment with the individual tax unit, that the U.S. and its scholars have not examined the British example when they debate changing the American tax unit should make us pause. Not only does it bode poorly for our consideration of this particular policy, but it also bodes ill for what we might be missing on other issues by not looking at other nations as models. In this one policy area alone, depending on the country in which a couple lives, spouses will pay varying amounts in taxes compared to their single counterparts. There is a variety of instruments and combinations of family tax policies in use in the western world.³¹⁴ There is no clear convergence within even E.U. countries for family tax policies and so, within the E.U. alone, there are many guides for the U.S.³¹⁵ We should be willing to learn from their successes and their mistakes.

³¹⁴ O'Donoghue and Sutherland, *supra* note *, at iii. While overall the law is converging, it is not in the area of family taxation. PAUL FARMER AND RICHARD LYAL, EC TAX LAW (1994).

³¹⁵ Anne H. Gauthier, *Family Policies in Industrialized Countries: Is there Convergence?* 57 POPULATION 447-74, 450, 468 (2002).