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COMMENTARY ON PROPOSALS TO IMPROVE THE ECONOMY BY REDUCTIONS IN TAXATION AND THE POWER OF BUREAUCRACY, BY THE INSTITUTE OF ECONOMIC AFFAIRS

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Introductory

In general, the proposals of the Institute of Economic Affairs are very simple, amounting to nothing more than the application of good housekeeping or efficient management to the government of the country and the confining of governments to their proper functions.

This policy is really a revival of "laissez faire", resurrected from the 18th and 19th centuries. The production of wealth at that time increased enormously, but this did not benefit the non land owning working class. It would be even less likely to succeed today because of the tremendous advance in science and technology and the consequent rise in economic rent. The maldistribution of wealth would worsen, together with unemployment and inflationary pressures.

It is proposed that there should be a substantial reduction in taxation, but there is no objection to the present basis of taxation other than the correction of certain anomalies. Colin Clark considers 25% of personal incomes is the maximum that can be taken in taxation without affecting incentive. This would amount approximately to a 50% reduction.

Of necessity, governments would have to recede from many of the present activities which include health, education and welfare. It is also proposed that pensions ultimately should be phased out.

With such objectives, the Henry George Movement is in general agreement, provided the need for the expansion of government declines simultaneously.

We believe, however, that unless there is a radical change in the basis of providing for the services of government, which is no where apparent in the proposals of I.E.A, that its objectives are not within the sphere of practicable politics. In fact, economic and social problems would be more likely to increase rather than recede with the application of its policies, desirable as these may be. This can only be demonstrated by a statement of principles and a study of cause and effect based on a knowledge of the science of political economy.

1. Wages tend to the minimum that men will be prepared to accept.
2. Wages are higher in newly civilised countries where there is less competition for the use of land and the margin of production, therefore, is higher. Wages are lower in older countries where the margin is lower and rent is higher. This is an observable fact.
3. The bargaining power of the land owner is greater than that, either of the labourer or the capitalist.

4. Factors which increase economic rent are :
   (a) Population increase.
   (b) Advance in science and technology.
   (c) Advance in manners and morals and the art of government.
   (d) Withholding of valuable land from use.

5. Taxation of monopolies can not be passed on, as it must be assumed that the full value of the monopoly is already being exploited. Taxes imposed on monopolies, therefore, must lower the value of the monopoly. The exclusive occupation of land is a monopoly.

6. Taxation, which bears on the rewards of labour and capital or the processes of industry, is passed on to the consumer.

7. If the consumer attempts to pass the tax back to the producer (assuming the return to the producer is the minimum he is prepared to accept) then the incentive to produce declines and production is marginally reduced.

8. Wages, the minimum that men are prepared to accept, is the net return after tax, and interest, the minimum return after tax.

9. Taxes, in theory, must be at the expense of rent, since the labourer and the capitalist will not accept a lower return.

10. The minimum standard of returns for labour and capital are fixed by competition.

11. Wages and interest increase marginally with the advance in science and technology because higher social standards are set, e.g: the use of motor cars, refrigerators, vacuum cleaners, radio and television sets are now accepted as necessities.

12. Taxation can not, always, be passed on to the consumer and from thence to the land owner in the case of export industries. This depends on accepted minimum standards in the importing countries and the international level of competition.

13. To the extent that taxes can not be passed on, either rent, in the exporting countries is reduced or production declines.

14. Consideration must be now given to the effects of a reduction in the high level of taxation but without any corresponding collection of land rent for revenue, which is the crux of I.E. A. proposals.

15. If taxation (other factors being equal) is at the expense of rent, it follows that a reduction in taxation must be to the advantage of rent.

16. It is necessary to consider how funds previously confiscated by taxation, if allowed to remain with the producer, otherwise would be spent. It is axiomatic that a greater proportion would be spent on goods and services for the satisfaction of desire of the producer, than if spent by governments.

The alternative avenues of spending are as follows :

(a) On consumer goods.

(b) On services, travel, entertainment etc.

(c) On capital for the ultimate production of more wealth.

(d) On investment in land.

17. Items (a), (b) and (c) call for a greater use of, and therefore, demand for land. Accordingly rent would rise and wages and interest would fall as a proportion of production.

18. Item (d) would result in a greater demand for land and a reduction in the supply of available land, also causing rent and land prices to rise.

19. The greater demand for land on a rising market would induce speculative investment and, therefore, the withholding of some valuable land from use. Rent would rise and wages and interest fall, as a proportion of production.

20. In the foregoing, it is assumed that there would be no additional collection of economic rent for public revenue; the reduction of taxation would be met therefore from a reduction in government services and public spending.

21. No consideration at this stage has been given beyond, or outside, the operation of natural law and free market competition.

22. It is, however, necessary to consider the short term affects of artificial legal restraints to the free operation of market forces.

23. Henry George has demonstrated that real wages can be increased by combinations of workmen creating monopoly conditions in some industries which flow on to some extent in all industries because of social pressures established in the privileged industries raising the level of minimum standards of living generally.

24. George, in his day however, was not faced with labour union monopolies developing wage structures beyond the earning capacities and beyond the willingness of consumers to pay.

25. This must cause secondary unemployment.

26. The primary cause of unemployment is due solely to the withholding of valuable land from use and the margin of production thereby being forced to lower levels than labour and capital will freely consent to use.

27. It is also true that other monopolies such as protective tariffs secure greater returns to investors than could be obtained in the free market. There is, however, a restraining influence; if the monopoly is extended beyond what the market will bear, the net return, actually, will be reduced.

28. This consideration does not seem to apply, to the same extent with labour union monopolies, under which, excessive demands result in unemployment, which appears to be ignored by those responsible.

29. The foregoing from Clauses 21 onwards, are stated as a background to determine whether a reduction in the high level of taxation would in fact raise real wages.

30. The first effect of lower taxes would be to cause prices to fall but artificially fixed wages and monopoly induced returns would not fall correspondingly. Real wages and the returns to capital, therefore, would increase.

31. There are, however, many activities in open competition such as rural and mining industries and the plight of self employed people generally, which would feel the effect of increased competition due to the greater capital investment in their industries.

32. There would be some benefit from lower prices caused by increased competition.

33. There would be an opposite effect to increase prices because of the greater demand caused by the short term rise in real wages and returns to capital.

34. Economic forces, however, would very soon respond to rising rents and land prices generally and the net effect of taxation reductions would not greatly effect the returns to labour and capital which, as noted, tend to a minimum.

35. Because of the inferior bargaining position of labour and capital as compared with the land owner, there can be no general improvement in real wages or real interest until the bargaining power of labour and capital improves in relation to that of the land owner.

36. This will hold, what ever the level of taxation or the efficiency of governments.

37. The foregoing arguments are theoretical and abstract and for this reason many people might not be impressed, notwithstanding that these are entirely consistent with the writings of Henry George and Ricardo's law of rent. It is nevertheless necessary for the political economist to understand the theoretical reasoning pertaining to his profession in order to be able to make economic forecasts and be in a position to advise governments.

38. Getting down to practical considerations, a substantial reduction in taxation is a "pipe dream" which can never eventuate under present circumstances. The theories of Fisher, Mises, Hayek, Friedman and others will never be called upon to stand the test of application.

39. The reasons being that the disparity betweeen the highest and the lowest incomes would increase as the rewards arising from land speculation increased, due to the greater efficiency of governments proposed by I.E.A. See Clause 4 (c).

40. Governments relying on disincentive taxation for revenue would not be able to balance budgets and inflation would be inevitable. Governments which tried to abolish inflation under such circumstances could not survive.

41. Such conditions, set against a background of a worsening maldistribution of wealth, would play into the hands of communists and subversives generally.

42. The same conclusion can be reached by an entirely different process of reasoning which is herewith developed.

43. When economic rent is appropriated by land owners who, as such, return no equivalent value in goods and services, notwithstanding that they have enormous purchasing power, the function of the monetary system becomes unbalanced, especially in a rising or inflationary market.

44. Let it be assumed that the value of production arising from labour and the investment of capital is 600 units of wealth, and that the value of rent arising without any contribution to production from land owners is the equivalent to 200 units of wealth.
Then purchasing power must be provided entitling total claimants with 800 units of value to 600 units of wealth.

45. Wealth producers with 600 units of value must receive a proportionally lower return in order that non producers may appropriate one third of their earnings.

46. Notwithstanding that the 200 units of economic rent were not created by the land holders, as such, these do represent value in the processes of production.

47. The people collectively (the 600 unit holders) create the value of 200 units of rent which should be returned to them through the services of government, by the collection of economic rent for revenue; and not to a non productive class of land owners.

48. Rent would continue to increase as population increased, science, technology and the art of government advanced, and as disincentive taxes on the processes of production were remitted but such increases would accrue to the people collectively and not to non producing land owners. On the other hand, rent would fall as it became no longer profitable to withhold valuable land from use. Wages and interest would rise. See Clause 4 (d).

49. Although rent would continue to increase with economic progress as a proportion of production, it does not follow that wages and interest, although falling proportionately, would fall quantitatively; on the contrary, such would rise because of the abolition of disincentives to work, to invest and to become enterprising.

50. There is a further consideration that would introduce new relationships in the distribution of wealth. The bargaining power of labour and capital would improve in relation to the land owner. The people collectively through their governments would be the owners of economic rent. Land price would disappear and the land would be held in trust by governments for all people, for all time as their means of subsistence. Land holders would continue as title holders which would ensure property rights to improvements, subject to their obligation to pay economic rent.

51. The State would have no interest in future values, or speculative investment or to extort such from producers. It would collect current value only for revenue and on a 'pay as you earn basis'; not as capitalised "interest" bearing land price.

52. That part of the rent fund now included as future value, would transfer to the rewards of labour and capital, and the State would be able to reduce many of the charges now passed on to taxpayers, from its buoyant revenue from economic rent.

53. Labour would no longer be faced with the spectre of unemployment and capital with the problem of replacements unsupported from earnings. People would work hard or enjoy leisure or invest in capital enterprise as they chose, in the certain knowledge that employment was always available to them.

54. Then and then only, would the cut throat competition of labour within its ranks be reduced and the bargaining power of labour improve.

55. The same would apply to the employment of capital. A greater proportion of wealth would be diverted to cultural pursuits, reducing the investment in capital to its required limits, eliminating the over investment and consequently the cut throat competition.

56. A further advantage is that government borrowing,for other than real interest earning requirements, would cease.
The money market is distorted by fictitious "interest" payable on government borrowings unrelated to the use of capital. This at present is unavoidable because of inflation, disincentive taxation and the costs of financing the Welfare State, made necessary because of unemployment, poverty, crime and injustices arising from the maldistributio of wealth, in disregard of the equities involved.

57. The fictitious interest paid by home owners and industry generally on land price also would cease and be replaced by 'pay as you earn' economic rent to the State. This would indeed be considerably less than the present scale of taxation.

58. Above all, the incentive to work and achieve would be restored and the host of non productive bureaucratic officials, inseparable from the present system, would be available to the productive work force.

59. It has been demonstrated that a reduction in taxation under the present system of land tenure, can have little permanent beneficial effect on real wages or the real earnings of capital. This can only come from the collection of economic rent for revenue and the abolition of all forms of disincentive taxation.

60. Until such time as these reforms are effected, the bargaining power of labour and capital will remain inferior to that of the land owner and the present form of servitude must remain.

61. Until the reforms we propose are initiated, there can be no means of checking or even preventing the expansion of government sponsored bureaucratic dictatorship in this country, no matter which of the political parties occupies the Treasury benches or what palliatives are attempted.