

MMT and tax havens

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A few days ago [a commentator asked on the blog](#):

I am not an economist so hopefully my ignorance can be forgiven. I find myself confused by your oft repeated view that governments spend before taxing, and tax merely removes inflationary pressures from the economy, and your criticism of secrecy regimes for preventing governments from collecting tax due. If governments don't need the tax in order to spend, and companies and individuals are removing the tax which should be due from the economy, doesn't this have the same anti-inflationary effect as if they were paying tax? Am I just being to simple or is there a bit in the argument I'm missing?

Clearly there is a moral argument (with which I completely agree) against secrecy regimes and the inappropriateness of comparing government finances with a private households also makes complete sense, but there seems, from my imperfect understanding, to be a paradox here?

It's a good question and one that has been worth waiting to answer. I apologise to the commentator in question for the time it has taken me to do so.

If we look at MMT What it says is that there is no reason for a government to raise tax to pay for its spending. In fact, that spending must come before tax can be paid, because if that spending had not taken place the currency in which the tax was due would not have been created to let that tax payment happen. Tax, then, in MMT has two obvious and immediate functions [out of the six reasons to tax which I have identified](#). These are:

* **Reclaiming the money the government has spent into the economy.** As already noted, it may appear that tax revenue is being used to pay for government services supplied but that is not true: government spending always comes out of funds the government borrows from its central bank. Tax, in that case, reclaims the money spent to prevent excessive inflation. The amount reclaimed is that which is considered sufficient to leave the desired rate of inflation in the economy.

* **Ratifying the value of money.** Because a government requires that tax be paid using the currency that it creates (simply because that's the currency it bills in) that currency has for all practical purposes to be used in the economy for which it is responsible, assuming that tax forms a significant part of people's total liabilities. The payment of tax does, therefore, give a currency its value in exchange and as a result passes control of an economy to the government that charges that tax. This makes tax an absolutely fundamental component in macroeconomic policy.

But these are not the only reasons to tax. One of my criticisms of MMT, and over time I have had them, [just as Steve Keen has had](#), is that the other four reasons to tax are, too often, ignored by those who promote MMT. Those other four reasons are:

* **Reorganising the economy.** Fiscal and monetary policy are the two fundamental tools available to a government to manage its economy, assuming it has its own currency. As the explanation already offered has shown, money creation and taxation are the flip side of each other. Tax is then an integral part of macroeconomic policy and so of reorganising the economy to meet social and economic goals.

* **Redistributing income and wealth within the economy.** Experience has shown that market economies are very good at concentrating income and wealth in the hands of a few people in a society. At the same time economics makes clear that this is harmful to the prosperity of a society as a whole because it seriously reduces overall levels of demand in the economy. Redistribution of income and wealth is then an essential function that any Government must undertake and appropriately designed taxes are a proven and effective method for delivering this policy.

* **Repricing goods and services.** Markets cannot always price the externalities of the goods and services they supply or reflect social priorities. Tax permits repricing of goods and services to reflect these facts.

* **Raising representation in a democracy.** The fact is that if people know they pay tax they vote. This only seems to be true, however, for income taxes. That's why it is important that people are in that tax system. When they are they want a say on how the system works and democracy is enhanced as a result.

The critical point to make is that once it is apparent that tax does not fund government revenue then tax takes on another wholly appropriate, but different role in the economy. That role is to be the most powerful instrument available to government for the delivery of its economic, social, environmental, industrial and other policies. This is the idea that lies behind my book 'The Joy of Tax' where I argue that the joy in question is the fact that taxes provide the single most powerful instrument available to government to deliver these strategies.

These points have been ignored by many in MMT: it is one reason why Neil Wilson alienated me from it for a long time because he appeared quite indifferent to tax evasion so long as sufficient tax was raised. I may well have the same issue with Bill

Mitchell, but I think Bill [has issues with almost everyone](#). In my opinion that indifference is quite wrong.

MMT is in itself a description of what actually happens in the economy. Its strength is precisely that. Unlike neoclassical economics, which has no adequate theory of money and tax or the function of deficits, debt and even inflation control (or it would not rely on interest rates) MMT has answers based on fact. This makes it very powerful. But it would be absurd to claim that this means it is morally superior. Being right is a technical claim, not an ethical one. Ethics have to be added to MMT to taste. But, as I note below this is unavoidable in the case of MMT. Whereas neoclassical economics is designed to suggest the government has no role in an economy, MMT says (not by design, but because it is a fact) that government choice is implicit in macroeconomic management and so too then is Tax and related policy issues. In that case it's my argument that MMT supporters cannot be indifferent as to how tax is collected in the economy.

Let's take one core MMT argument and my first reason for tax as a starting point, which is the fact that tax is the main mechanism available within an economy for the control of inflation. When doing so let's recall that the wealthiest gain most from controlling inflation. It is their wealth that is preserved in that process, and the creditors' obligation that is upheld by controlling inflation, at cost to them. And it is also the wealthy person's businesses that benefit from the stability low inflation provides. It is, then, also in very many cases the wealthy who benefit most from the good ordering of a market economy that a government backed currency based on the price stability that sound taxation provides.

My point, then, is that the wealthy are the greatest beneficiaries of the most important use to which tax is put i.e. the controlling of inflation. Logically then you would think that they would be the greatest exponent of tax compliance, which is seeking to pay the right amount of tax (but no more) in the right place at the right time where right means that the economic substance of the transactions undertaken coincides with the place and form in which they are reported for taxation purposes.

What we actually know is that they do the exact opposite. Gabriel Zucman has suggested [the wealthiest evade the most tax](#). I am not quite as persuaded of this argument as Gabriel is, but I think it has merit. The consequence is obvious. Inequality is increased. Demand is reduced. The prospect of full employment is diminished. The need to run government deficits grows. The consequent demand for tax revenues to potentially control inflation will, in the long term at least, increase, and so the cycle continues. Tax evasion in this context is, then, not a micro economic issue of concern only when appraising the efficiency of the tax authority and when

considering the culpability of a particular taxpayer; this is an issue of macroeconomic concern.

Tax evasion does not simply mean that the government has greater difficulty in reclaiming these expenditure that it has injected into the economy, and so has to make greater demand of those with less capacity to pay; the entire structure of the economy is distorted as a consequence and we cannot be indifferent about. If anyone thinks MMT is then only about the quantum and not the profile or quality of the tax collected then, I think, they have seriously misunderstood the fact that whilst MMT might be descriptive, it is within the process it describes an economic theory that demands macroeconomic management in a way that is the precise opposite of the neoclassical economic prescription which suggests that governments must leave everything well alone.

Matters do, in fact, go further than that. Presuming the we are looking at something beyond the quantum of tax collected (T in the formula for national income accounting [I describe here](#)) and think that tax does have a social purpose then the failure to collect tax, whether as a result of poor tax design; a failure to resource tax collection, or because of tax evasion and avoidance, is not just a technical economic issue but is instead about the delivery of government policy across the whole spectrum of issues. Once more, this suggests that the concern is not a micro one, but is instead at the heart of macro policy, including macroeconomic policy. I will be publishing more theory on this point soon. For now let me suggest that this puts tax, and its payment or non-payment, at the core of the social contract, democratic process and the rule of law. Or, to not be too unsubtle, it makes it central to the right ordering of society that is, dare I say it again, the central underpinning of the system that preserves the property rights of the wealthy in all societies.

So what has this to do with tax havens and so potentially the broader issue of tax abuse? And is the claim that tax havens remove funds from the economy in the same way that tax does, and thereby deliver a similar inflation control mechanism, of any merit? I have to make it clear that the resounding answer is 'no'. Let me offer three reasons.

The first is that tax havens do not in any way take funds out of the economy. The suggestion that they might do so assumes that money does, in some literal physical sense, have a tangible existence, and that when money goes to a tax haven it is then removed from use. This is not true. Money may be deposited in tax havens but that does not mean that the money is then removed from use: it remains wholly available to those who sent it to an account in such a place or, of course, they would not have made use of such places. So the money is not taken out of the system.

The second reason is that because the primary reason for sending the funds to a tax haven would be to circumvent an obligation to pay tax then we can be fairly sure that tax is not paid as a consequence. But, if the total sum that has to be collected to ensure that inflation is controlled remains constant despite these funds moving to a tax haven then the wrong people will end up paying tax as a consequence with the results outlined above, and a consequent increase in inequality. That is socially harmful and subversive of the intent of any government likely to introduce MMT.

Third, because tax havens exist to undermine the authority of a government outside their own domain (and I stress, they have no other purpose) then is activity means that the delivery of democratically chosen policies is harder to fulfil, and the action is, then, inconsistent with the rule of law, the social contract, and democracy itself, all of which are implicit in the reasons for paying tax in an MMT system in my opinion.

In other words, within MMT we cannot be indifferent to tax havens: they are in fact antithetical to MMT in just about every way that can be thought of.

But I am open to other suggestions.