governments operate a system called *progressive taxation*. This means that the more you earn, the more tax you pay. People are usually allowed to keep some of their income without paying any tax. This is called the *personal allowance*. The rest of their income is then taxed using the progressive system. For example:

Income before tax	Personal allowance	Tax to pay after allowance
£0 - £1,999		10%
£2,000 - £29,999	£5,000	22%
£30,000 and over		40%

Governments can decide to change the size of the personal allowance, or change the percentage that each income group has to pay. If the economy is growing too fast, and demand for goods and services is more than the economy can supply, the government will want to slow down spending.

To do this, they can decrease the personal allowance, or they can increase the percentage to pay in tax. This will mean people have less disposable income, and spending will slow down. If the economy is slowing down too much, governments can do the opposite.

What about government spending? How does that affect economic growth? The key to this is something called the *multiplier effect*. To understand how this works, let's look at an example. Imagine that the economy is not growing. This will make aggregate demand fall. In turn, productivity falls. This situation means that the nation's resources are not all being used. In other words, there are surplus raw materials, machines are not being used and workers are unemployed. What the economy needs is a *pull* in demand for goods and services.

The government can provide this pull by spending a large amount of money on public projects. For example, imagine that the transport department decides to spend £200 million on building a new motorway. This will give work to building companies and jobs to unemployed workers. In other words, more resources are being used and the nation's productivity is increased.

Companies and workers on the motorway project will save some of the money they earn, but also spend some. The money they spend will be income for others in the economy. If half of the £200 million is spent, then the total national income has grown by this much:

£200 million + (0.5 x £200 million)

Each time a proportion of the income is passed on, the economy grows again:

£200 million + (0.5 x £200 million) + (0.5 x £100 million), etc

In theory, the multiplier effect will continue until there is full employment and the nation's resources are being used to their fullest extent.

B Comprehension

Now read the text again and answer these questions in your own words.

1 What are the two tools of fiscal policy?
2 What is someone's personal allowance?
3 What will the government do to taxes if the economy is slowing down?
4 How can the government create more demand in the economy?
5 When does the multiplier effect stop working?

Before you listen

Discuss these questions with your partner.

→ What do you think makes a good tax?
→ Which four things listed below do you think are the most important?

1 It's easy to collect.
2 It's paid often.
3 It's easy to understand.
4 It's not paid too often.
5 It's a low percentage of income.
6 It's easy to pay.
7 It's fair.
8 It's large enough for the government to use.

C Listening

Now listen to someone talking about Adam Smith's four rules for good taxation. Which four ideas from the list above are mentioned?