People's Budget

THE PEOPLE

Land Research Trust

A budget for the people

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Why did HM Treasury treat this man as if he was insane?

Because, for 30 years, he championed the economics of a fair and efficient fiscal policy:

" It worries me...that we don't have a land tax. In a sane world, we would have a proper land tax. Sadly the only person to try it was Lloyd George and he ended up having to pay every single penny back."

Lord Macpherson

Permanent Secretary to HM Treasury (2005-2016)

NICK MACPHERSON

TONY BLAIR

Who's insane?

Nick Macpherson was one of HM Treasury's most talented economists. He had one problem: a social conscience.

During his 30 years at the centre of fiscal policy-making he tried to explain that a tax on transactions (such as VAT on the sale of goods) was "pointless" (his word). So was taxing capital: its mobility meant that owners could escape their fiscal obligations.

Taxes on transactions and on the ownership of capital deprive the public purse of revenue. They also damage productivity. Economists have a term for that effect: *deadweight*.

As the UK's productivity slid in the last decades of the 20th century, and the real value of take-home pay faltered for the majority of people, remedial action ought to have been a priority.

"This country is crying out for tax reform," Macpherson declared at a Resolution Foundation seminar on October 24, 2018.

But despite Macpherson's interventions, his political masters refused to listen when he explained the need for "a sensible property tax system".

And when he tried to engage them in a discussion on the land tax, "everybody just looked at me as if I was insane" (RF 2018).

He was eventually elevated to the House of Lords by David Cameron, where he now sits as a cross-bencher.

Macpherson's insight into the attitudes that prevailed within the Treasury affirms the suspicion that the UK cannot rely on Whitehall for leadership in the realm of fiscal policy. The treatment of the Permanent Secretary – the top civil servant – as if he was insane is an indictment that needs to be forensically interrogated by the House of Commons Treasury Select Committee.

It explains the failures of governance during the years of Tony Blair's experiment in Third Way economics. A failure for which there can be no excuses.

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Irresponsible governance

SOME RECESSIONS are random events. Others are written into the DNA of the economic system, which is why they are repetitive.

And predictable.

History teaches us that a recession strikes mid-way through the 18-year business cycle. The last one was the dot.com boom/bust of 2000-2001 (driven by speculation in the rents of the electromagnetic spectrum, without which the business models of corporations like Amazon would be worthless).

That crisis could have been avoided. In 1997, the Treasury's two top policy-makers – Gordon Brown (Chancellor) and Alistair Darling (First Secretary) – were alerted to the boom/bust cycle that would terminate in 2010. A briefing paper to Brown, dated November 1, explained:

> **"Under existing strategies, there will be a mini boom/bust in the lifetime of this Parliament…followed by the cyclical Big One after the next general election… there is nothing in the policies of New Labour that would obviate this outcome."**

A warning in similar terms was written to Darling on November 13 (Harrison 2010: 9-10).

As the UK swept through the cycle, Brown kept promising Parliament: "There will be no more boom/busts".

We now know, based on the testimony from Lord Macpherson, that the Treasury would not countenance counter-cyclical action to save Britain from the dot.com crisis of 2000 or the banking crisis of 2008. *The price was paid by the people* in the form of a decade-long austerity from which the UK has yet to recover.

GORDON BROWN

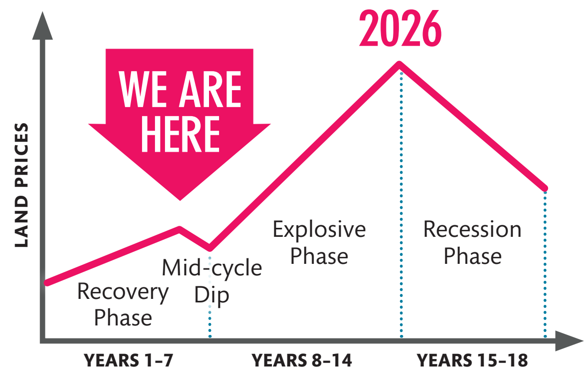
ALISTAIR DARLING

At the end of that last cycle (2010), it was possible to forecast that a downturn would strike in 2019.

A responsible government had eight years to construct defensive barricades against a mid-cycle recession.

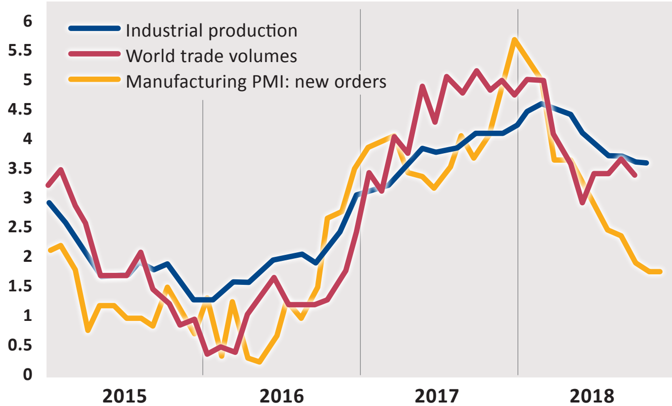
The UK is poised at the point of a downturn (Graph 1). So are the other economies. According to the IMF, the global indicators now point to a recession within the next 12 months (Graph 2). Understanding how this could have been avoided provides an insight into how to avoid *future* recessions.

Graph 1. Where are we in the 18 year land-led cycle?



Graph 2. Slowing down (IMF)

After rapid growth in 2017, industrial production and trade have slowed, and business confidence has fallen.
(percent change, difference from 50 for PMI)



Such strategic thinking runs counter to the culture of HM Treasury.

A plan to ring-fence the UK against the explosion of the financial sector could have been constructed under the guidance of Nick Macpherson, who by then had been promoted to top civil servant in the Treasury. That would have fulfilled the Treasury's purpose as steward of the nation's finances.

That this did not happen ought to be the subject of investigation by the House of Commons Treasury Select Committee.

It didn't happen, but the lost opportunity needs to be brainstormed as a learning exercise in how to avoid future recessions. The elements of a coherent strategy would include the following reforms:

- **2008:** bank seizure: a rescue operation that accepted them into public ownership, to safeguard depositors but penalise shareholders who profited from sub-prime mortgage speculation.
- **2009:** as the alternative to "austerity", renegotiate terms of sub-prime mortgages, to secure families in their homes;
- **2010:** launch new fiscal strategy, beginning with
  - transforming the residential property tax to one based on the annual rental value of land; and
  - initiate the revaluation of commercial property locations.
- **2012:** Halve the rate of VAT, to raise real value of lowest incomes; replacing revenue with a reformed charge on commercial location values.
- **2014:** Halve national insurance charges which damage employment, and raise revenue from an increase in the rate of the Annual Ground Rent.

Such a programme would have required all-party consensus. A political coalition around this rescue operation would have relieved the UK of immense social grief. The impacts from serving the national interest would have been many and varied. To cite just two outcomes:

- accelerated house construction, to remedy the deficit in the property market: rents would have adjusted to affordable levels;
- forestall the rise in land values, avoiding the speculation in property that triggers the mid-cycle recession.

The tax burden

This plan for a post-crisis recovery is based on a revenue neutral approach to the public's finances, an approach opposed by those who claim that the tax-take is excessive. This is one of the false doctrines that shape the guidance offered to government ministers by the Treasury.

According to the Taxpayers Alliance, the tax burden in Britain has reached a near 50-year high, having increased to 34.6% of GDP for 2018-19. The bottom 10% of earners pays 49.5% of income in tax (TPA 2018).

These fiscal outcomes rest on crude doctrines about the public's finances.

What matters is not how much, but how, the revenue is collected

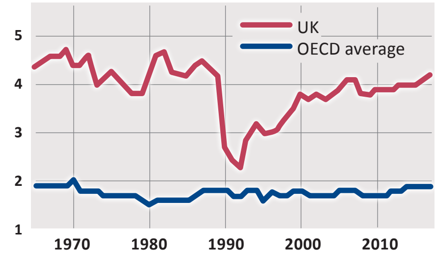
How the revenue is raised determines

(i) whether people are receiving the services they need, for which they are willing to pay, and

(ii) whether government is supporting or burdening the population...

As evidence of over-taxation, critics compare the UK's property tax with the OECD average (see Graph 3).

Graph 3. Property tax revenues as % of GDP (OECD)



In reality, property is the most cosseted of all assets. This explains why, no matter how many houses are constructed, affordability will remain a problem for the bottom half of income earners. But to establish the facts, we cannot rely on the advice of even the most high-profile economists. People like Arthur Laffer.

The Laffer Curve

ARTHUR LAFFER

He drew his curve on the back of a serviette for Ronald Reagan. Arthur Laffer, an academic in California, had read a book called *Progress and Poverty* by Henry George, a 19th century social reformer. And he seized every opportunity to explain to politicians that bad taxes were a brake on productivity.

His curve was meant to demonstrate this fact for the Hollywood actor turned president of the United States.

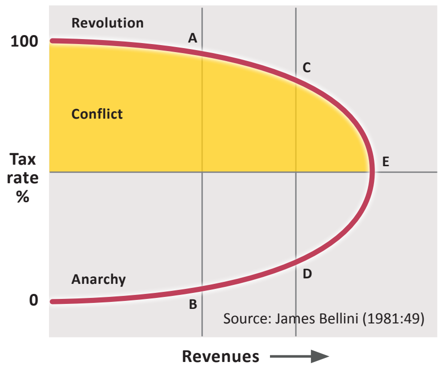
But there was one problem with the advice Laffer offered: *he remained silent on the correct way to raise revenue*.

Henry George had emphasised a theory that was solidly established in the literature: that the optimum way to fund public services was out of the rent of land.

HENRY GEORGE

Laffer understood this, but he chose not to say so at his private lobbying meetings with policy-makers, or from the public podium. Not in the 1980s, and not now, as an adviser to arch land speculator-turned President Donald Trump (Moore and Laffer 2018).

The Laffer Curve



So the Laffer Curve entered the textbooks as a cute way to justify the reduction in revenue from bad taxes. President Reagan bought into the idea Big Time. He liked the narrative.

- If the tax-take was too low, there was anarchy.
- If the tax-take was too great, there was conflict.
- Pitch the tax-take at the right level (at point E in the graph above), and all was well.

But because Laffer failed to stress that the balanced – sustainable – strategy was a *shift* away from taxes on earned incomes, and raising revenue from the rents of land, the rich got richer from tax cuts. Inevitably, *the poor got poorer*.

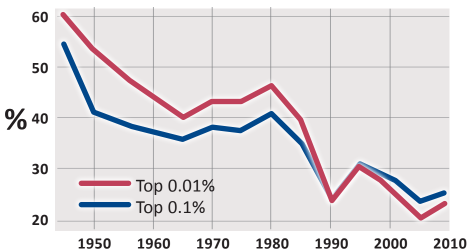
RONALD REAGAN

GEORGE H W BUSH

During the presidential election of 1980, Reagan was accused of employing "voodoo economics" by George H.W. Bush.

The US paid a heavy price for its misaligned fiscal policy. During the Reagan presidency, while the top marginal rate of tax fell from 70% to 31% (see Graph 4), the national debt grew from $997 billion to $2.85 trillion. The U.S. moved from being the world's largest international creditor to the world's largest debtor nation.

Graph 4. Average tax rates for the highest-income taxpayers, 1945-2009



David Stockman, Ronald Reagan's budget director during his first administration, maintained that the Laffer curve was not to be taken literally. In *The Triumph of Politics*, he wrote:

> **"[T]he whole California gang had taken [the Laffer curve] literally (and primitively). The way they talked, they seemed to expect that once the supply-side tax cut was in effect, additional revenue would start to fall, manna-like, from the heavens".**

Donald Trump revived that delusion.

A conspiracy?

Economists like Arthur Laffer, who choose to remain silent about the optimal tax policy, contribute to the zeitgeist that lends itself to conspiracy theories. Are there sinister forces at work to manipulate fiscal policy?

There is no need to indulge in conspiracy theories. The explanation is mundane. Rent-seeking doctrines dominate policy-making in the realm of economics, especially the discourse on taxation. This explains why the data on which to reshape policy is fatally flawed. For example, *for good governance people need to know* both

- the rate at which deadweight taxes deplete national assets, and
- the impact of sovereign debt on the net wealth of the nation.

According to the IMF, filling the gaps in government data is "doable". Governments, it declares:

> **"...should start by bringing data together to come up with a rough estimate of public sector assets, liabilities, and wealth. Over time, better accounting and statistical collections can improve the accuracy of these estimates. Governments can use them to do basic balance sheet risk and policy analysis... Once governments complete this exercise they *will be able to show their citizens the full extent of what they own and owe, and better use public wealth to meet society's economic and social goals*."**
>
> (IMF 2018)

There is a risk with assembling such information, however. It eventually leads enquiring minds to ask: *Is there an alternative to deadweight taxes*?

Democracy is debased when decisions are made without full transparency. But governments which need to avoid accountability must, out of self-preservation, impose limits on information available to their electorates.

Who, for example, should be held responsible for the coming recession? That question is difficult to answer if the policy-making footprints have been camouflaged by finance ministers who treat their informed advisers as if they were insane.

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Democracy Depleted #1

New Zealand

COLONIAL settlers had no choice: if they wanted modern infra-structure, they had to fund such investments out of the rents which they created. It was by this means that a modern European nation was constructed in New Zealand.

The 150-year NZ history of land valuation and rent collection provides a remarkable record of the economic strengths of collecting public revenue direct from a nation's taxable income, and the vulnerability of democracy to the culture of *rent-seeking*.

By 1982, 90% of municipalities had adopted land value rating, raising 80% of local government revenue. This outcome was the will of the people: "[W]herever land-value rating applies, it has been adopted by poll of ratepayers".[1]

Political sabotage came in the form of the Rate Payers Act (1988-89). It *withdrew people's right to hold a poll* to determine the nature of the property tax. Democracy was depleted. The rent-seeking culture triumphed. Following the re-organisation of local government, the number of municipalities raising revenue from land value rating was reduced from 90% to 73%, and the database was degraded. The outcome:

- housing markets suffered soaring prices, creating the largest boom in NZ history. Homeowners and speculators reaped fabulous riches. It all terminated with the recession of the early 1990s.

Attempts at reviving the direct collection of revenue from rent have been repressed. Outcome:

- since 2010, the price of residential and commercial premises has reached unaffordable levels.

As in countries like the UK, problems linked to property are glibly analysed in terms of blaming the town planners, and/or the need to increase the supply of dwellings. Meanwhile, urban sprawl continues to blight the countryside. Remnants of the history of rent-as-public-revenue may still be found in some municipal rating systems, but a more radical approach is needed to restore the country's foundation fiscal philosophy, according to two lecturers at the University of Auckland.[2]

1 Robert Keall (2000), "New Zealand", in R.V. Andelson, Land-value Taxation Around the World, 3rd edn., Oxford: Blackwell, p.427.
2 https://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11543819