

Tax as the economic steering wheel

<https://www.taxresearch.org.uk/Blog/2025/08/15/tax-as-the-economic-steering-wheel/>

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Politicians tell us taxes pay for public services. In reality, it does something far more important — it shapes our society. In this video, I explain why tax is an economic steering wheel, not a fuel tank or piggy bank, and how we can use it to create fairness, tackle inequality, and protect our environment.

<https://www.youtube.com/watch?v=hQd5qLEfwZw&si=1enPA2UZIOR3EFDv>

This is the audio version:

https://www.podbean.com/player-v2/?i=8phr3-1933712-pb&from=pb6admin&share=1&download=1&rtl=0&fonts=Arial&skin=f6f6f6&font-color=auto&logo_link=episode_page&btn-skin=c73a3a

This is the transcript:

This video exists to talk about a lie that you have been told, and that is the lie that tax exists to pay for government spending.

It doesn't.

In reality, tax exists to shape our society by controlling inflation, by controlling inequality, by deciding what is good and bad by the way of pricing certain products and services, and by deciding whether we wish to promote certain economic activities or

reduce others.

Tax is the steering wheel that drives our economy, but it doesn't pay for government spending, and that's what I hope you'll understand by the end of this video.

The household analogy that we've discussed on this channel suggests that governments must earn before they spend. But in a modern economy, that's false. Governments create the money that they spend - something that I've said time and again, and which is obviously true because every time a government asks its central bank to make a payment, that central bank simply marks up its overdraft and doesn't look to see if there's money in the bank before making the payment that they've been instructed to do by a government with the legal backing to give the instruction, which is why, of course, the central bank can't argue.

So, tax does not exist to fill a bank account with money for ministers to spend from. That is not its role. If you think that tax is the fuel tank which lets the government spend, you've really misunderstood the analogy to the car that I've just been making. Tax is the steering wheel. It's not the fuel tank. And understanding this changes just about everything about what tax is for.

Tax exists to control inflation above all else.

Yes, I know you've been told by central bankers that, in practice, interest rates are used to control inflation, but to be polite to them, and I'm going to try to be polite to them, that's not true. Interest rates can't control inflation, and the best reason for suggesting that is that, firstly, interest rates are incredibly slow to have an impact upon the economy, and so in fact, if you change interest rates to try and control inflation, the inflation will probably have gone away before the interest rates have had an effect. So in fact, the move in interest rates that you put in place to control inflation will probably create deflation in the end of the day rather than inflation, or simply reduce growth: either way, the outcome will be undesirable.

But it's also because interest rates don't affect most of the things that cause inflation. For example, there was no way on earth that changing UK interest rates could change the supply chain disruption that created the inflation that we suffered in 2021 to 2023 as a result of the post-COVID supply chain breakdown and the outbreak of war in Ukraine, neither of which were within the reach of the Bank of England and its interest rate policy.

So we have to control inflation in a different way, and in fact, we always have.

The amount of money that is drawn out of the economy by taxation is the effective way in which the government controls the growth of the economy.

If it doesn't pull out enough, the economy grows too fast, and we might get inflation. If

it pulls out too much, the economy grows too slowly, and we could get a recession.

Finding the right balance, that gentle point where we are making a bit of progress, but not with too much inflation, is the whole goal of taxation within macroeconomic policy management, and that has nothing to do with interest rates.

So let's understand that tax is the central mechanism for controlling inflation within any economy.

But, once that fundamental role of tax is taken into consideration, we can also think about a whole load of other things that tax can do at the same time, because, like money, tax can fulfil many roles simultaneously.

It can, for example, control inflation and simultaneously redistribute income and wealth by choosing who should be paying tax to reduce the level of consumption in the economy, and since most excess consumption is by those with high income or wealth, they're the obvious targets for taxation if you're trying to control inflation.

So there is a symbiotic relationship between inflation control and redistribution of income and wealth by taxation. But there's more to tax than that.

For example, suppose that we want to reduce the amount of alcohol consumption in the economy: we increase the tax on alcohol.

Suppose we want to increase the amount of education in the economy: we provide tax subsidies for people who go on lifelong learning courses.

Suppose that we want to improve healthcare: we remove VAT from all healthcare products, and so on.

The point is this, that tax is able to shape what we do by the way, it can change the prices that we pay for certain things.

And it can also support redistribution in a different way. Tax can be used to change the balance between regions and even communities in the country through local taxation systems, and that is entirely possible as well.

So, tax is this massively important tool, which, as I've said, is rather like a steering wheel.

We can target harmful activities such as polluting industries, or we can strengthen underfunded regions via fiscal policy, and we can close the gap between the rich and the poor, and all of that is possible without being trapped in the "we can't afford it" way of thinking that neoliberalism suggests.

If we don't understand tax properly, we can leave wealth inequality unaddressed. And

we know that is deeply damaging.

We can starve regions of opportunity within the UK, and we can paralyse future debate on public services by simply permitting the false narratives on affordability that the household analogy and neoliberalism promote.

We have to understand taxes correctly. Tax is not a constraint on anything. It doesn't stop businesses. It doesn't stop people. It doesn't present us with problems which will prevent saving. Tax is, in reality, a tool for justice. It is a tool for creating economic level playing fields. It is a tool to make sure that we have a stable, strong, and progressive economy. It is one of the most powerful democratic levers available to any government.

It is in fact, this democratic control that it affords a government over the economy that is so useful about it. I called it 'The Joy of Tax' in my 2015 book of that name, most of which is, by the way, still entirely relevant today, and is probably worth a read. You can pick up copies secondhand very cheaply now, or you could still buy a new one, and I earn about enough to pay for a decent curry year as a consequence of the royalties I earn from that one. So I'm not doing much self-promotion by putting the idea forward, but it's there for you to have a look at.

Critically, without this understanding of tax inequality is inevitable, so we need to change politicians' understanding of tax.

We have to tell them to stop pretending that tax fund spending when it doesn't.

We have to tell them to design taxes that redistribute income and wealth and, as a result, create opportunity.

We have to use tax to penalise those who are destroying our environment.

Applying tax policy to deliberately rebalance our economy is the duty of the government, and it's time that our governments did that instead of pretending they can't afford to do so.

We need tax systems that work for fairness and not just for revenue, and we need to have reforms that create a genuine steering wheel arrangement so that tax can drive where we are going. We can't build a just economy without knowing how tax works.

So, as is usual at the end of a video, there's a poll.

What do you think?

Do you think tax funds the government?

Or do you think that tax is a tool, as I've explained in this video, to steer the economy in

the way that the government wants it to go?

Or do you think that doesn't matter?

Or do you just not know?

Let us know because this does help us to understand where you are and what videos we need to make.

But it also does something else. It helps us understand where public opinion is and what we need to do to help change it to create the fair and just society which is the ultimate goal of this channel.

Poll

[poll id="181"]

Taking further action

If you want to write a letter to your MP on the issues raised in this blog post, there is a ChatGPT prompt to assist you in doing so, with full instructions, [**here**](#).

One word of warning, though: please ensure you have the correct MP. ChatGPT can get it wrong.

Comments

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