DODSON: Discussions on Henry George do not generally focus on his contributions to economics as a science. Georgists tend to concentrate on his ideas about land monopoly, land tenure and taxation. We are going to broaden this discussion as far as it can be taken based on our perception of what is involved in the subject. I am going to lead and participate in this discussion. My name, for those who do not know me, is Ed Dodson. I am a trustee of the Henry George School in New York and am currently its President. And, I have more than a passing interest in this subject because I am working on a book, so I hope to learn from my fellow discussants and from the audience. Perhaps I will come away from this discussion with some ideas of what to write about that I can steal from them. We will talk for forty-five minutes and then open this up to audience participation. We hope this will be entertaining and enlightening as well. With that, I am going to ask each of our discussants to re-introduce themselves to you.

LAMBERT: I am Ian Lambert. I am an attorney at law down in the Cayman Islands. I have been coming to Georgist conferences since 1989 in Philadelphia, and I am one of the founding members of the Congress of Political Economists.

TIDEMAN: I am Nicholas Tideman, professor of economics at Virginia Polytechnic Institute and State University. I am also a fourth generation Georgist. My great grandfather came to this country without knowing how to speak English. But he asked another Swede how to learn to speak English. That Swede suggested he read the Standard because of the excellent English in it, and so my great grandfather picked up Henry George's ideas along with his English. And, they have been transmitted through the family ever since.

HUDSON: I am Michael Hudson. I am Research Director of the Henry George School. My background is mainly in financial analysis. I came to New York in 1960 and spent four years as economist with a savings bank analyzing how property prices were a function of financial flows and distinguishing between savings banks, commercial banks, S&Ls and financing real estate. I went to work for Chase Manhattan Bank as a balance of payments analyst and most of my work since that time has been on international flow of funds, balance of payments and domestic flow of funds analysis.

DODSON: Let me open this discussion by saying that I started out teaching Henry George's work at the Henry George School in Philadelphia. And, for those of you who have had that experience as either a teacher or a student, you know that the School teaches the full system of production and distribution that Henry George wrote about – the laws of production and distribution which he describes as "laws of tendency." There has been a lot of academic evaluation of George's writings, and the bottom line seems to be that while economists and others support his analysis of the laws of rent and wages, there is a lot of criticism of George and his law of interest. That is where I would like to start, by throwing out to our discussants a question to respond to; that is, do you think based on your understanding of George that he gave us a good picture of how the fundamental laws of production and distribution work and, in particular, what do you think about his analysis of the law of interest?

LAMBERT: I think a lot of people do not realize that George's whole theory of political economy evolved over time. And, what he ended up with in his final book, which he never actually completed but almost completed (the Science of Political Economy) had the same essential framework but in many respects was very different from what he had in *Progress and Poverty*. Progress and Poverty is the book that everyone has read and everyone knows. And, in particular, it seems to be the only book that known Georgist economists touch on. In there, George has what he calls a "natural fructification theory" of interest. But, by the time he has got to the Science of Political Economy, he has really changed that and doesn't talk a great deal about interest. For the first time, he started to talk about credit – and implicitly about time preference, and he is going towards a much more Austrian theory of interest which is related to time preferences.

Now, I think it is a great tragedy that theory was not worked out more fully, because people constantly go back to his original observation and then dismiss it out of hand. I think there is a great deal in the Science of Political Economy which hadn't really been teased out. The way I describe it is that there are a great many unpolished gems there. You keep stumbling over those which are almost like throw-away lines. And, I genuinely feel that if he had lived another ten years he would have polished up a number of those and would have taken his system of political economy in a way in which it would have addressed credit, banking, money markets and dealt with the growth of national debt on money markets, and things like that a lot further.

HUDSON: A hundred years ago when Henry George wrote, the English language was used differently than its is today. If you read the works of anyone who wrote at that time, they used the word "interest" ambiguously. They used it both to describe the money interest earned and accruing on money capital and they also used it to mean profit. For instance, the Austrian who wrote about capital and interest was really referring to profit. This made people who earned money interest real happy because by justifying the profits that the entrepreneur made undertaking physical investments, they somehow got a free ride on what they did which was money stipulated in advance. No economist at the time really made much of a difference in this even at the other end of the political spectrum. Karl Marx in the third volume of Capital wrote that, of course, there is a distinction between money capital and interest, but he believed that the growth of money interest and financial capital -- if everything would be consumed by industrial capital as would rent in the aggregate as land would be converted into capital -- that none of this would be a problem in the industrialized countries. Nobody was making the distinction that we see coming to be made in the twentieth century.

LAMBERT: Michael has mentioned the *Science of Political Economy*. In addition, George has an entire chapter in *Social Problems* on the national debt, and he developed what he called "fictive" capital. This is a wonderful word because it shows that George saw there was a difference between physical capital and money capital. Money capital riding on the shoulders, not unlike the industrial capital investors, but also on the landlord. And, nobody of his time denounced national debt as more of a fraud, more a parasitism and a rip-off than Henry George. The landlords which managed to load down the ratepayers with bonds and interest. So, we see policies developed in the late 1880s and early 1890s. George was writing at a time when America almost entirely paid off its national debt. So, Henry George comes to Europe. He is listened to by the land reform league, and others listened to what he said. Then, they all asked what about debt? George responded that debt was not a problem in America. But, the Europeans said it certainly is a problem here. Debt ends up loading down the economy with taxes and basically the tax growth in Europe was a function of national debt incurred in wars. Neither of these are part of the productive system. They were part of the parasite system living off production. Yet nobody at that time drew the conclusion that actually these were claims on production. So, I think the results of that -- if you want to carry forward George's spirit -- you have to develop these strains that he began to develop and see where they lead today, where no one a hundred years ago would have believed. Everyone, no matter where they stood in the political spectrum a hundred years ago thought things would turn out naturally, for the best and well. Nobody saw that there were many ways of being unnatural and that what we live in today is certainly unnatural and is not only an unnatural economy but one in which the problems no one anticipated to the degree they have developed.

TIDEMAN: I am afraid it has been too long since I have read the *Science of Political Economy*. I really cannot add anything to what these gentlemen have said.

DODSON: Would you add your perspective on George's overall system? How does it square with your understanding of economic principles and economic science? Do you feel as though he basically got it right, and we are in need of fine-tuning his work, or are there elements in this that are fundamentally off the mark?

TIDEMAN: When George was teaching himself economics, economics was just on the verge of some important new insights into how prices are determined, particularly prices for products and how the output is divided among wages, rent and interest. In economics this is called the "marginal revolution," and it occurred in the 1870s. And, George relied on the ideas of Ricardo and to some extent those of John Stewart Mill, and there really wasn't anything wrong with what Ricardo and Mill said, but the ideas that were new in the 1870s in economics provided an important generalization of the problems that rent is determined by the output on marginal land. It generalized that idea to show how you could look at prices of products generally and prices of factors of production as determined by what happened in marginal circumstances. And, I think that it is unfortunate that Henry George did not absorb that new learning that was occurring at the same time he was writing, because it created a gulf between him and other economists. But, at the same time there isn't anything wrong with what George did. He just did not absorb the generalization of the ideas that other economists were working on at that time.

LAMBERT: I would only add one thing, and that is that there were three economists who independently worked on marginal utility theory and came up with roughly corresponding theories. One was the historian Karl Menger, the second the Englishman Stanley Jevons, and the third was Leon Walrus, the Frenchman. And, he [Walrus] in fact – although he did not call himself a Georgist – specifically was very much a proponent of land value taxation. But, as Nic Tideman rightly said, one of the problems that George had in the *Science of Political Economy* is that the Austrians who we know were writing in the 1870s had almost none of their publications in English, so that when he is talking about Austrian theory in there (he doesn't talk for very long), he is talking about such ideas as he knows from secondary writings. And, I think there is a genuine misunderstanding there because he did not have more writings in English; and, vice verse, I do not think any of the Austrians had George's writings in German.

HUDSON: I would mention the gap that has certainly grown up and widened between George and the other economists. And yet, at the time John Stuart Mill supported the idea of land value taxation, he said: "here are people getting an unearned increment," as did Wolrath (sp?). Ever since, as I am sure most of you know from the mailings, many, many economists have endorsed taxing the land because you tax the unearned increment. And yet, they are not very interested in this. They grant that the principle is right, but they all had reasons for believing it is not as important as the other things that they have studied. So, what had begun as a central point of economics – through Ricardo and many others – the tendency for unearned increment to crowd out earnings, for unproductive income to crowd out productive income – has been dropped by modern economists.

Everything has been homogenized to a large degree. And, the fact that the Georgists are one of the few people retaining the classical distinction between productive and unproductive income -- or earned and unearned – had lead to this divergence and it has not been put back together.

TIDEMAN: I hate to take exception, Michael, to your statement that John Stuart Mill supported a tax on land. One might remember the qualification from what you said. And that is, John Stuart Mill said it was quite alright to tax additions to land value but you should not tax the starting land value. I think this inability to deal with the injustice of the past is something that pervades the response to Henry George. I think, as Henry George said, recognizing that land is our common heritage is very much like freeing the slaves. It is something that people find hard to realize is right because there is such strong self-interest involved in continuing to see the world in such terms as allow you to continue to get what you get without any work. And, I think that John Stuart Mill could not overcome that, and it is important to recognize that.

HUDSON: I think more he was being political. He realized well we cannot take away the vested interests as they are. We can't come right out and take what they already have. At least lets stop them fro getting any richer, and I think there were discussions at the time that may be after a hundred years we get to take it back. They wanted ... to tax the future increment in land value for society. That logically implies that the point does not have quite the public legitimacy of other forms in this country.

TIDEMAN: There are times when I have taken that tact, and I think it is worth developing just a little bit further. It is worth realizing now that if our forbearers had gotten John Stuart Mill's agreement or the agreement of society then that they would only let land rent be collected for another hundred years that by now we would be done. Maybe what we should do is try to get people to agree that, suppose we were designing society for a hundred years from now, what rules would you want, or a thousand years from now? Pick some time that is long enough in advance that they are not going to be concerned about the problem of transition. And then, after you get them to agree what the idea looks like, then ask them what is the most appropriate transition time.

HUDSON: Or, what if you asked: Suppose you were designing perfect rules for a hundred years ago. What rules would have produced a better today?

DODSON: I am going to shift gears a little bit, taking the prerogative of the moderator. And, the things I am interested in talking about. We will find out what you all think.

I, as a practical person not really trained in economics but working in the housing finance industry and business in general, I sort of observe how the market works, how people really react under different conditions – what interest rates are in the market, what demand is for goods and services, etc. And, one of the things that I feel as though we write about and need to talk about is the idea that, with regard to land, the price mechanism does not work. Everyone who has had Economics 101 (or 102 or however high) gets taught that the price mechanism in a market economy is the clearing device. And yet, inventories run in the face of that to me. For example, individual companies have a vested interest in keeping producing wights, whatever those wights are, and those wights hopefully have a home. At what price, the market will determine on a constantly changing basis. If the supply of wights is very high and there are too many wights on the shelf, what happens to price? Price comes way down. In fact, some prices come all the way down close to zero even though the cost of producing them was quite high. So, this element of the price mechanism clearing markets works very well for things that we produce and which are in a constant state of depreciation.

Wights depreciate very quickly. Computers are a perfect example. Five years ago I bought the best computer I could buy in the market and today – $6,000 later – it is totally depreciated and obsolete. I couldn't sell it for $200. There are computers hitting the market right now that will be obsolete by Christmas, Hanukkah or whatever ethnic holiday you want to chose. The land market is in my view one exception. That the price mechanism does not work with the land market because land doesn't depreciate; so, those with the deepest pockets in our society are able to keep land off the market for the longest because they don't need any cash flow. That is my observation. I would ask my discussants whether they think I am on the money.

TIDEMAN: I think that you are on the right general track, but I would put it differently. The question is not whether land is depreciable but whether land is producible, which is closely related but is not exactly the same. That interacts with another important aspect of the difference between the real world and the idealized markets that economists talk about. Economists often assume that people will be able to predict the future accurately. And, that doesn't happen with land. The fact that land cannot be produced makes it possible for people to have fantastic dreams about what land will be worth in the future. Economic theorists sometimes refer to these as "bubbles." There was the great South Sea bubble of about 1720 or so. The tulip bubble.

A bubble is a price that rises and rises for no good reason but keeps on rising because it is hard to come up with supply to meet the rising demand; and, people keep thinking that it will keep going up as it has in the past. People get these unrealistic expectations about land and it creates an artificial scarcity of land and inability to get land for productive purposes. And then, eventually you have some kind of correction to people's beliefs and a big crash. And, a lot of banks go out of business, and we tax ourselves to bail them out, and things like that.

So, if there is an important difference between land and other things, it has to do with the combination of the fact that land cannot be produced and people develop unrealistic expectations that get supported by markets for awhile and then we have these violent oscillations.

LAMBERT: It is an interesting thing that Ed has raised. I think as a lawyer the comment I would make is that when you talk of land as a thing that you can sort of give and take and use and transfer, but in fact you cannot do any of those things with land. When we are talking about land in this sense, we are really talking about rights over land, rights to use land in some particular way. And, those rights must have some time horizon. And, in the case of most freeholds, there is no ultimate time limit when you lose the title. But, not all land rights are like that. You could take, for example, a hotel room for an evening or a seat on an airplane. Now, those have a very short life span.

When you have a hotel room you are really taking a lease for some land for twenty-four hours. And, it is effectively a perishable and the clearing mechanism that Ed was describing does work to some degree with things like that. We all know that it is quite possible to get standby tickets at airplanes and hotels if you are prepared to go "right now" because any money made in the next twenty-four hours is well worth it given that tomorrow hotel rooms for tonight are already gone. So, it does work in that sense. And, the reason it doesn't work in relation to what we call the "land market" is that it doesn't work in relation to (what effectively freeholds are) very long leases. But, if this clearing mechanism takes time – this whole element of things being capable of being reproduced, of being depreciable – they depreciate or are capable of being reproduced over time. What Nic is talking about when he was talking about the tulip bubble is the fact that the tulip growers cannot get tulips on the market fast enough to create the extra supply because the demand has grown absolutely crazy. So, it is all related to time and what is the time horizon your land rights have. Then, if you get toward near the end, when you run out, that clearing mechanism may start to work. But it is never going to work for something that is an absolute title.

When there is an infinite time horizon and land doesn't depreciate and is not capable of being produced.

HUDSON: There is an accounting aspect to this. Any healthy society should be able to have a statistical picture of what is happening just as a doctor when he takes a diagnosis takes the blood pressure and other things. Land is not accurately reflected in our accounting system. Nor are the categories that economists use such as "rent" or "profits" or other categories represented by our accounting. The result is that since the 1950s, actually the 1920s, you have had an entire profession of brokerage house analysts scanning the balance sheets of corporations looking for undervalued property. And, the main undervalued property there is, is land.

They want to look for a manufacturing company that has a whole factory that really should be torn down and made into something other than a factory that is a luxury development. As a matter of fact, if there is no productive activity at all on the area it would be even better because he wouldn't have the costs of tearing it down.

You cannot look at a statistical picture of the American economy and see the under-utilization of land because you wouldn't have a need for the wonderful profession of analysts. As a matter of fact, if you look at the employment of the United States since World War II, you would see that all the growth in employment has been in what is called the "fire sector" -- finance, insurance and real estate, all benefiting from this invisible land appreciation process that doesn't seem to appear in textbooks and has no place in the economic curriculum and is difficult to locate in the national income accounts.

DODSON: I think what Michael is referring to is the source of leverage buy out activities that corporate raiders have been so successful in taking advantage of. I was going to say "capitalizing on" but I would rather say taking advantage of. It brings up the next subject that has always interested me. In fact, the first Georgist conference I attended I gave a presentation (I think it was in about 1984) on the "debt bomb." – the international debt bomb. What was going to happen. And, I was one of those who was very pessimistic that the international monetary system was on the verge of collapse. Lo and behold, the banks came up with a number of schemes that transferred debt from one to another and many of them have managed to survive.

We – as we are in some respects in my view the beneficiaries of the results of the fact that most of the international debt was in dollar denominations, so the less developed fourth world countries who owed debt to banks had to sell everything they could – their land, their crops, whatever they could get hold of to sell in order to raise revenue and pay the interest on their debt or restructure their debt with banks or the IMF. This game seems to be continuing now, and many other countries seem on the verge of very difficult economic circumstances because of the debt.

Some of us in the United States – not all economists – are very concerned that the national debt of the United States is fast approaching $5 trillion, and that the interest on that debt results in heavy taxation in order to maintain it in a constant refunding. I would ask our panelists to give me their thoughts on how important an externality do they see national debt and what do they see as the immediate consequences of hiding of this global problem.

HUDSON: I should probably speak first because I have written seven books on the subject of third world debt.

A topic that once again does not appear in the economic curriculum -- as a matter of fact it doesn't even appear on the side of the lender -- I got involved in the subject in 1964, when I was Chase Manhattan's balance of payments analyst, specifically dealing with third world countries. Every study that I did showed that there was not ability for any of these countries to generate more revenue. This made the international department head very unhappy, and the real estate man (who was getting promoted) making all of these loans.

David Rockefeller then came in and replaced George Champion as head of the bank and said: "Look, the State Department wants us to make this loan to Argentina. What do you mean they cannot pay?" We all went over to the Federal Reserve in New York, and the Federal Reserve man said: "Mr. Hudson, by your analysis, England is broke and cannot afford to pay." And, I said I cannot see how it could. He said: "England has been broke since 1945. How has it paid? We have lent them the money." Of course. "And we have to keep lending the money to friendly governments so that they continue to pay. We want to be good citizens and make money at the same time.We have a moral responsibility."

Well, David Rockefeller believed in this. That was the year that his brother, Nelson, said that New York State had a moral responsibility to repay the thruway bonds and real estate development bonds. When they defaulted two years later, he said: "Thank god we only have a moral responsibility and not a legal responsibility." Unfortunately, the banks were not able to claim that when it came to their loans to the third world countries. It was obvious from the very beginning that the third world could not repay their debts. That is why they took it on. The third world banks and the presidents of their countries knew that the attempts to repay debt far beyond their ability to pay would lead to a currency flight. Countries like Argentina would simply print the local money – the pesos, they kept changing the name of the money; but, whatever it was they would print as much as they needed to raise the dollars at some price, to repay their creditors. Why did they do it? Were they crazy? Well, not really.

Because they were not Argentina, or the third world as a whole, they were a particular class within the country. And, it was very well-known to the banks and to the industrialists and to the rulers that if you did print the money and ... your currency, that meant that labor unionization was not really a problem because what they were really devaluing was the price of your own labor. The price of world raw materials were fixed in dollars. They remained constant. The only thing that you could effectively devalue was labor. And, the method to devalue labor relative to other sources of production was to take on debt so far beyond the capacity to do so that your currency depreciated.

The relationship between debt and the ability to pay that you got the disparity that has lead to the bubbles in some countries with regards to many of the other problems. To read the economics books, you read a kind of Walt Disney story about why people borrower; they borrower because you calculate how much you can afford to pay and you are always able to repay it. But, in reality, most of the really dynamic changes in the world come from the inability to repay debt. Something happens. It is not well-known, for instance, that – well, many of you may be familiar with Malthus comparing the arithmetic rate of increase to the geometric rate of increase in population. What not many people know is that Malthus plagiarized this idea from a book by a friend of the American revolution, a reverend Richard Price, who was writing about England's national debt, forecasting in the 1770s with remarkable accuracy what would happen to the next 200 years (although he didn't quite mean to do this). He pointed out that if you had a penny saved at 4 percent interest (at the time it is price deferred), and you calculated it at simple interest, it would accrue to about 15 pounds; but, if this penny accrued at compound interest (that is, if you reinvested the interest every year) the value of this penny would be a solid sphere of gold extending from the sun out to the orbit of Jupiter.

DODSON: Then, I'll blame my ancestors for failure to properly invest.

HUDSON: That brings up a point. Obviously, somebody would save a penny at the time of the great spurt. Somehow, nobody has a sphere of gold extending out to the orbit of Jupiter. Why is this? Well, Price thought there was a wonderful way of repaying national debt. And, that we to start a sinking fund. You would appropriate a million pounds and you would just let it accumulate at compound interest until the magic of compound interest would repay the debt. Well, what England did was it had to go to war with Napoleon, and it borrowed the money again and again for military reasons, and it never did try this grand experiment in repaying debt with compound interest.

LAMBERT: I think the national debt is probably the biggest problem that faces the world today. We don't even have a proper handle on it in the United States. Because of what we have there and around the world – I see it in my legal practice all the time – is what is properly called "creative accounting." In particular, what is called "off balance sheet financing." I will give you a rough idea because I do not know how many people will understand this. If you have a holding company, for example, that has its shares posted on the stock exchange, it will have a number of operating subsidiaries doing a number of different activities around the world. If you were to draw up a sample set of accounts for that top company, the only assets it would show would simply be shares of stock in subsidiaries. Now, that is not much help to investors because they want to know what the real underlying activities are of the corporation. And, so the corporation is obliged to produce what are called "consolidated accounts." They are a kind of pass thru photograph. It is a kind of barren photograph that is taken at the top of the building that actually shows you what is happening at the basement or ground floor level and takes away all the intervening levels. They have to do that if it is a subsidiary of a controlling company, or something, and what has grown up is a huge industry of corporations that do financing transactions where they say, "We want this company to do something and, of course, we are going to tell you what it is going to do, but we don't want to own it because we don't want to have to include it in our accounts."

It means that accounts today are extremely misleading in some cases. It has become a real art form. How any accountant ...

DODSON: Or government agency ...

LAMBERT: Sure. It is the same sort of thing that is happening because as far as I can gather, every so often you have a problem like the savings and loan problem, you simply get it of the balance sheet and get it into some other agency's accounts. And, then magically it doesn't appear in your figures. It disappears into somebody else.

I think the situation is so bad that we have ourselves into the position that we have to keep lying to ourselves that it is not quite as bade as it is. There is a book by (I can't remember the name) ... it's a book called "***The Greatest Every Bank Robbery***," about the collapse of the Saving and Loan associations. And, one of the things that is mentioned and that I find deeply, deeply worrying is what were called "regulatory accounting principles."

Let me give you a brief idea of what we involved. If you have a loan of $100,000 outstanding but the borrower is paying you a very low fixed rate of interest, it may well be that loan to you does not really correspond to an asset worth $100,000. If you were to sell it, you would probably get $80,000. It is like selling a bond. The savings and loan associations were encouraged to off-load those badly performing -- under performing -- loans. So, you would have made a loan for $100,000. You would have sold it to somebody else for $80,000, and you would (in anyone's book) realized an immediate $20,000 loss. But, under regulatory accounting principles, you were not obligated to take that loss in the year that you made it. You were allowed to -- wait for this -- amortize the loss over the outstanding period of the non-existing loan. Which, basically means that if it has a 20 year track, you could take $1,000 a year for the next 20 years. It is one of the reasons why when they foreclosed on some of the savings and loan associations all these assets suddenly up and disappeared. In one minute they had millions of dollars wiped off their balance sheets because it was never really there.

DODSON: I just wanted to comment specifically about what Ian talked about -- because it is close to my pocket book. Another think that is going on in the banking industry (at least in the United States) is a very strong regulatory pressure -- post Reagan/Bush -- to mark assets to market value. This is extremely controversial because of the balance sheet implications. But, prior to the current regulatory environment exactly what Ian described took place. I do not blame the S&Ls -- as managers and as business persons. They were, in effect, forced by other circumstances into a lot of these actions. Approximately $300 billion left the thrift industry after the 1970 deregulation of interest rates and the creation of money market accounts. This also resulted in closing of your friendly S&Ls in all of the inner city neighborhoods and any neighborhood that had marginal business opportunities.

After the debacle that occurred and the estimated $1 trillion clean-up bill that we as taxpayers are paying (and will pay over time), the regulators were finally given a little teeth and the banks now have more pressure to mark their assets to market value. Their response, however, is that: "We don't know what the market value is of an asset until we actually sell it." And so, the debate continues over how this ought to be incorporated.

LAMBERT: Just one thing I would add. The regulatory accounting principles were specifically political creations, and almost all of the major accounting firms specifically criticized them and did not like having to use them, but were opposed by the Administration.

TIDEMAN: A couple of points I want to make. First, a kind of off the top of m head reaction to what Ed just told us about being unable to value things to market. One of the possibilities that comes to mind is to create a market in options in some of these things.

DODSON: There is a market in options, as there is market in national debt...

TIDEMAN: A bank could hold onto a loan while finding out what its value is by trading some kind of options on that specific loan.

But, I also want to get back to the problem of excess debt. As Michael said at the beginning, there are good reasons for going into debt as well as bad reasons for going into debt. You can go into debt because you are interested in undertaking a worthwhile project that you can provide benefits over a long span of time. Those future benefits will be able to pay back the loan with interest. And, a lot of cities and states have gotten into trouble over the last couple of hundred years in the United States by borrowing too much money and then going to the taxpayers and having to declare bankruptcy of one kind or another. And, through all of these experiences, we have come up with some devices for avoiding excessive debt. We require very often that the voters themselves approved bonded indebtedness of a city or a state. And, sometimes we require such approval to occur with the ...

It is interesting to ask what kind of... how much of the trouble of the third world debt would have been avoided if the only way a nation could incur the debt was to have a plebescite approval of the debt that was proposed. It seems to me that you might even argue that if a nation throws out the rascals (as, for example, in the Philippines when Marcos was thrown out), if you took a billion dollars and stuffed it in a Swiss bank account the people of the Philippines should not have to pay that back. If people would lend whatever money, international agencies would lend them without regard whether it was in the interest of the citizens, the citizens in bringing in a new government might be able to say: "We didn't approve those loans. There is no reason why we should be taxed, our wages should be taxed, in order to pay them back."

HUDSON: There is an illusion that is always necessary to avoid and keep in mind. Most people think that the reason you go into debt is because you borrower the money. That is the reason the government goes into debt. It borrows the money, maybe to advance programs. But that is not the reason that most debt occurs throughout history. Debt simply accrues interest.

If you look at the United States budget, almost the entire budget deficit in this country each year is interest payments on the past debt. In effect, what America does is borrow the money to pay the interest; or, it lets interest simply accrue and by paying the interest it puts the money into the monetary system that is then recycled into acquiring new debt. America in this sense is joining the ranks of Brazil. I mentioned the meeting at Chase. Brazil was notorious for saying: "We are going to borrow every year and keep on borrowing the interest. At some rate of interest you will always lend us the money." That worked until 1983, when the money was no longer available.

In this country, we are having this debt grow by accruing the interest. And, as a matter of act if you look at the United States economy, all the savings in the American economy – and, in fact, the only savings in the American economy – are the accrual of interest to holders of money capital; that is, holders of bonds, mortgages, bank loans, etc. Most of the American economy, 95 percent, are not net savers. They save nothing at all over and above their going into debt. Each year the debt for the private sector – for the corporations, for individuals – the debt goes up more than savings. So, all of the savings that are jumped on by the security holders (and this includes the institutional investors) have the interest accrue. So, it is not really a borrowing process at all. It is not as if money were advanced to somebody for use in investing in something that can repay the debt. It accrues.

LAMBERT: It is like a credit card you cannot afford to pay?

HUDSON: That is correct.

DODSON: Well, you have all patiently sat there. I didn't see very many eyes closed, so hopefully we have covered some topics of interest that have stimulated your thinking. We will now take some questions.

AUDIENCE: What is the difference between "earned" and "unearned" income?

HUDSON: The beauty of the difference is that it can be whatever you want it to be.

DODSON: That is the economist's answer. And, now, he will answer on behalf of humanity.

HUDSON: I think unproductive is when somebody earns an income without being part of the productive process. In most of Henry George's literature and the writings of mostly every other economist, they talk about the factors of production and they talk about the rewards to the factors of production – land, labor and capital. That is all clear. But what about taxes? What about interest? What about criminal profits? What about all these ways of making money that have nothing to do with the productive processes that are claims on production?

DODSON: I use this in teaching. The most distant relationship between production and services is perhaps the professional musician or athlete. These individuals certainly do not produce wealth. But, I note that after I watch Monday night football, the next day I am psyched up and ready to go (if my team has won). So, I get great... my own production may increase because of the services the entertainment services of some other individuals.

AUDIENCE: Does Michael Hudson think there will come a time when the interest on the debt exceeds the ability of government to raise revenue to pay the interest? Rephrased, the interest will exceed taxes unless they raise taxes by 100 percent.

HUDSON: And, will this lead to bankruptcy? The answer is no. First of all, if you go bankrupt, you wipe out the debt. It is a wonderful thing to go bankrupt if you are a debtor. You wipe out the debt and begin with a clean slate. I don't anticipate the United States doing that by 1995. Also, the United States is very different from other debtors. The United States cannot go bankrupt. You can simply print the money. And, you can print as much money as there is, if you control the printing presses, than if you are a corporation or an individual.

DODSON: I think you will definitely bankrupt the creditors, but the government may go on and on for a time.

AUDIENCE: What does Michael mean when he uses the word "profits" as distinct from the Georgist definition of "interest"? Or, is there a distinction? And "money capital" as well.

HUDSON: By "profits" I mean the earnings on physical capital and enterprise. These profits are known only after the fact. You don't know them beforehand because you are taking a risk. Interest is a claim on money advanced or the value of money advanced which is stipulated in advance regardless of the rate of return.

The profession now distinguishes between these two forms of what used to be called "interest" and now distinguishes between profits and interest; but, in the national income account you will have profits reported to the government. Interest is considered a tax deductible expenses. Profits are what is left after taxes. So, by law, these interest and profits are distinguished in our tax code and therefore used that way by the economics profession.

TIDEMAN: Well, I think there is an important difference between accounts and economists in the meaning of the word "profit." I think that what Michael has given us is the economic definition of profit. Profit is the return you receive on your investment. Whereas, an economists is inclined to separate out this amount of money into two parts. One part is what the economist calls "interest" -- the ordinary expectable return on the money that was invested. To an economist, profit is the unexpected part which could be positive or negative and averages out to be zero. So, in the way economists use the word "profit" is something that only happens as a result of our inability to foresee the future and the ordinary profit is zero and the expectable return is called "interest."

AUDIENCE: What is your definition of "money capital"?

HUDSON: The amount of bonds, the amount of mortgages, the amount of debt claims. Anything, any instrument or security which yields a stipulated rate of return.

LAMBERT: I think that "money capital" is ... if you remember, George said money was not capital at all, and he talks in ***Science of Political Economy*** about value from production and value from obligation. And, he says that when you look at the overall economy, anything which represents an obligation effectively nets out because there is an obligee and an obligor -- a debtor and a creditor. Money is not capital but because people think of money certainly in casual terms as capital and as an asset, anything like stocks and bonds and cash is traditionally thought of as a capital asset and called money capital to distinguish from physical capital.

AUDIENCE: What political reforms do we feel are necessary to help us in the economic area?

HUDSON: I think the tragedy of our time is that our economic environment does not steer wealth to be invested in ways that increase the productive resources and well-being of our society. Now, of course, when you talk about production, there are many grey areas here (which is why I did not want to discuss it). But, you can go further. You can say that the way our society operates is to create an economic environment where the fastest way to get rich is to be a landlord, or to buy underdeveloped land, or to be a creditor or to be a corporate raider. I think that all of us would agree that whatever productive or unproductive enterprise or labor is, these are not the most productive ways of developing an economy. And, yet that is the way the political system has created an environment in which enterprise operates.

DODSON: I would comment this way. It has a lot to do with the comments we heard earlier. We heard yesterday about the attitude that the United States is founded under perfect principles, when we know that the system is flawed. Is, that anyone here who really believes we live in a society with anting close to full participatory democracy? That ought to be our objective. Certainly, mistakes will be made under participatory democracy. Nic specifically referenced having citizens approve spending and approve borrowing. Right now that is done in some cases but not very often. So, we need much stronger participation in the governing process. I personally am a strong advocate for cleaning the House every so often. Let's have term limits and make our politicians representatives of us rather than full-time bureaucrats or virtual holders of office. ...A balanced budget amendment. All these things ought to be in my view seriously considered by us as an electorate, so that we take control of society and not let a small elite of the most wealthy, the most powerful, maintain control of our destiny.

LAMBERT: I think one of the first things that ought to be done is to say that, if government wants to borrow, for example, without the kind of plebescite Nic suggested, to have a constitutional provision that there has to be "limited recourse borrowing," which means the monies have to be used for a specific purpose and the recourse of the lenders is limited in getting repaid out of the particular assets or enterprises into which the money is put.

It basically means that the Philippine people can say to Chase Manhattan, "you go and try to find out where Mr. Marcos put all that money. If you can find it you can get repaid. But, we are not paying out of taxes levied on production."

TIDEMAN: I wanted to answer Floyd [Morrow's] question by saying that it seems to me that we want to further the distinction that Henry George began to develop in the tenth book of ***Progress and Poverty***; that is, the distinction between acquiring wealth by producing something and acquiring wealth by arranging for something that is already been produced to come to you instead of somebody else.

I think we need to call attention to that distinction as a very important moral distinction. At the same time, we have to recognize that when we do so, we have a bit of a problem because we are saying that something that would otherwise belong to landlords ought to belong to everybody. So, we have to be somewhat more complex and say that the basic principle is that everybody gets to keep what they produce; and, we have an obligation to share that which nobody produced. And, the redistribution that is involved in that transition from the existing order to one in which we share the proceeds from that which nobody produced is governed by a principle that we all ought to accept and is fundamentally different from the kind of activity that economists call "rent seeking," which involves arranging for laws to be made that you benefit at the expense of other people.

AUDIENCE: What is your definition of land value in the context of George's tax principles?

TIDEMAN: I want to take the first shot at that one. It is necessary to distinguish between the rental value of land and the sale value of land. The sale value of land is what you can get for land if it is unimproved and you put in on the market. The rental value of land is what somebody would be willing to pay for the use of the land for one period of time -- a year -- if you could renew the lease in the future on whatever terms comparable land would be rented for elsewhere. So, when people say the value of land, what they ordinarily mean is the sale value of land. And, the simple way to implement Henry George's idea is to have a tax on the sale value of land.

But, a full implementation of Henry George's ideas would involve collection of all the rental value of land, which would drive the sale value down to something close to zero. And, then, you would have to shift your basis of taxation from sale value to rental value in order to make it work as your drove up the tax rate. But, it really isn't all that difficult to do that administratively. You just have to recognize that in the limit, as a percentage of the rent approaches 100 percent collected by the government you need an arbitrarily high multiple of the sale value to collect that revenue. But, the value of land is what land itself is.

HUDSON: You could say that the disparity between the sale value of land and the rental value is the definition of the public. And, in the Henry George News that will be available later this afternoon, there is an article on that very subject as it applies to Russia.

AUDIENCE: Common Ground has urged a separation of the budget process for government between capital expenditures and operating expenditures. What does the panel think about that?

HUDSON: It sounds like a wonderful idea in principle. But in New York City they tried that and they seemed to call everything capital. And, you can call everything capital in the sense that everything somehow feeds into the development of society. So, they have been using their capital budget for all sorts of operating expenditures for years. So, you have the problem that the gentlemen from Pittsburgh mentioned earlier today; the problem is in the administration of this principle.

DODSON: I have one thought, politics aside, that grows out of my own experience in mortgage finance. One of the innovations in the mortgage finance industry has been what some of you may know as the "mortgage backed security." And, basically, as an investor you buy a security that has a constantly decreasing principle, or face value. Every time people make mortgage payments you get principle and interest back.

I would suggest that one way to finance capital by government would be by a mortgage backed bond that would fully amortize, so that by the end of the life of the capital infrastructure the whole debt would be retired and there would be no principle to be refunded by a new debt issue. And, the principle and interest payments due on that bond could be by statute collected on a balanced budget basis through taxation. That's just one idea. ...

AUDIENCE: [to Ed Dodson] Did you intend to mean that by limiting the term of elected officials you limit the term of bureaucracy?

DODSON: I was speaking directly about elected officials. If, however, you have some ideas about limiting the tenure of bureaucrats I would be glad to support you.

AUDIENCE: There is a certain distinction between paying taxes on earnings from investment in equities versus taxes paid ... [rephrased] Will we be successful in convincing others if we do not emphasize the moral principle that we all have an equity interest in the earth?

TIDEMAN: I think that Steve Cord is showing that it is possible to make progress without convincing people on a moral basis. But, I also think that if we are ever going to tax land to the point where we seriously reduce its value, we are only going to make that acceptable by getting people to agree that land is our comment heritage.

DODSON: My response is that I am a Georgist because I am looking for moral justice in the world and ethical systems of government and for living. Taxation is just a means to help us get there.

AUDIENCE: [Jerry Shaw] Do we talk about taxation when we talk to people about how to positively improve things?

TIDEMAN: It depends on how much of a hurry I am in. I often do take the time to say that I am not talking about a tax. But, sometimes the only way I can make a point is to use the traditional language.

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