

Tax in a Proutist Economy

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Version 2.1, 24th June 2005

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Part 1: Taxation as public income

1. Introduction

This article is intended as a contribution to a discussion on taxation in a Proutist economy. Sarkar has written little on the subject and what there is, is better understood by reference to the existing literature. As can readily be imagined, the literature is vast and detailed, having evolved over many centuries. This article attempts to distil relevant principles guided partly by Sarkar's comments and partly by common sense. The final conclusions are not concrete policy suggestions because too much depends on the time, place and circumstance in which a tax is levied. There is much to learn about taxation and the author hopes that this article offers Proutists a helpful introduction. The author also believes that the mode of argumentation required to discuss taxation policy can usefully be carried over to other areas of debate about Proutist economic policy.

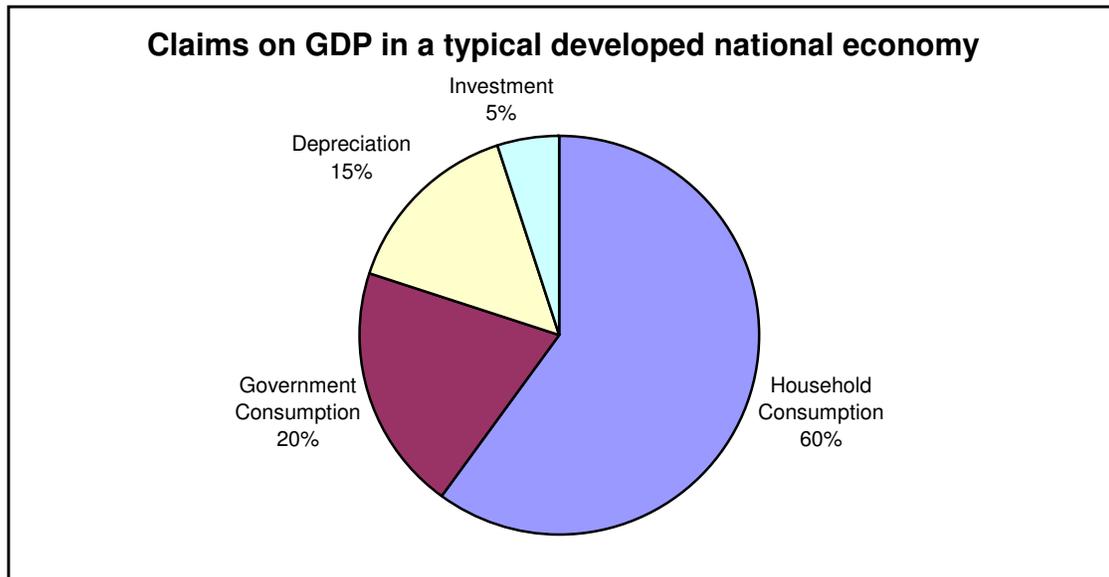
Taxation policy must address simple questions such as "*what to tax?*" and "*how much to tax?*". Therefore such questions partly structure this discussion. Obviously the total of taxation collected will depend greatly on the government's role in the economy. Hence this issue is discussed in Part One. Part Two constitutes the bulk of the article and surveys a range of taxes that could be applied in a Prout economy - in other words "*what to tax?*". Part Three describes important concepts that help to answer the question "*how much to tax?*" and concludes with a broadly defined taxation policy that Proutists could discuss.

2. The big picture

Taxation represents a government claim on a portion of the wealth produced by a community. It is useful to know what size that portion is. For convenience we assume that there are three claimants on GDP (Gross Domestic Product - the total of goods and services produced within a country in one year), households, government and the business sector. Typically, around 60% of GDP is consumed by households, 20% is invested in the private business sector and 20% is claimed by government for the provision of public goods and services. In fact three-quarters of private sector investment (15% of GDP) is required for depreciation, that is to maintain existing stocks, buildings and machinery at their current level of productivity. The remaining 5% of GDP is growth investment – used to expand future production.

Typically, governments as diverse as those of New Zealand, Poland, UK and Canada have expenditure programs that amount to about 40% of GDP. For some countries it is over 50% of GDP. However half the expenditure is *transfer payments* (to be explained below) which redistribute income and is not counted as a direct claim upon GDP. These average figures were gleaned from tables and charts in Miles and Scott [2002]. The 20% direct claim on GDP by governments is remarkably consistent both between countries and over time. When politicians talk about small government it is often the income redistribution component that gets reduced. The proportions of GDP shown in the pie-chart below are typical for a developed economy. In

the devastated economy of post-war Japan, the rate of investment was close to 30% but this is obviously an unusual example. It is not unreasonable to suppose that these proportions would remain pretty much the same in a developed Proutist economy. The business sector would be structured differently of course, but we might expect that its overall need to cover depreciation and investment would be much the same as today.



3. Why is taxation necessary?

Traditionally, government claims on GDP are justified on three grounds: 1. The necessity to provide public goods and services. 2. The necessity for public insurance schemes, such as pensions, health and accident insurance. 3. The desire to promote a more *equitable* distribution of income and opportunities, for example by providing unemployment benefits. Expenditures on insurance and equity objectives are referred to as *transfer payments*, because the end result is a redistribution of income without any direct contribution to GDP. A fourth area of government activity in communist economies is (was) direct involvement in the production and distribution of goods and services. However Sarkar is clearly opposed to governments having a significant business relationship with the general public and we would not expect this to be a feature of a Proutist economy.

Public goods and services are those to which one cannot sell access or offer for sale in a market. Defence, policing and the legal system are the obvious examples. But public health programs to combat infectious diseases, AIDS and drug abuse are also public services in this sense. Once available to one person, they are of benefit to all. Their benefit cannot be broken into parts which are sold individually. By definition, the planning and provision of public goods must be collectively organised and cannot sensibly be devolved to businesses run for profit. However, while the government may have a responsibility to fund public services, it does not always play a direct managerial role. For example, the legal system, research and development and universities

can and should be run by autonomous bodies that are independent from government control even though they are (entirely or partly) funded by taxation. See Towsey [2005] for a discussion of the role of autonomous bodies in a Proutist economy. We now discuss in more detail, the three justifications for government expenditure and taxation, the provision of public goods, insurance and equity.

4. Public goods and services

Public goods make a far more potent contribution to an economy than is immediately obvious. It is clear that normal economic life depends on public order and the rule of law. But it also depends on intangible characteristics such as trust, honesty and goodwill between people. When these qualities are missing from economic relations, the market place suffers, business suffers and unproductive costs associated with litigation, surveillance and security consume more of the GDP. Any reader whose memory goes back to the 1950's and 60's will appreciate how the breakdown of community life since those decades has been matched by a corresponding increase in security.

The moral and cultural factors underpinning economic life are often collectively referred to as *social capital*. Tim Hazeldine, Professor of Economics at Auckland University, defines social capital as the *empathy and sympathy* in human relationships and the *shared attitudes and goals* of a community. Social capital is embodied in the social, educational and cultural institutions of a country and is hugely important in explaining the differences in wealth and productivity between nations. Government investment in activities which promote community life, says Hazeldine, can be as productive as business investment in new machinery and factories.

In his book "*Taking New Zealand Seriously - the economics of decency*", Hazeldine [1998] offers a critique of the economic program adopted by New Zealand since 1984. This program, which is variously labelled, neo-conservative, new-Right or neo-classical, is characterised by a dogmatic belief that market forces promote the greatest human welfare. Of course this dogma has also infected most other capitalist nations over the past 20 years but perhaps nowhere with as much ideological fervour as in New Zealand. Hazeldine argues that the result has been a destruction of the social foundations upon which economic life depends. In other words, New Zealand is now consuming at a prodigious rate, the social capital which was accumulated over many decades by previous generations. Such a situation cannot last for ever.

Sociologist Paul Wong, makes the same observation about corporate culture in the United States. He argues that for any corporation to be healthy and productive, it needs to be strong in four core areas: "(a) financial capital in terms of investments and profits, (b) technological capital in terms of cutting-edge software and hardware, (c) human capital in terms of knowledge, expertise, and creativity and (d) social-spiritual capital in terms of ethics, relationships, meaning and purpose." When senior management forgets the importance of social and spiritual capital, the results can be catastrophic. He cites the Enron scandal as an example. "Enron's senior management failed to maintain a relationship of openness and trust with employees. Staff members who questioned the wisdom of some of Enron's decisions and practices were either ignored or silenced. Senior management cared more about self-enrichment than the needs of employees. They showed little

regard for meaning and ethics beyond the bottom line. There is an absence of shared vision that transcends moneymaking. Enron's deficiency in social-spiritual capital proved to be fatal!" [Wong, 2002] It is hardly surprising that modern businesses and governments have abrogated their responsibility with regard to social capital. Despite all the evidence to the contrary, they have embraced the new right dogma summed up most succinctly by Milton Friedman, that to believe business has a social responsibility is "fundamentally subversive".

While Proutist governments will not be directly involved in business activities, they must take an interventionist role in the care and accumulation of social capital because, if for no other reason, this is what underpins healthy business activity. Sarkar notes in several contexts that cooperative enterprises, which are the cornerstone of a Proutist economy, cannot thrive in a climate of dishonesty and greed. "For their success, cooperative enterprises depend on morality, strong administration and the wholehearted acceptance of the cooperative system by the people. Wherever these three factors are evident in whatever measure, cooperatives will achieve proportionate success. To encourage people to form cooperatives, successful cooperative models should be established and people should be educated about the benefits of the cooperative system." [Sarkar (1), 1992] In other words, the role of government is not just to provide security, law and order. It is also to build a culture of trust, discipline and caring which constitutes the essential foundation of civilisation. In this regard, Sarkar also believes that governments should take an active role in the promotion of literature, theatre and the arts. "The first step of this policy must be to build up fully or partially government aided theatres in every major village and city, which must be exempt from amusement taxes." [Sarkar, 12]

5. Social insurance

The insurance component of government expenditure is designed to reduce the risk of misfortune, accidents, ill health and disaster which inevitably strike individuals, communities and businesses from time to time. Insurance is necessary to maintain the smooth running of a society. It may be viewed as an economic application of the principle of *prama*, which states that a dynamic equilibrium can be maintained through a triangulation of forces [Sarkar (3)]. Sarkar gives the example of the production and distribution of rice. One economic force is the willingness to produce rice. Another economic force is the desire to consume rice. And the third force, necessary to preserve an adjustment between supply and demand, is a reserve or stockpile of rice. The concept is quite general. In our current context, an accident insurance fund or workers compensation scheme can be likened to a stockpile that maintains adjustment between the supply of and demand for social and economic resources.

There are several options to fund insurance schemes. On the one side, health insurance could be totally managed by the government, or it could be totally managed by non-government agencies such as cooperative insurance companies. Indeed for virtually any insurance scheme, one can devise a government mechanism and a non-government alternative. In one case, the policy objective is funded through taxation, in the other by some mix of compulsory and voluntary non-government saving. Such choices should be decided on the basis of equity and efficiency. There is a common perception that government involvement in public insurance promotes equity while

non-government insurance schemes are economically more efficient. Finding the right mix is a policy issue.

What might be a Proutist approach to these questions? There is an important distinction in Prout between the *minimum required* allocation of a commodity or service and the additional *amenity* component which makes life easier but is not essential. In the case of health care, the Australian government makes the same distinction. The government provides essential health services, while private insurers cover *optional extras* such as doctor of choice, massage and optometry. This arrangement or something like it, seems elegant. In a Proutist system, the government would have a constitutional obligation to ensure that everyone gets the minimum health care services so it should be given the necessary powers to achieve this goal, thereby taking care of the equity objective. Cooperative health insurance companies could provide cover for the additional health amenities that become desirable as a community becomes more wealthy.

6. Equity

An important function of government transfer payments is to promote equity. The obvious examples are unemployment benefits, pensions and child endowments. Transfer payments are now up to 20% of GDP in developed countries. Note that the transfer payments themselves do not figure in GDP calculations but the salaries paid to the public servants who administer the transfer payments are a direct claim upon GDP.

One hopes that in Proutist system the figure of 20% could be reduced by achieving a more equitable primary distribution of income. Furthermore public enterprises and cooperatives would take more responsibility for the welfare of their employees while government encouragement of *not for profit* organisations would ensure community safety nets are ready to help those in difficulty. However frictional unemployment* brought about by technological change cannot be ignored and there will always be persons who cannot work even to get their minimum essentials.

Other questions arise. How should the very young, the old and the infirm be guaranteed their minimum requirements? Should children receive their income through government payments to parents (a transfer payment) or through a wage increment paid by the businesses employing the parents? As with health and accident insurance, there are various funding options available to achieve the desired policy objective. Since in a Proutist system, the government will have a constitutional duty to ensure that everyone receives the minimum requirements of life, it is essential that the government has the necessary economic powers to bring this about. The distribution of non-essential or amenities is however, better left to the non-government sectors.

7. Where does the money come from?

Traditionally governments finance their expenditure by taxation, the printing of money and borrowing from the non-government sectors, that is private individuals and businesses. There is

* Frictional unemployment is that associated with people changing jobs. The change may be voluntary or forced. It is a particularly significant form of unemployment in times of rapid technological change.

also the possibility to generate revenue from the sale of goods and services, but such charges can be considered taxes. It is clear that Sarkar is opposed to governments having direct control over the money supply to finance their expenditure. This is for the good reason that the printing of money is inflationary where there is no corresponding increase in production or compensating withdrawal of money from circulation. Sarkar also suggests that the less the government has a direct business relationship with the general public the better. Thus it seems a Proutist government would have little prospect of generating revenue from the sale of goods and services.

However funding a government deficit (the difference between tax revenue and expenditure) by borrowing is an option that needs more thoughtful consideration. The economic effects of government borrowing can be complex and much depends on how wisely the government targets its spending programs*. Borrowing saddles future generations of taxpayers with interest repayments but if government investment promotes economic growth then the debt burden can be justified. From the Keynesian perspective, budget deficits can be used to stimulate a stagnant capitalist economy and reduce the effects of a recession. But this is only a short term measure. Eventually the debt must be repaid by a subsequent government surplus or future growth.

From a different perspective (a Proutist perspective?), government deficits can be viewed as a symptom of unresolved distributional conflicts in a capitalist economy. The government has a spending program (that is, an intention to claim some portion of the GDP) but does not have the cooperation of other sectors of the economy to reduce their claims on GDP – that is, to reduce their spending and pay the necessary taxes. So the government is obliged to sell debt (government bonds) at sufficiently high rates of interest to entice the private business sector to divert resources away from investment.

The essential problem for governments in capitalist economies is that they must compete with the powerful business sector for the resources to provide essential public goods and services. To lessen the damage caused by this competition, complex financial markets and systems of arbitration have been developed but the underlying tensions persist. The approach taken by a Proutist economy to solve this problem would be the one always advocated by Sarkar, *cooperation!* When a local or national community designs a budget to allocate its available resources, it would be drawn up by a truly *collective body* consisting of representatives of the government, business and consumer sectors. The business sector would obviously include public, cooperative and private enterprises. This *cooperative* budget (it could also be viewed as an *incomes accord*) would decide total claims on the GDP by all the different sectors. It would set tax rates, wages and salaries and make decisions about gross business saving. Obviously such a budget can only be achieved through cooperation between the various sectors (government and non-government) of the economy. The cooperative budget is just one practical example of the *collective body* at work as referred to in the first principle of Prout [see Aappendix 3]. Assuming

* Sarkar is particularly adamant concerning the use of monies borrowed by business or government. The following paragraph is worth quoting in full. “The science of economics teaches that the rolling of money should never be blocked by any sort of non-productive investment. Sometimes people misuse loans to construct an unnecessary building or a new showroom for their business, and thus prevent the possibility of reinvesting the capital and increasing their wealth. Economics teaches that loans taken for business investment should always be utilized for productive purposes, and should never be utilized in any unproductive venture. Foreign loans, for example, should never be invested in constructing large railway stations instead of railway lines.” [Sarkar, 17]

that the budget process is successful then, in normal circumstances, the government sector would not have a deficit to finance. Thus taxation would constitute most if not all of government revenue in a Proutist system. Borrowing would be required only when a sector missed its budget targets but this would represent a tactical adjustment as opposed to a strategic investment.

The success of a cooperative budget also depends on the distribution of money by the financial system being in accord with the budget. Prout is opposed to private business people having control of the financial system. Rather, the distribution of money should be in the hands of cooperative banks or credit unions under the supervision of a central bank operating as a public corporation. In such a situation, the central bank must be part of the cooperative mechanism that makes the budget.

8. What is an effective tax?

Over the centuries, many different kinds of tax have been levied, limited only by the human imagination. Given that there are so many tax options, the question naturally arises - what is an effective tax? Today there are three universally recognised criteria by which taxes are judged, *equity*, *efficiency* and *simplicity*.

a. Equity: Taxes should not only be fair but be seen to be fair. However there are different kinds of equity, not necessarily consistent with one another. Two well recognised equity principles are the *benefit* principle and the *ability to pay* principle. The benefit principle says that those who receive the benefit from a tax should pay the tax. This is essentially a *user pays* argument which is used to justify road user charges, water and sewage rates. This principle has the obvious advantage that, for example, it makes people think more carefully about the water they consume and the waste they produce. The principle also has an obvious limitation - it makes no sense to tax the poor in order to address the problem of poverty. Hence, the other approach to equity is the *ability to pay* principle - the more you consume or take out of the system, the more you should return in the form of tax.

In designing an *ability to pay* taxation system, two more principles are invoked. The *horizontal equity principle* says that persons with the same ability to pay should pay the same amount of tax. The *vertical equity principle* says that a person having more ability to pay should pay more tax than a person with less ability to pay. With regard to income tax, for example, it is said to be *regressive*, *flat* or *progressive* if the average tax rate decreases, remains the same or increases respectively with increasing income. That is, income tax is progressive if individuals with higher income pay a greater percentage of their income in taxes than do individuals in middle and lower income brackets. Giving tax breaks to the wealthiest people (as done by President George Bush in 2004) is a regressive taxation policy. It is generally argued that vertical equity demands a progressive tax rate.

b. Efficiency: In the context of taxation, efficiency refers to the property of not producing undesirable distortions of economic or human behaviour. For example in 17th century Great Britain, a tax was levied on windows. It was meant to be a wealth tax based on the assumption that persons with more wealth would have bigger houses with more windows. Predictably, people

began building houses with fewer windows. Not only did the government collect less revenue than expected, but people began living in unhealthy conditions. Not an effective tax!

All taxes have some effect on human behaviour but the efficiency criterion demands that these effects be minimised. A flat rate sales tax is more efficient than a sales tax on selected commodities because it does not cause individuals to discriminate between commodities. Taxes which do not distort choices are said to be *neutral*. Sales taxes on specific commodities typically induce a *substitution effect* because people switch to the cheaper untaxed substitutes. Some taxes, of course, such as *eco-taxes* on plastic bags and petrol are intended to induce substitution effects.

Typically, taxes are neutral with respect to some choices but distort others. Income tax for example, does not distort choices between goods and services but it does distort patterns of consumption versus saving, because it reduces disposable income and therefore the capacity to save. The individual may not readily recognise such effects, but they certainly become apparent at the macroeconomic level.

In any assessment of the efficiency of a tax, it is assumed that public expenditure is at least as efficient as private expenditure and therefore the transfer of resources from private individuals to the public sector is not in itself a source of inefficiency. Only the effect of the tax on economic decisions is assessed for efficiency.

c. Simplicity: Taxes should be simple to collect and administer. The *administrative costs* incurred by government are distinguished from the *compliance costs* incurred by individuals. Administrative and compliance costs vary greatly with the tax. Tax reform movements in the USA claim that the compliance costs of their current tax system are nearly 50% of tax revenue [TR, web site]. Eliminating income tax and replacing it with 17% flat sales tax would save the country an estimated \$600 billion in tax compliance costs! By comparison, the compliance costs of a flat sales tax are estimated at \$1.5 billion, around 500 times less! Unfortunately, sales taxes are regressive, which highlights a trade-off problem - the different tax criteria are known to work against one another. In particular it is often argued that the pursuit of tax equity increases compliance costs.

Part 2: A Survey Of Taxes

Taxes can be categorized in a variety of ways. Stretton [1999] makes a major distinction between direct, indirect and business taxes. Another distinction is between taxes whose primary purpose is to gather revenue and special purpose taxes whose purpose is to achieve some specific social or economic objective. We begin by distinguishing taxes on *economic transactions* from taxes on *wealth*. Transactions involve flows of money into and out of economic entities - taxes on incoming money are *direct* taxes, the taxes on outgoings or expenditure are *indirect* taxes, for example *sales* tax and *excise* duty. Wealth tax, on the other hand is levied on what is owned by economic entities. We also discuss two other general tax categories, *special purpose* taxes and *in-kind* taxes paid in the form of physical commodities or services. Although in-kind taxes are not usual in developed economies, they were common in early civilisations and Sarkar suggests that they could be useful today, especially in underdeveloped economies.

All taxes can be levied on individuals or on corporate entities. In every case, we must assess the effectiveness of a tax from the perspective of its *equity*, *efficiency* and *simplicity*. These criteria will be as relevant in a Proutist economy as they are today. Because income tax and sales tax are well known, little space is given to them here. Instead, more attention is devoted to resource and wealth taxes which are less well understood.

9. Personal Income Tax

The main advantage of income tax is that it can promote equity. In most countries the marginal rates are set so as to have a progressive effect. However it should be noted that so-called reforms to income tax since the 1980s have reduced the progressive outcomes in many countries. In New Zealand, for example, real disposable income (i.e. income remaining after income tax) increased markedly for the highest income quintile but has declined steadily for all other quintiles since 1982. [Scollay and St John, 2000]

From the point of view of efficiency, income tax is neutral with respect to choices between goods and services but tends to discourage saving and the incentive to work, particularly at high marginal rates. However the most serious inefficiency caused by income tax is the encouragement it gives to a black economy and to tax avoidance schemes that hide income. Compliance costs are high for income tax because in a modern economy, people have so many different sources of income and so many possibilities to incur tax exempt expenses. Compliance costs are particularly high if the income tax regime attempts to be *comprehensive*, that is, attempts to include all kinds of cash and non-cash income. Non-cash income includes fringe benefits, in-kind payments and capital gains.

Despite the potential to promote equity, Sarkar is opposed to personal income tax because the complexity in assessing income encourages avoidance measures that are mostly available to the rich. (Disguising income as a *capital gain* is the primary form of legitimate tax avoidance in capitalist society.) In addition, it is bad psychology to give money in one hand and immediately take from the other.

A particular feature of a Proutist economy is an upper limit on annual income or some estimate of it smoothed over the previous year(s). This limit is fixed as a ratio to the guaranteed minimum income (GMI). Although the income ceiling is not a tax because the government derives no direct revenue from it, nevertheless its imposition can be expected to have ramifications that should be scrutinised according to the same criteria of equity, efficiency and simplicity. The income ceiling is one of several measures at work in a Proutist economy to prevent undue concentration of wealth. In this respect, it promotes not only equity but also reduces the possibility for economic stagnancy arising out of speculative activity. Obviously the lower the maximum/minimum income ratio, the more egalitarian the outcome. However there is a contrary effect. Lower income ratios will also reduce work incentive with a consequent reduction in output. Such effects were commonly observed in communist economies. The choice of income ratio in a Proutist economy could be as important a macro-economic instrument as interest rate and money supply are today. A ratio that is too low would reduce incentives and stifle economic initiative. A ratio that is too high would tend to concentrate wealth and lead to stagnancy. It might be a fine line between the

two. Both these effects could be modelled mathematically (see for example Friedman [web site]) but in the absence of a realistic and workable model, the choice of income ratio will be a political decision based on a community's perception of equity, greed, motivation etc. It could well be that the wrong choice is made and the income ratio has to be temporarily increased. However the long term trend (over decades) should be a gradual reduction in the income ratio as community psychology adjusts to work motives other than profit.

10. Corporate Income Tax

Corporate income tax is levied on the excess of revenue over expenditure for a given time period. The problem to be solved is how best to split the profit three ways - one portion going as tax to the government, another going as dividends to shareholders and the remaining portion retained for investment in the company. The problem is complex because modern capitalist economies offer a bewildering array of commercial levers which interact with one another.

In the traditional system, tax was levied on the gross profit and the remainder either distributed as dividends or retained by the company. More recently there has been a trend not to tax company profit at all. For example Germany abolished corporate profit tax in 2000. The rationale was that companies are fully owned by individuals. The distributed profit will be taxed indirectly through a tax on dividend income and the retained profits (which make the company more wealthy and therefore push up the market value of its shares) will be taxed via capital gains on individual shareholdings.

A Proutist economy will be commercially simpler than today (at least as we currently envisage it) but it will have structural constraints that do not exist today. For example, a Proutist economy will distinguish three kinds of enterprise, public, cooperative and private, the cooperative sector being the largest [Towsey, 2005]. Public enterprises will be run on a *no profit - no loss* basis and thus would not attract a tax on profits. They would however be subject to other taxes as discussed later. Cooperatives are owned by their workers and their shares are not tradable. An additional structural constraint is the growth limit placed on private enterprises and cooperatives. When a private company exceeds a size threshold (which will be determined by some function of its capital stock, turnover and number of people employed) the company will be transformed into a cooperative. A cooperative which exceeds its size threshold would be split into two cooperatives or else converted into a public company, the choice being determined by what makes most economic sense. When we also take into consideration the ceiling on personal income, profit taxes in Proutist economy require careful consideration.

By way of example, let us suppose that a particular cooperative is enjoying a boom period and has made a substantial profit. The government has levied its tax and the after-tax profit must now either be distributed as dividends on worker shares or retained for investment and company growth. What happens if dividends cannot be distributed to some workers because this would push them above the income ceiling? And what happens if retained profits push a cooperative over its maximum size threshold.

The first point to emphasise in this example is that the high profits being made by this cooperative should send a clear signal to the rest of the economy that here is a business opportunity. A cooperative which refused to expand in these circumstances would be extracting excess profits by restricting supply. In a healthy economy with open markets, new cooperatives would immediately jump in to soak up some of the excess profit. In other words in a healthy economy, excess profits should only be a temporary phenomenon.

If retaining profits pushed a cooperative over its size threshold, then indeed it would be divided or converted to a public company. Splitting a large cooperative would be justified on the same grounds that U.S. anti-trust legislators use to split giants like Bell and Microsoft. It promotes competition, boosts production and reduces excess profits.

In some cases, it might not make economic sense to split a wealthy cooperative or force a small but wealthy private company to become a cooperative. In cases where company profits can neither be retained nor distributed to shareholders, a number of alternatives suggest themselves. 1) The government could take the excess. 2) The excess could be directed to a social body such as an association of cooperatives that promotes the interests of cooperatives. 3) The excess could be directed to local community groups or charities. This practice is already common today for local businesses. 4) The excess could be directed to a charity run by the cooperative itself. Options 3 and 4 are elegant because they preserve the incentive to be productive and they preserve a sense of economic independence, both of which are psychologically important. Option 1 is least desirable for the same psychological reasons. And it is most likely in a Proutist economy that cooperatives would already pay regular levies to an umbrella organisation that promotes their welfare. It is worth noting that the Mondragon cooperatives in Spain donate 10% of their profits to charities as a standard practice.

11. Personal Consumption Taxes

There are several kinds of personal consumption tax, the two most common being value added tax (VAT) and retail sales tax. The former levies a tax at each stage in a production sequence on the value added at each step. A retail sales tax is applied only to finished products at the point of sale. Both taxes if applied at the same rate to the same production base should generate the same revenue. However the VAT, of which the New Zealand and Australian GST taxes are variants, has much higher administrative and compliance costs.

A flat rate consumption tax on all goods and services is regressive because the poor spend a higher percentage of their income on consumption. Put another way, a flat rate sales tax will gradually widen the disparity between rich and poor because the rich will be able to save and accumulate more assets. A progressive income tax can correct this situation but other measures are also available. One is to provide a sales tax exemption on essentials such as basic foods and health care. Another is to levy various kinds of wealth taxes, including gift and death duties. A positive feature of sales taxes is that, unlike income taxes, they do not distort the choice between saving and consumption.

Sarkar proposes that all goods and services should be divided into three categories, *essential*, *semi-essential* and *non-essential*. The last category would be considered luxuries. As an example, milk, cheese and ice-cream might be assigned to the three categories respectively. If sales taxes are adopted, then essential commodities, according to Sarkar, must remain entirely tax free. [Sarkar (4), 1992] A broad base flat-rate sales tax does not distort choices between goods and services whereas a selective sales tax, such as Sarkar describes would clearly promote a substitution effect. While this is considered a disadvantage by free market purists, Sarkar would consider it an advantage because it would stimulate the demand for essential goods and services and therefore increase their production. One of the problems arising out of concentration of wealth is an overproduction of luxuries or conversely, an underproduction of basic necessities.

This is clearly what Sarkar has in mind when he proposes a "protective" role for sales taxes in an economy that is trying to make the transition from a private enterprise capitalist economy to a cooperative economy. He acknowledges that it is difficult for new cooperatives to survive in open competition with pre-existing private enterprises. Young cooperatives require, he says, a "protective armour" in the form of "exemption from sales tax, duties, etc." [Sarkar (5), p.15] This discriminative use of sales taxes is not dissimilar to the use of import taxes to protect local developing industries. Isolating young businesses from competitive pressure may be essential to start with but can eventually lead to inefficiencies and increased costs. Sarkar also acknowledges this argument and notes that such systems of protection "should be withdrawn slowly". Furthermore he is in favour of protection only for businesses producing essential commodities. [Sarkar (5)]

12. Corporate Consumption Taxes

In order to produce goods and services, businesses consume resources, the so called *factors of production*. In a capitalist economy, the factors of production are assumed to be owned by individuals who earn an income by selling them to producers. These transactions can be viewed either from the perspective of the individuals receiving an income or from the perspective of the businesses consuming resources. In order to maximise profits, capitalist businesses have a long tradition of attempting to hide true costs, in particular environmental and social costs. Perhaps for this reason, the focus of taxation has been on the income side of the transaction. It is easier to tax individuals than it is to tax powerful corporations. However there are good reasons to place the tax focus on the consumption side. Sarkar, as we have noted above, is opposed to income tax. "Instead", he says, "taxes should be levied at the starting point of production." [Sarkar (4), 1992] The starting point of production involves the consumption of natural resources and labour. The primary argument in favour of taxing these resources is that, if wisely applied, such taxes promote a more efficient use of scarce resources.

Traditionally, the factors of production are land, labour and capital. However it is helpful to be more explicit. Land includes physical space, minerals, water, air, animals and plants - in fact the entire ecosystem that supports an economy. Labour is all forms of human activity directed towards the production of wealth. Capital includes not just financial capital and physical capital (machinery and buildings) but also intangible social capital such as community spirit, trust etc which are the invisible moral foundation of an economy. One of the revolutionary features of a

Prout economy will be to identify and incorporate into cost calculations, productive resources that have previously been invisible and intangible - factors such as environmental diversity, work in the home, child rearing and social capital components.

According to classical economic theory, a rational producer will combine the factors of production so as to minimise the cost of producing a given level of output. In other words, producers will consume more of the cheaper resources! This behaviour is said to be economically efficient because no other combination of resource consumption at their current costs would make everyone better off. In short, efficiency equates with maximising economic welfare.

One of the problems with classical economic theory is that it assumes all of the factors of production are accurately costed. But this is not the case. The consumption of many kinds of resource involve what economists call *externalities*, that is, effects on human welfare which are not or cannot be incorporated into cost accounting. A typical example of a *negative externality* is pollution resulting from the burning of fossil fuels. Businesses recognise their *internal* private costs in the purchase of oil but not the external social costs of pollution. The attempt to make businesses incorporate external costs into their accounting is known as the *internalising* of external costs.

Economists have long recognised the phenomenon of external costs and a few have advocated internalizing these costs by charging *Pigouvian taxes*, taxes which when added to marginal private costs bring the total cost up to the true marginal social cost. While this solution is elegant in theory, in practice it is difficult or impossible to implement. Some external costs such as pollution costs, can be roughly calculated. But how does one calculate the costs associated with consumption of social capital.

Fortunately, it is not necessary to have a complete cost accounting of all the forms of capital consumed during production in order to implement an effective system of taxes on business consumption. It is necessary only to levy taxes on visible and measurable consumption at a rate which meets the overall perceived social costs of production. From the point of view of classical economic theory this approach is crude. But from a practical point of view, business consumption taxes are a powerful tool to promote the efficient use of resources and to promote an equitable distribution of income between the factors of production.

Of the physical resources consumed during production in a capitalist economy, natural resources are virtually uncoded. They are taken for free. On the other hand, the external pollution costs associated with wasteful consumption of natural resources are becoming more and more evident. Therefore environmentalists promote taxes on natural resource consumption as an exercise in rational accounting. Shifting the tax base from income taxes to resource taxes would internalise the external costs associated with pollution and would encourage more careful and efficient consumption of precious environmental resources. In fact, say environmentalists, not having resource taxes is like having taxpayers subsidize pollution.

Resource taxes would have an additional benefit. Businesses, particularly small businesses, in modern capitalist economies complain that labour is too expensive. Indeed labour is expensive

when compared with the other two major factors of production, natural resources and physical capital. No matter how low labour costs are pushed they cannot compete with natural resources which are virtually free. Physical capital is also cheap partly because of the under-costed natural resources embodied in it and partly because it is relatively easy to accumulate physical capital over a period of years by saving and investment. But the cost of labour cannot be reduced below the point required to maintain a minimal standard of living (except in slave societies and third world countries). Given the relative prices of natural resources, labour and physical capital, producers naturally try to reduce labour costs by substitution. A tax placed on resource consumption or on physical capital or both would make labour relatively cheaper. Producers would attempt to substitute their use of natural resources and capital with labour. So there are three benefits arising from resource taxes - reduction in wasteful resource consumption and associated pollution, a more economically efficient recognition of social costs and a more equitable distribution of income, that is a reduction in unemployment.

Herman Daly, formerly a senior economist at the World Bank and now at the University of Maryland School of Public Affairs summarises the argument thus: “We have to raise public revenue somehow, and the present system is highly distortionary in that by taxing labor and income in the face of high unemployment in nearly all countries, we are discouraging exactly what we want more of. The present signal to firms is to shed labor, and substitute more capital and resource throughput, to the extent feasible. It would be better to economize on throughput because of the high external costs of its associated depletion and pollution, and at the same time to use more labor because of the high social benefits associated with reducing unemployment.” [Daly, 1994]

Before considering resource taxes in more detail, we briefly consider two other kinds of tax on business consumption, *payroll* tax and *import* taxes. Taxes on physical capital are considered in the context of wealth taxes.

13. Payroll tax

Payroll tax is levied on employers, sometimes as a percentage of their total wage bill but also in the form of direct contributions to accident insurance, health insurance and superannuation (pension) schemes for employees. Payroll tax becomes another cost of production built into prices paid by the consumer. If the tax rate reflects the danger of the work involved, business will have an incentive to adopt safer practices. Payroll tax for this purpose can be justified on grounds of user-pays. The obvious argument against payroll tax is that it encourages substitution of labour and therefore should not be applied in conditions of labour surplus or unemployment. However, Stretton, [1999, p 632] describes an imaginative use of payroll tax to reduce unemployment. He suggests that payroll tax should not be levied on the first 35 hours of each worker's week but above that it should be levied at a high enough rate for the overtime wage plus that payroll tax to cost the employers twice as much as it would cost to get the same work done by hiring additional workers. The conclusion appears to be that payroll taxes should not be used for general revenue gathering but are appropriate as targeted taxes to achieve specific policy objectives such as to change work practices.

14. Import Taxes

Import taxes have a legitimate purpose when designed to protect fledgling local businesses from the kind of overseas competition that would destroy them before they got off the ground. Import taxes were used successfully for this purpose by New Zealand for many years. However as noted above in the context of sales and excise taxes, in the long term, import taxes can hide inefficiencies and keep costs high. This argument was strongly promoted by free market purists to abolish New Zealand's complex system of import restrictions in 1984. Sarkar recognises the advantages of free trade and notes its success in countries such as Singapore. [Sarkar (6), 1992]

However the advantages of free trade are only realised where the trading partners are of similar economic strength. The North American Free Trade Association which pits the giant USA against Mexico is only of advantage to the USA. In truth, powerful countries are never interested in free trade except when it is to their advantage. The USA has a significant subsidy system in place to protect it from Australian competition. A higher policy objective than free trade is to provide everyone with the minimum requirements of life. This objective implies that a nation (or other economic unit) should attempt to become self-sufficient in the production of its essential goods and services. A country such as Singapore, which is dependent for its water and food supply on a not necessarily sympathetic neighbour is placing itself in a dangerous situation.

As noted above, a Proutist economy makes the distinction between, essential, semi-essential and non-essential goods and services. The logic of Sarkar's argument concerning sales tax, can also be applied to import taxes. In general, the classical advantages of trade should be allowed to manifest for semi-essential goods and luxuries. Taxes on the import of essential commodities can be applied where their purpose is to protect developing local industries. The policy objective is that an economic unit should eventually become self-sufficient in the production of its essential requirements without the need for protective armour. Until that objective is met, protective armour may be required.

Hazeldine argues that the belief in trade as the path to economic health is a myth. He turns the notion on its head and says that a country needs to import so much only because it exports so much. [Hazeldine, 1998] In particular, he argues against the modern trend of investing heavily in tourism as a means of earning foreign currency. The foreign currency which New Zealand earns from tourists is then used to pay for imports required to replace the local goods that are not produced locally because the people who could produce them have been sucked into the tourist industry. Sarkar's proposal to obviate the foreign exchange complications arising from multilateral trade is to promote barter trade. [Sarkar (7)] This is particularly helpful for developing countries when trading with powerful developed countries. It obviates the need for a poor country to hold large foreign currency reserves just to maintain international liquidity, a system which advantages only the wealthy nations whose currencies are used for trade.

15. Resource Taxes

Holland and Scandanavia are leading the world in the introduction of eco or green taxes. The primary purpose of eco-taxes in these countries is to promote effective environmental protection

and they are accompanied by education programs. The results are impressive in changing consumption patterns. A tax on shopping bags introduced to Denmark in 1993 has reduced the consumption of plastics and paper for these products to one third of the original figure. A tax on chlorinated solvents reduced consumption of these products by 60% over the years 1995 to 1999 [Gade, 2001]. In other cases behavioural and environmental effects have been slower but nevertheless effective. These examples are however a limited application of resource taxes. Danish environmentalists have been at pains to tell the public that the intention of these taxes is not revenue gathering. The point of the taxes is to avoid them! Nevertheless the Danish Ministry of Taxation estimates that eco-taxes account for some 10% of total tax receipts and have allowed the government to reduce other taxes and charges.

The next step beyond targeted green taxes is a broad base resource tax. The best way to illustrate how such a tax might work is by an example. The following example is adapted from an article “An Example of an Eco Tax Reform” [AH 2, web site] and summarised in Tables 1 and 2. The example is not easy to digest for those who are unfamiliar with the territory, but it is worth the effort if you want to understand the important contribution that resource taxes can make to building a better world. Let us assume a closed society (one which is not trading with the external world) having 1000 inhabitants and a GDP of \$100,000. Therefore the average income is \$100 per year. To keep the example simple, we disregard capital and interest and assume all income is earned from labour.

TABLE 1

Composition of GDP and personal spending for a society *prior* to introduction of a tax on resource consumption.

GDP	\$ Value	Average personal expenditure	\$ Value
Government services	40,000	Tax on labour income 40%	40.00
Production of physical goods	30,000	Expenditure on goods	30.00
Production components		Cost components	
Resource extraction - 15,000		Resource extraction – 15.00	
Processing – 15,000		Processing – 15.00	
Total - 30,000 (10,000 units @ \$3)		Total - 30.00 (10 units)	
Production of services (non-govt)	30,000	Expenditure on services	30.00
(10,000 units @ \$3)		(10 units @ \$3)	
Total GDP	100,000	Disposable Income	60.00
		Total Income	100.00

Given an income tax rate of 40%, individuals will have \$60 of disposable income which we assume to be spent equally on goods and services. At the prevailing prices, \$30 buys 10 units of goods and the other \$30 buys 10 units of services. Consistent with these figures, the composition of GDP for a given year *prior to introducing a resource tax* must be as shown in the left side of Table 1. As another simplification, we assume that no material resources are used in the provision of government and non-government services. Further we assume that the production of 10,000 units of physical goods at \$3 per item is achieved at a cost of \$15,000 for the resource extraction and \$15,000 for the manufacturing process. These figures show up in the right side of the table as cost components in the goods purchased by individuals.

Now let us suppose that the government introduces a 200% tax on resources. It does this gradually, say over a period of two or more decades, during which time market competition forces producers to reduce by half the quantity of resources used per unit of physical product. It is further assumed that the demand for, and hence production of, physical goods remains unchanged at 10,000 units per year. So now only half the labour force earlier used for resource extraction is required. The other half is gradually absorbed into the non-government service sector. Everything else being equal (for example, we disregard inflation) the composition of the GDP is as shown in the left side of Table 2.

TABLE 2

Composition of GDP and personal spending for a society *after* introduction of a tax on resource consumption.

GDP	\$ Value	Average personal expenditure	\$ Value
Government services	40,000	Tax on labour income 25%	25.00
Production of physical goods	22,500	Expenditure on goods	37.50
Production components		Cost components	
Resource extraction – 7,500		Resource extraction – 7.50	
Processing – 15,000		Resource Taxes – 15.00	
Total - 22,500		Processing – 15.00	
(10,000 units @ \$2.25)		Total - 37.50 (10 units)	
Production of services (non-govt)	37,500	Expenditure on services	37.50
(12,500 units @ \$3)		(12.5 units @ \$3)	
Total GDP	100,000	Disposable Income	75.00
		Total Income	100.00

The first point to note is that total tax revenue has not changed because the government has a fixed program of spending. Only the composition of the tax base has changed. Income tax revenue has been reduced by the same amount that resource taxes have increased. From the point of view of the individual, disposable income has increased 25% (from \$60 to \$75) due to the cut in income tax. Half of this increase has been absorbed by the 25% increase in the cost of physical goods. The other half might have been spent on more physical goods but was instead diverted to the purchase of more services. Why? Because the increase in the price of physical goods has had the effect of making services relatively cheaper, even though their absolute price remains unchanged. The price differential has induced consumers to demand more services which sustains the shift in employment from the resource sector to the service sector.

The crucial assumption in this example to bring about the changes in composition of GDP *hinge on changes in factor productivity*. We assumed that resource efficiency gradually doubled after the introduction of resource taxes. That is, the same amount of goods were produced (10,000 units) but with half the consumption of resources. The result was a 25% decrease in the cost of producing 10,000 units of physical goods. Such gains in efficiency can be achieved in the real world both by design and engineering improvements and by recycling. However the assumption of *everything else being equal* implied that there was no increase in labour productivity.

The motivation to make gains in factor productivity is to reduce costs. In a system without resource taxes, labour costs are comparatively high and there is a corresponding motivation to achieve gains in labour productivity. That is why there is so much emphasis on labour

productivity in capitalist economies. After the introduction of resource taxes, we assumed that the focus of scientific research was on gains in resource productivity. The price paid for increased resource productivity in our example was no growth in labour productivity. This is not necessarily bad, since rapid increases in labour productivity lead to high levels of so-called *frictional* unemployment, another feature of capitalist economies. In practice the imposition of resource taxes would lead to a more balanced increase in productivity over all the factors of production.

Finally we must consider the effects of resource taxes from the point of view of human welfare. In our example, per capita GDP remained unchanged at \$100. Economists would say that there has been no change in human welfare. However the balance sheets do not tell the whole story on human welfare because they do not account for external costs. Resource consumption has dropped by half and so also the associated pollution costs. Quality of life will have improved and therefore, by definition, human welfare. In addition, the focus on per capita GDP hides an increase in consumer purchasing power. The increase in resource efficiency allowed some of the work force to be diverted to the production of more services. The end result is that an income of \$100 can purchase more than it did before. This example demonstrates why traditional macro-economic accounting is quite unsatisfactory in measuring true economic progress. This deficiency must be addressed by a Proutist economy.

The above example has introduced the big picture. However a broad-based resource tax is not just one tax. It is many taxes on a wide range of environmental resources such as water, air, forests, mineral ores and various types of resources found in the oceans and in space. Some of the taxes will be truly on resources and some will probably be taxes on pollution, especially air and water pollution. The relative tax rates on the different kinds of resource must be appropriately adjusted so as to avoid undesirable shifts in consumption from one resource to another. Environmentalists recognise that resource taxes require constant monitoring and ongoing scientific and economic research in order to be effective. But this kind of research must be done. It is in fact the practical application of the economists attempt to calculate theoretical Pigouvian taxes. The management of resource taxes may be difficult, but this is not an argument against their implementation. It is better to make a start with taxes that are not optimal and gradually make adjustments, than not to start at all. However it must be admitted that introducing resource taxes in a capitalist environment will be an uphill struggle because it will require a cultural change in the way business people think about the resources they now consume for free.

In a Proutist economy, most natural resources will be made available through key industries [Towsey, 2005]. The cost of resource taxes will be factored into the *no profit no loss* policy followed by key industries. In other words resource taxes will be built directly into the cost structure of the economy. Most cooperatives will purchase their resources from key industries and resource taxes will not enter into their accounts. However, primary production through farmers cooperatives may be an exception to this general rule.

16. Wealth Tax

The taxes we have considered to this point are taxes on transactions, involving inputs and outputs, income and expenditure. By contrast *wealth taxes* are taxes on what people own, more accurately their *net worth* or the difference between their assets and debts. In our discussion of business consumption, we did not discuss taxes on the use of land or capital. Instead we discuss them here in the context of a wealth tax. But this raises the point that the distinction between a wealth tax and a transaction tax can be ambiguous. For example, a tax on land rents (essentially an income tax) is similar to a tax on land value (an asset tax) because land rents have a fairly close connection to land value. Another important issue in the implementation of a wealth tax is that there is not always a simple relationship between wealth and the income generated by that wealth.

Wealth taxes are of particular interest because one of the major causes of economic and social instability in the modern world is extreme concentration of wealth or, to use other words, the gap between rich and poor. Proponents of wealth taxes believe that they not only promote equity but also stability. Managing the concentration of wealth is also a key policy issue in Proutist economics (indeed it constitutes the first principle of Prout, see Appendix 3) and not surprisingly Proutist economists such as Ravi Batra have recommended the implementation of a wealth tax. A wealth tax could be used during the transition from a capitalist to a cooperative economy in order to achieve major shifts in wealth ownership. The very wealthy would be forced to sell some of their assets in order to pay the tax. And a wealth tax could also be used by a cooperative economy to effect small adjustments in wealth distribution. However, wealth taxes have the potential for the same defect as income taxes - it is bad psychology to give and then take away. Thus a Proutist economy has several built in features to prevent extreme concentrations of wealth developing in the first place. The most obvious of these are 1) a guaranteed minimum income. 2) a maximum income which is fixed as a ratio to the minimum income. 3) employee ownership of cooperatives - this prevents company profits being distributed to non-workers and it eliminates speculative trading. 4) the implementation of other progressive taxes such as sales taxes on luxuries and resource taxes which promote full employment.

Wealth taxes are highly controversial because, as might be expected, they are opposed by the wealthy! And the wealthy are powerful. Nevertheless as of 2002, wealth taxes are implemented in eight European countries, Austria, Denmark, Finland, Germany, Luxembourg, the Netherlands, Norway, Spain, Sweden, and Switzerland. In addition, France had a wealth tax system in place from 1982 to 1987 and Ireland from 1975 to 1977. With the exception of Spain, most of these systems have been in place for at least 60 years.

All eight countries exempt some level of wealth from tax, as shown in the third column of Table 3. In addition, the tax rate varies. In some cases it is progressive while in the case of Finland, Luxembourg and Sweden it is a flat rate. The amount of revenue also varies as a percentage of total tax take and as a percentage of GDP. But even in the maximum case, Switzerland, wealth tax amounts to only 2.89% of total tax revenue and 1% of GDP. In all countries, wealth tax is administered in conjunction with personal income tax and, except for Germany, a joint tax return is filed for both income and wealth.

TABLE 3

Different implementations of a wealth tax in eight European countries.

Country	% tax rate	Tax free allowance (Euros)	Wealth tax revenue as % of total 1999 tax revenue	Wealth tax revenue as % of 1999 GDP
Finland	0.9	185,000	0.15	0.07
France	0.55-1.8	720,000	0.32	0.15
Iceland	1.2-1.45	43,000	0.86	0.30
Luxembourg	0.5	37,500	2.10	0.88
Norway	0.6-1.1	15,078	1.15	0.48
Spain	0.2-2.5	108,182	0.48	0.002
Sweden	1.5	110,380	0.56	0.29
Switzerland (Zurich Canton)	0.05-0.3	45,900	2.89	1.01

IBFD and OECD statistics as reported in Hansson [2002]

Almost all the countries in Table 3 also tax estates (or inheritances), capital gains, and real property. However, inheritance taxes have sufficient loopholes that they do little to prevent the concentration of wealth running down family lines. Famous family names such as DuPont and Rockefeller bear testimony to this. Capital gains taxes can be designed to limit speculative activity but once again this has done little to limit the incredible concentration of wealth that is the hall mark of modern capitalism.

Wealth statistics are infrequently gathered partly because they are difficult to get, partly because they are volatile due to fluctuations in prices and partly because the inequalities they reveal are disquieting. A 1995 estimate revealed the USA to have 129 billionaires, the most wealthy man being Microsoft's Bill Gates -- \$12.9 billion. The average American family, by contrast, is worth \$52,200. So it would take a city of almost 250,000 such families (around one million people) to match the net worth of Bill Gates and a town of 80,000 people to own as much as a billionaire. (Recent 2005 figures suggest that Bill Gates is now worth about \$60 billion. Forbes and various other money magazines regularly publish figures on the net worth of the mega-rich.)

These large inequalities are growing. Between 1983 and 1989 (the years of the Reagan presidency), the existing top 20 percent of wealth holders received fully 99% of the total additional national wealth created in those years. The wealthiest one percent enjoyed 62% of that increase. These figures and others in this section are taken from Wolff [1996]. The best way to get a feeling for the equity, efficiency and simplicity characteristics of a wealth tax is to look at a specific example, such as that in Appendix 2 which describes what would happen if a Swiss style wealth tax were levied in the USA.

We conclude this discussion by asking whether and how a wealth tax might be applied in a Proutist economy. Here we must make a distinction between the application of a wealth tax in a transitional economy (that is, transitional between a capitalist and a Proutist economy) and a wealth tax in an established Proutist economy. In the context of post-independent India, Sarkar discusses the approach that the Nehru government should have taken to deal with the tremendous

wealth and land holdings of the zamindars. (The zamindars were a wealthy class of tax collectors that became entrenched in Indian society over hundreds of years. More on this system later.) The point of interest here is that a wealth tax on both land and bank balances could have been applied but how and in what order was the critical policy question.

“One pertinent question is whether both a ceiling on landed property and a ceiling on bank balances have to be imposed. It goes without saying that both methods have to be adopted, but the latter should precede the former. This will bring immediate cash to the government to help establish new industries on the one hand, and it will check the growth of capitalism on the other. By enforcing land ceilings no direct benefit can be expected to accrue to the nation because the available arable land will not be increased, nor will production be increased, since it is not the function of the government to cultivate land. Such an approach would wound the public sentiment and the public would think that the state had replaced the Zamindars. In the face of food shortages it is not advisable to change land policies immediately.” [Sarkar, 15]

From this passage we conclude that Sarkar is in favour of wealth taxes judiciously applied. But it is clear that, more generally, he views controls over wealth accumulation as essential for the well being of society. “There should be rational acquisition and rational distribution of mundane property, otherwise the peace and tranquility of society will be disturbed. The per capita limit of acquisition should be fixed according to the collective resources of the universal society.” [Sarkar, 5, Section 1]

In an established Proutist economy, a ceiling on income will go a long way towards preventing the obscene accumulation of wealth that is the trade mark of modern capitalism. Furthermore, most home ownership and business capital will be in the hands of cooperatives or public utilities. Therefore the opportunities for speculative investment in real estate, shares and bonds will be limited, although investment in bonds issued by key industries could be a major form of long term saving. In such an economy, it is more likely that wealth taxes will be levied on cooperatives than on individuals. As described earlier, this should be done in a psychological way to preserve the entrepreneurial motivation. We can expect land to be an important asset category in a Proutist economy and although it will be managed primarily through cooperatives, the efficient use of it through a system of rents or taxes is an important policy question. This leads us directly to the consideration of land tax.

17. Land Value tax

Land value tax is a wealth tax levied on the unimproved value of land. It is also called a *property* tax. Land tax can be levied on other characteristics such as land area and it can include improvements such as buildings and roads but these alternatives are not discussed here. Land tax will be taken to mean a tax on *unimproved land value*. Land tax is levied by local bodies all over the world because of simplicity. Collection costs are low and compliance costs are virtually zero. Land cannot be hidden, its ownership is easily established and land tax generates a predictable flow of revenue. These are important virtues because local governments do not have the resources to administer an expensive tax system. The system is well proven and there appears every reason to continue it within a Proutist economy. The primary issue addressed in this section is the extension of land taxes as a revenue base for higher levels of government. Is this a good

idea and how would it be implemented? Can land tax replace income tax as a tax base, either partially or completely?

The most famous proponent of land taxes was Henry George. His name is still associated with the land tax movement and its advocates can be passionate [HG]. He proposed that a land tax should be the *one and only* tax base for a nation. He called it the *single tax*. His argument was that land is of natural origin, a gift of nature and not created by human effort. Furthermore, land is a more permanent and reliable source of income than the artefacts created by humans. Thus all land is ultimately public property and its value to humans is derived from nature itself, from government policy and from spillover effects of development of adjoining lands. All these values being unearned by the individual landholder, they are fit to be taxed.

In order to make the discussion more concrete, we examine a specific proposal published by Neil Gilchrist to increase land tax revenue collected by local and state governments in Australia [Gilchrist, web site]. It should be kept in mind that the intention is not to increase tax revenue but rather to find a substitute for other taxes, in particular income tax. The Gilchrist proposal includes the following:

- (i) a flat rate with no threshold,
- (ii) minimal exemptions e.g. public roads and railways, parks and recreation areas.
- (iii) government instrumentalities and agencies at all levels included,
- (iv) provision for deferment for the aged, pensioners, the poor and those on seasonal incomes (temporary hardship).

The absence of a threshold requires comment. The wealth tax described previously had a generous threshold because its intention was primarily to target the rich. A threshold on land tax would have the undesirable effect of increasing the demand for low value land. It would add greatly to the complexity of administration and would destroy the usefulness of land tax for local body revenue.

As with all taxes, we must consider land value tax from the perspective of equity, efficiency and simplicity. If simplicity were the only criterion, then land tax would indeed be the single tax. This assumes of course that social systems are in place to establish the ownership and value of land. But this kind of basic infrastructure is already established in developed societies quite independently of a tax system.

Land tax also meets the basic equity requirements. Wealthy people own the more valuable land and thus even under a flat rate tax schedule, would pay more tax. Two contrasting principles are the *user pays* principle and the *ability to pay* principle. In a developed society, land value is in part determined by the public services available to it - for example, water reticulation, sewage, waste collection and so on. Therefore a land value tax satisfies the user pays principle to the extent that the people who own more valuable land also command more public services.

With respect to ability to pay, land tax is more problematic. Ability to pay means having an income that allows one to meet one's tax liability without hardship. But it is well known that there is not always a strong connection between the value of land and the income generated by that

land. We will return to this problem later. It is sometimes claimed that land value tax is regressive because local governments can levy at lower rates in areas of high land value and still generate the same revenue. But this criticism only applies when each locality levies at its own rate. In the land tax policy described here, the same state or national land tax schedule would apply to all.

Recall that efficiency in the context of taxation is concerned with the effect of taxes on consumption decisions and the allocation of resources. An efficient tax does not produce undesirable changes in economic behaviour and it should correct market failures by compensating for external or hidden costs. The low rates of land value tax usually levied by local bodies have a minimal impact on economic decisions. But what if the tax rate were increased significantly as a replacement for income tax?

A land tax is a cost of owning land. Increasing its rate significantly would have the immediate effect of making land more expensive to own and would make people think more carefully about buying land for security and for speculative purposes. This would reduce the demand for land and drive down its price. More land would become available for housing purposes which is a necessity of life. In addition, those who own land would have a strong incentive to use it efficiently, to develop it in ways that would make it easier to pay the tax. Proponents of land tax argue that it would encourage higher density housing and lower the costs of service provision. It would discourage urban sprawl and the loss of agricultural land to wasteful non-agricultural purposes. In the absence of developers and speculators, land prices would become more stable.

Those who rent housing or office space would find rents increasing. In a Proutist system, housing cooperatives would be obliged to pay land tax. On the other hand disposable income would increase to offset the increase in rents and other flow-on effects. This is exactly similar to the example of resource taxes that we examined above. However advocates of land tax argue that the tax would also flush out unused accommodation and therefore increase supply and keep the price down. The balance of these effects would vary from locality to locality.

Like a resource tax, a land value tax would decrease the relative costs of labour and capital as factors of production. Therefore a land tax would encourage employment and capital development as producers attempted to find substitutes for land. But it would also increase the incentive to extract natural resources. This may explain the reluctance of environmentalists to embrace the cause of land taxes. They prefer to focus on the consumption of resources as opposed to resources as an asset. But proponents argue that a land tax would have many of the same advantages as a resource tax [HG, web site]. In particular it would encourage the development of solar and wind power.

Possibly the most serious argument against land tax is the sometimes poor connection between the value of land and the income it generates. This is not consonant with the *ability to pay* principle. Consider for example, land used for farming where the harvest varies from year to year depending on the season. In the worst case, a farm that has a sequence of bad harvests might be obliged to sell the farm. One can also readily imagine situations where a school or non-profit institution or elderly person who has occupied a piece of land for many years can no longer

afford to pay the tax due to increased land values. Some advocates of land tax are quite cavalier in their approach to this problem. Gaffney for example admits the problem. "A land tax is a fixed periodic charge. It is based on qualities inherent in the land with few concessions to the landholder's personal illiquidity, weakness, setbacks or aging." But he then adds, "*Use it or sell it* is the message, which many consider too harsh. What is harsh for the distressed holder, however, is accommodating to frustrated buyers, and it boils down to which group shall be accommodated." [Gaffney, web site]

This is indeed harsh. If the land tax rate is set too high, it will place unnecessary hardship on seasonal businesses such as farming. This is neither equitable nor efficient since frequent changes of land ownership and land use must necessarily be accompanied by wasteful moving and establishment costs. Gilchrist's fourth proposal above allows for land tax to be deferred in cases of temporary hardship. For the aged and pensioners, the tax could be deferred until death of the owner.

With regard to land management, Sarkar says that "The preservation and utilization of land should be the responsibility of the local government, which in turn should carry out its duty through producers' cooperatives composed of actual farmers." A Proutist economy would endeavour to reorganize all agricultural land to ensure that each landholding becomes an economic holding. Obviously, the size of an economic holding will vary from region to region: a semi-arid region will require a large area of land to make an economic holding, while a fertile region will require comparatively less land. This is why it is essential that land tax be levied on value and *not* on its area. And it is obvious that agricultural land which provides an irregular income would not be valued so highly.

As a final note, Gaffney describes a proposal put forward in England for a centralised system of land taxation. Local governments throughout the country would be ranked in order of their land value per capita. The central government would then apply a surtax on local governments in a graduated scale starting from zero for the poorest locality and increasing to the richest locality. The local governments would collect the surtax and pass it on to the higher levels of government.

Should a Proutist economy replace income tax with land tax? The weakness of a tax only becomes apparent when one attempts to push its rate too high. At the present time, land taxes are typically applied at low rates by local bodies. It is not clear how they would stand up to being levied at the rates necessary for a broad based revenue collection by a central government. However economic efficiency arguments (for example the 2nd and 3rd principles of Prout, appendix 3) justify pushing land tax to the point where it encourages maximum utilisation of land without creating undue hardship and frequent changes of land use. Reduced income tax (i.e. increased disposable income) would offset increases in rents. If land and resource taxes are applied in combination, some consideration will have to be given to primary producers who both occupy land and consume resources.

18. Special Purpose Taxes

Special purpose taxes target particular kinds of economic behaviour. They may be justified as user pays taxes or as compensating for external costs. Examples of the former are water rates, sewage rates, road maintenance fees. Examples of the latter are punitive taxes on cigarette smoking and pollution taxes on consumption of plastic bags and fossil fuels. An interesting example of a punitive tax designed to have macro-economic consequences is the Tobin tax. It would discourage speculation on international currency markets and protect individual nations from its consequences. Punitive taxes are deliberately set at a rate which encourages tax avoidance. However there is a disturbing trend in recent years to tax people's weaknesses for revenue. The proliferation of casinos is an example.

In many cases it may be possible to establish the cost of the particular behaviour that a tax targets. For example, the federal government of Australia has estimated that drug abuse costs the nation \$34 billion per year, of which 80% is due to cigarettes and alcohol. [LDW, 2003] This figure should be compared with Australia's \$13 billion annual defence budget. The report also noted that revenue from tobacco taxes exceeded government expenditure on tobacco illnesses by almost \$2.8 billion and yet only \$2 million was spent on anti-smoking efforts. This is another disturbing indication of the use of punitive taxes for general revenue. Here it is worth commenting on the environmental movement's slogan that governments should only tax 'bads' and not 'goods'! This makes sense from a purely ecological point of view where, for example, a tax on plastic bags induces a substitution behaviour to use calico bags. However this approach can fail from a social perspective. The state governments of Australia obtain a large revenue from casinos, despite the fact that studies have shown gambling addiction to be a serious problem in Australia. From a theoretical point of view, the problem is that a person with an addiction is unable to adopt a substitute behaviour. Indeed, the government has an interest to maintain the addiction.

19. In-kind taxes

Taxes paid in the form of physical commodities or services are not usual in developed economies but they were normal in early civilisations which operated so-called *storehouse economies*. Surviving records of ancient Egyptian tax accounts written on papyrus can be viewed at the internet site of Duke University [DUS, web site]. The taxes were paid as barley and wheat by tenants of state and temple land. Totals and remaining dues were also listed in columns on the papyrus which suggests a well developed accounting system.

A difficulty with storehouse economies, in which all transactions involve barter and all taxes are paid in-kind, is that they do not scale well in size. They depend on centralised and immediately available information about supply and demand for commodities. Storehouse economies collapsed and monetary systems evolved because the information required to coordinate a complex economy was far too great to be centralised in ancient times. [Stodder, 1998, 2000] Money (from a root word meaning *to monitor*) is more convenient and efficient than barter because the physical exchange does not have to be balanced immediately. It is interesting to note however that there is a revival of interest in moneyless exchange because modern

communications offer the possibility of rapid and wide dissemination of information. In particular the internet is making large-scale information centralisation efficient and barter clearing houses are an emerging form of e-commerce.

Sarkar argues that both barter and in-kind payment of taxes still have a role in underdeveloped economies where cash markets are not well developed. In a discussion of agricultural taxation, Sarkar is critical of land taxes in India, both the present system and the *zamindari* system established during the British rule of India. The land tax is a fixed annual payment in cash regardless of the harvest. He notes that sometimes farmers cannot arrange cash because a proper market does not always exist to sell their produce.

“The best system of taxation was in vogue in the ancient Hindu age. In those days only twenty-five percent of the entire produce was given to the king as taxes. The farmers could also give cows, horses or sheep as taxes. In such a system farmers did not face any inconvenience. Today, however, farmers face much inconvenience because they have to pay their taxes in cash. Farmers cannot always arrange cash by selling agricultural produce, because a proper market does not always exist.

“According to Prout, a certain percentage of the farmers produce should be collected as direct taxes. It is also convenient for the government to realise taxes in the form of goods, because it needs to store produce as insurance against future contingencies. Taxes in such a form can easily be distributed from government stores when the people are in need. Moreover, this system will easily meet the requirements of people in the towns and cities. Such a system can rapidly transform the Indian economy.” [Sarkar (9), 1992]

Part 3: Practical issues

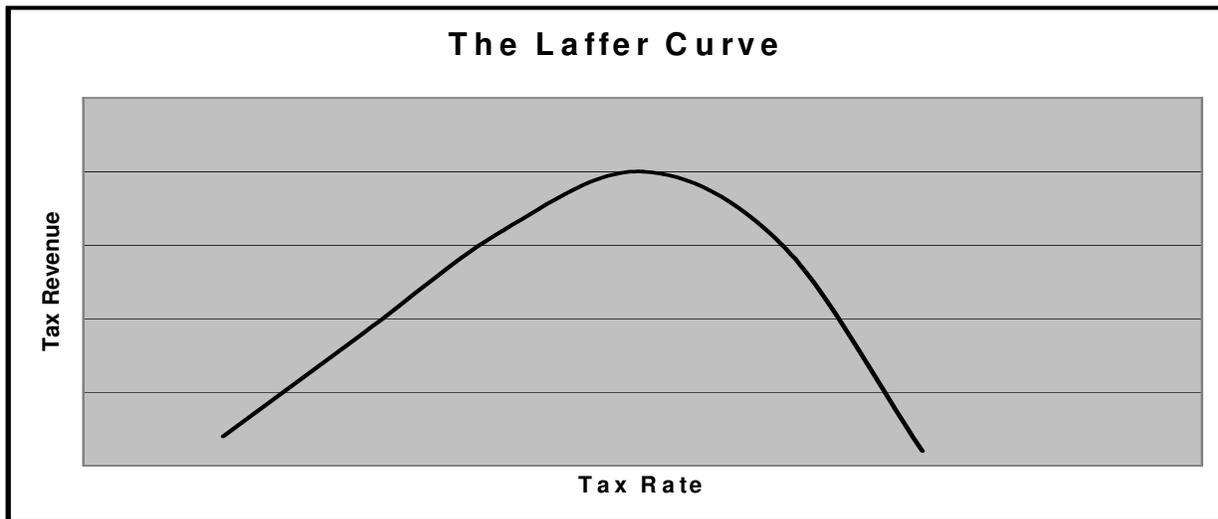
20. How much to tax?

Increasing the rate of a particular tax, incurs two kinds of trade off, a *revenue - avoidance* trade-off and a *cost - benefit* trade-off. Understanding these two trade-offs is necessary in order to maximise the effectiveness of a tax.

With respect to the revenue-avoidance trade-off, it is obvious that *potential* revenue will increase in proportion to the tax rate. However attempts to avoid the tax will also increase. It can be shown that the dissatisfaction caused by a tax increases faster than in simple proportion to its rate. Dissatisfaction can be given a monetary value by measuring changes in prices and purchasing behaviour. In simple economic models of taxation, dissatisfaction increases with the *square* of the tax rate. And of course dissatisfaction leads to tax avoidance. At low rates, dissatisfaction is minimal and small increases in the tax rate can increase revenue almost proportionately. However, there comes a point where tax avoidance behaviour exceeds the revenue effect and total revenue starts to decline. This relationship between actual revenue and the tax rate is known as the *Laffer curve* (see diagram).

Knowledge of the Laffer curve is obviously crucial for broad base revenue gathering taxes. It tells us two things. There is a maximum revenue that can be gathered from any single tax and

there is an optimum rate if the purpose is to gather revenue. The location of this point depends on the commodity being taxed and the availability of avoidance strategies. The demand for luxury goods is typically *elastic* precisely because they are not necessary. Any significant increase in price will decrease demand. However demand for essential commodities such as basic foodstuffs is *inelastic*. Taxes on these items will not greatly decrease demand and will affect the poor significantly more than the rich. We have noted that flat rate sales taxes and land taxes are considered to be effective precisely because avoidance strategies are difficult to implement.



The second trade-off is the cost-benefit trade-off. Recall that the purpose of many taxes is to compensate for the external or social costs of a particular economic activity. Furthermore, placing a tax on an under-priced commodity can increase the efficiency of its use. For example, we noted that land value taxation can have two conflicting effects. It can flush out underutilised land (a benefit) but it can also lead to inefficiencies if land is forced to change hands too frequently (a cost). At low rates of land tax, the increased efficiency of land use is the dominant effect. When the the tax rate is too high, the inefficiencies become predominant. Somewhere between these two is the optimum.

The cost-benefit trade-off is of particular importance for eco- and resource taxes, whose purpose is to offset external costs by increasing resource productivity and decreasing consumption. The first step in setting an eco-tax is to establish a target level for consumption of the commodity in question and this depends upon a cost-benefit trade-off. Consider the specific example of a *carbon tax* whose intention is to reduce the consumption of fossil fuels. Each reduction in carbon dioxide (CO₂) emission is an incremental improvement in the environment (a benefit which may or may not be quantifiable). However there is also a cost because research must be done to find alternatives to carbon fuels and the alternatives taken up will have their own inefficiencies and detrimental effects. But of particular importance is that the benefit from each percentage decrease in CO₂ emissions becomes less and less while the cost becomes greater and greater. The cost and benefit curves have a point where they cross and that is the level of CO₂ emissions that we would like to establish, that is, where the marginal benefit and the marginal cost are equal. This point maximises overall welfare.

The only problem with all this beautiful theory is that both curves are impossible to quantify! They depend on many assumptions and unknown variables. They depend on what you consider to be a cost or a benefit and they depend on how much importance you attach to each effect. Nevertheless there is a trade-off even if it is not quantifiable and the cost-benefit relation should be kept in mind. There is a limit to how much cost can be accepted to improve the environment. Of course, in some cases where a pollutant must be eliminated (as for instance CFC's) then the taxation mechanism to influence market forces is irrelevant. Such substances should be banned by legislation. In other cases, government controlled rationing may be more appropriate.

Once a target level for the consumption of a resource or production of a pollutant has been established it is then necessary to set a tax rate that will achieve the target. Let us suppose that the government accepts a target of the Intergovernmental Panel on Climate Change (IPCC) to reduce CO₂ emissions by some fixed percentage. The question becomes which energy prices will have to increase and by how much? This answer to this question depends on the elasticity of demand for the different fossil fuels. It is possible to get a good estimate of this elasticity because the cost of energy varies greatly around the world and it turns out that there is a strong inverse correlation between prices and per capita consumption of energy. In other words, the demand for fossil fuels is elastic and will be responsive to the imposition of a tax. Armed with this information, it is possible to calculate the required tax rate. Such a tax should be introduced gradually to allow time for scientists and engineers to discover more efficient ways of using fossil fuels and to find alternatives. Time must also be allowed for the existing capital stock to wear out, otherwise the capital losses for society could be large. Once the tax has been introduced, technological developments and adjustments in consumer behaviour must be monitored. In particular, careful observation will be required to detect undesirable changes in economic behaviour. The same calculations will have to be done for all resources subject to a resource tax. There is a wealth of information about the setting of eco-taxes available on the internet.[AH, ASE, ETR]

Another important factor determining the rates of individual taxes is the breadth of the tax base. One can imagine two extremes. One extreme is to have a single tax levied at a high rate. The other extreme is to cast a very wide net but levy each tax at a low rate. Not surprisingly there are advantages and disadvantages to both extremes. The single tax levied at a high rate has the advantage of simplicity particularly if it is a land tax. However a high rate of tax always invites avoidance and efficiency problems from which even land tax is not exempt. Levying a wide range of taxes allows the individual tax rates to be low so minimising the efficiency problems but collection and compliance costs begin to rise. A compromise would be a mix of taxes with low collection costs. Of the taxes we have discussed, land tax and retail sales taxes on commodities are easy to collect. Finding the appropriate level for resource taxes is difficult but the actual collection and compliance costs are not necessarily high.

21. Who collects the taxes?

Tax Collection in the past

Most of what Sarkar has written about taxation concerns systems of tax collection in historical India and other parts of the world such as Russia [Sarkar, 14, 15, 16 and 18]. For our purposes,

the main point of interest is the remarkable pragmatism that Sarkar displays when considering reforms of the tax system in India.

It was common practice in the past for rulers in all parts of the world to collect revenue from peasants via intermediaries. In India such intermediaries were known as *zamindars*. The system was a constant headache for Indian peasants because a fixed tax was levied by the zamindars each year based on area of land and without regard to the season or size of harvest. Furthermore, the zamindars used to collect more tax than they were required to pass on to the local ruler and hence they became social parasites. When the English arrived, they adapted the system to their own purposes but after independence in 1948, the zamindari system was replaced by a revenue department typical of a modern government.

Elsewhere Sarkar states his opposition to income tax and also to the system of tax collection through intermediaries [Sarkar, 18]. Yet about the abolition of the zamindari system he has this to say.

“The abolition of the Zamindari system has not been able to eliminate these drawbacks, rather it has adversely affected government revenue. Although PROUT does not support the Zamindari system, legalisation should have been passed to remove the inherent defects in the Zamindari system rather than abolish it. This should have involved curtailing some powers of the Zamindars and safeguarding the interests of the peasants. Legislation to this effect was passed in Bengal and goes by the name of the Bengal Praja'satwa Bill. It curtailed some powers of the Zamindars and accepted the rights of peasants as the owners of the land. In a backward country like India the government should not have nationalised the Zamindari system. Instead, it should have fixed a ceiling on bank balances and confiscated the savings of the Zamindars for investment in key industries. The huge margin between the revenue collected by the Zamindars and that paid to the state could have been reduced by imposing a tax like income tax on the personal income of the Zamindars.” [Sarkar, 15]

The pragmatism shown here is that the primary and immediate objective should have been to ease the plight of the peasants and at the same time to build the economy of India. While the long term objective may be to abolish personal income tax and taxation through intermediaries, the transitional policy must be practical and serve the immediate objective. Instead, the abolition of the zamindari system failed to help the peasants. It also failed to help the Indian economy because the wealth accumulated by the zamindars was not put to economically productive purposes.

Tax Collection Today

Prout promotes a policy of *economic decentralisation and political centralisation*. This policy has significant consequences for tax collection. It clearly implies the existence of a hierarchical political and economic administration such as exists in federal countries like the U.S.A., Canada and Australia. In any federation there is always the vexing problem of tax sharing arrangements between the centre and lower levels. In Australia, an annual meeting between the federal and state governments arrives at an agreement but given the greater political and economic power of the federal government, the outcome is inevitable. The Federal government collects all the tax and the states must beg. Are there any principles to guide a Proutist economy on these questions?

Let us consider a theoretical two level system consisting of a *centre* and the *regions*. Once again, it is possible to imagine two extremes. The centre could collect all the tax and distribute to the

regions, in which case the regions have minimal economic power. Or tax collection could be totally decentralised, i.e. collected by the regions who would pay taxes to centre. Such a system was proposed in our discussion of land taxes. There are advantages and disadvantages to both options. Prout promotes decentralised economic development and local control over the local economy. This cannot be achieved if local economic authorities have no control over the kinds and rates of local taxes. Recall that taxation provides social income for the building of social capital and to promote the local economy. The range of taxes and their rates must be allowed to vary from region to region. On the other hand, there are obvious inefficiencies in having multiple tax administrations. Firstly, the borders between regions having different tax rates will attract smuggling activity. Secondly, large scale business corporations spanning several regions will play one region off against the other for special tax breaks. And thirdly, some social goods, such as defence and national health campaigns cannot be managed at the local level.

The solution to these conflicting tendencies will depend on the specific situation and the political balance of the day. Although cooperation is the ultimate answer to all economic problems, we should be under no illusion about the slogan “*economic decentralisation and political centralisation*”. It has built into it all the friction and tension that fuels political life. There is no mathematical calculation to determine the economic balance of power between the centre and the regions. Nevertheless the different properties of the taxes suggests that some are more appropriate for central administration and some can be decentralised. For example, land value tax has the advantage of simplicity and low administration cost. Thus it is easy to decentralise and is a good revenue base for lower levels of government. If the system of land taxes was to be extended, then the higher levels could tax the lower levels on their *per capita* land value. By contrast, sales tax is more complex to administer but nevertheless has some other desirable properties. It is difficult to avoid and a flat rate tax does not distort consumer choices. These properties make sales tax appropriate for central administration.

Resource taxes are more complex. If the purpose of resource taxes is to compensate for external costs, then it must be kept in mind that these costs may be incurred locally and globally. For example, the external costs of burning fossil fuels are both local and global, acid rain and ozone layer depletion being the well known global costs. Global external costs can only be compensated by global administration and the expense involved in researching and monitoring resource tax rates also requires central administration. This suggests that some resource taxes should be collected centrally. By contrast, the costs of water consumption vary tremendously depending on the locality. It is obvious that water should attract a higher tax in arid climates than in the tropics. Furthermore in many cases, the external costs of water consumption tend to be localised. (Large irrigation schemes and rivers like the Tigris which cross multiple frontiers are obvious exceptions.) This suggests a strong local component to some resource taxes.

There are at least three possibilities here. The first is that each level of government estimates the external costs (at its level) for the consumption of a specific natural resource. The summed tax is collected and distributed to each level appropriately. The second is to identify two kinds of business - local and federal. Local businesses are registered within a region and are managed at the local level. Resource taxes levied on these businesses are collected by the regional administration and spent in the region. Federal businesses are managed at the federal level and

are taxed directly by the central or federal government. A third possibility is to distinguish strategic and non-strategic resources. Strategic resources would be controlled and taxed centrally because of their importance on the global scale. Gold, oil and uranium might fall into this category. Water might be a non-strategic resource managed and taxed locally.

In an essay, *Some Different Forms of Government*, Sarkar describes the practice of revenue sharing in federal systems such as India and implicitly appears to accept the third option above.

“A written constitution clearly defines the jurisdiction and rights of the federal state and the unitary states in areas like industry, energy production, irrigation, transport and communication. These things are partly given to the federal government and partly to the state government. Excise tax also rests partly with the federal government (on sugar, tobacco, jute, tea and coal) and partly with the unitary provincial governments (ganga, hashish, wine etc.) In India none of the four major cash crops and products (jute, tobacco, tea and coal) are in the control of the unitary states.” [Sarkar, 13]

Of course this passage is not to be read as the endorsement of a specific Indian tax policy, nor does it rule out other kinds of tax sharing arrangements. But it can be read as an acceptance of the tax sharing principle in a federal system. There is no guarantee that a particular mix of taxes will always and everywhere yield the appropriate level of taxes required by each level of administration. Thus, there will always be a need for meetings to reappraise the current tax sharing agreements!

22. Conclusions

Sarkar has written little on the subject of tax. Apart from his discussion of taxation in times past which offers interesting insights into his opinions, we must surmise his views on taxation in a contemporary Proutist economy from just a few passages. For example:

“Essential commodities will have to be entirely tax free. There will be no income tax. Instead taxes should be levied at the starting point of production.” [Sarkar (10), 1992]

“There will be no income tax, but there should be a tax levied on the production of each commodity.” [Sarkar (11), 1992]

“Prout advocates the abolition of income tax. In India today if income tax is abolished and excise duty on excisable commodities is increased by only ten percent, there will be no loss of government revenue. When there is no income tax, nobody will try to accumulate black money. All money will be white money. As a result there will be economic solidarity, an increase in trade and commerce, more investment, more employment and an improvement in the position of foreign exchange. Intellectuals should demand the abolition of income tax.” [Sarkar, 19]

“Taxes, levies, excise duties, etc., should be collectively paid by the cooperative, thus freeing individual farmers from financial pressure and economic exploitation. In many economically developed countries, there are no land taxes because the revenue collected from such taxes is only a very small part of the total revenue.” [Sarkar, 20] This paragraph is in the context of farmers cooperatives.

“According to Prout, a certain percentage of the farmers produce should be collected as direct taxes. It is also convenient for the government to realise taxes in the form of goods, because it needs to store produce as insurance against future contingencies.” [Sarkar, 9, pp.120]

All this conveys the impression that Sarkar accepts a variety of mechanisms to gather public revenue and enough has been said to derive the following basic elements of a taxation policy.

- 1: The gradual abolition of income tax phased in by gradually raising the tax free threshold.
2. The introduction of a rational system of resource taxes. Rational in this context means that an attempt is made to calculate resource taxes at rates which reflect the true costs of the resources concerned.
3. A system of sales taxes. Essential commodities and all services would be exempt. There are two advantages to these exemptions. Firstly, a simple retail sales tax on commodities is much less costly to operate than a GST. Secondly the effect of resource taxes will be to shift production from physical goods to services and one would like to encourage this trend.
4. Tariffs may be applied at Block or national level to protect fledgling industries producing essential commodities.
5. Taxation of farmer’s cooperatives should be a fixed percentage of their produce, thereby reflecting seasonal conditions.
6. In general it is better to tax businesses than it is to tax individuals.
7. To preserve social and economic stability, there should be a maximum ceiling on annual income and net worth. The management of these ceilings should be done in a psychological way, perhaps by allowing the wealth to go to favoured charities. It should be noted that the elimination of income tax and increased reliance on sales tax in a capitalist economy would *increase* wealth inequality. In a Proutist economy, income and net worth ceilings would more than offset this effect. Wealth tax is highly *progressive*.
8. Land taxes continue to be a suitable form of revenue for local government. If farmers are paying resource taxes, then some adjustment may have to be made to their payment of land tax. Land taxes could be gradually increased from their present level for local government revenue to provide additional income for the state level (i.e. the middle tier of government in a three level system such as Australia's).
9. An annual cooperative budget will calculate shares of GDP to government, business and households. In particular this means that the government should be able to set taxes at a level sufficient to fund its spending without borrowing.
10. Tax sharing arrangements between different levels of government must be part of the annual budget negotiations. Note that the combined effect of the above taxation policies would be to

divert revenue from the federal level to the local and state levels, consistent with the move to economic decentralisation.

11. In the established stage of a Proutist economy, an appropriate tax base would be resource taxes, sales and excise taxes and land value tax. Land tax would be collected by the local and state governments, sales tax by the federal government. Resource and excise taxes could be levied by all three levels of government as agreed between them.

12. A variety of user pays taxes, punitive taxes and other special purpose taxes could be levied consistent with social and economic policy.

In the end, much depends on the time, place and context. Any particular tax regime however, cannot ignore the basic principles that have been outlined in this article. And like everything else in Prout, taxation will always be subject to the principles of maximum utilisation and rational distribution for the welfare of all.

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Appendix 1: Social Capital

The term social capital is mostly used in an entirely positive sense, implying that it is associated in some way with human spiritual values. However the concept can mean different things to different people. The sociologist Robert Putnam adopts a broader definition in "Bowling Alone", his widely acclaimed critique of social capital in the 20th Century. Social capital, he says, consists of the "connections among individuals - social networks and the norms of reciprocity and trustworthiness that arise from them." [Putnam, 2000]

However there are many kinds of social capital just as there are many kinds of physical and human capital. The most important distinction Putnam makes is between bridging capital (or inclusive social connections) and bonding capital (or exclusive social connections). "Examples of bonding social capital include fraternal ethnic organizations, church-based women's reading groups, and fashionable country clubs. Other networks are outward looking and encompass people across diverse social cleavages. Examples of bridging social capital include the civil rights movement, many youth service groups, and ecumenical religious organizations."

From this perspective, social capital can be used for good purposes or bad. Bonding social capital can encourage a struggling cooperative to greater achievements. Bridging social capital encourages trade between strangers and distant countries. But bonding social capital can also be used to erect trade barriers. However in the end, Putnam sees social capital as an essential and ultimately positive driving force in a community. He draws on a vast array of new data that reveals how Americans have become increasingly disconnected from one another and how social structures -- whether they be PTA, church, or political parties -- have disintegrated. He describes the harm that these broken bonds have wreaked on physical and civic health, and reveals their power to create a society that is happy, healthy, and safe. Enthusiastic reviewers of "Bowling Alone" claim that it will do for community life what Rachel Carson's "The Silent Spring" did for the environment.

Putnam's approach to social capital corresponds to Sarkar's Neohumanist analysis of collective psychology. Sarkar also makes the basic distinction between narrow geo-and socio-sentiments that cement a group but tend to pit group against group, nation against nation and the inclusive neo-humanist sentiments which embrace not only humanity but plant and animal life as well. [Sarkar (2)]

Appendix 2: How would a wealth tax work?

People hold wealth in four major asset categories:

1. Homes (referred to as "owner-occupied housing");
2. Liquid assets, including cash, bank deposits, money market funds, and savings in insurance and pension plans;
3. Investment real estate and unincorporated businesses;
4. Corporate stock, financial securities, and personal trusts.

Other kinds of wealth such as cars, precious stones, paintings and personal effects may or may not be included in calculations of personal wealth. Debt consists primarily of mortgage debt (usually on one's home), credit card debt and consumer loans. (NOTE: For the purpose of claiming government welfare benefits in Australia, corporate stocks, financial securities, personal trusts and any asset that can be converted to cash within 28 days of unemployment, are counted as liquid assets. So the definition of liquid assets depends on the context.)

TABLE 4
Composition of Household Wealth in USA, 1989

	All families	Middle income families	The super-rich
Owner-occupied housing	28.5	68.6	6.6
Liquid assets (cash, bank deposits, money market funds, cash surrender value of insurance and pension plans)	17.1	17.0	11.0
Investment real estate and unincorporated businesses	29.4	7.5	45.1
Corporate stock, financial securities, personal trusts, and other assets	25.0	7.0	37.3
Total	100.0	100.0	100.0
Total debt	14.1	59.0	4.7

Middle income families are those in the third quintile-incomes between \$21,200 and \$34,300 in 1989. The super rich are families in the top one percent of the wealth distribution-families with a net worth of \$2.35 million or more in 1989. Figures taken from Wolff [1996].

The asset mix held by super-rich families and middle income families is quite different (see table 4). The very rich hold 82% of their wealth in investment real estate and corporate stock. However more than two-thirds of middle-class wealth is invested in home-ownership, a figure that often leads to the misimpression that housing is the major form of family wealth in the USA. Another 17% goes into monetary savings of one form or another. Together, housing and liquid assets account for 86% of middle-class wealth. Note how the average figures shown in the '**All families**' column of Table 4 disguise the differences between the very rich and the middle-class. This is particularly important when we consider debt burden (shown in the last row of Table 4). The ratio of debt to assets is very high for the middle income group (59%) due to home mortgages but only 4.7% for the very rich. Wealth, then, takes very different forms for the middle-class and the super-rich. These differences are important when we consider how taxes on wealth would affect different economic classes.

Wolff proposes that the United States should adopt a wealth tax along the lines of the Swiss system. All household effects, pensions, and annuities would be excluded from the tax base. In addition, a \$10,000 exemption would be provided on automobiles (that is, only more expensive cars would be subject to the tax). The basic exclusion would begin at \$100,000 -- only families with a net worth above \$100,000 would be subject to the tax. The marginal tax structure would look as follows:

\$100,000 to \$199,999: 0.05 percent

\$200,000 to \$349,999: 0.10 percent
 \$350,000 to \$499,999: 0.15 percent
 \$500,000 to \$749,999: 0.20 percent
 \$750,000 to \$999,999: 0.25 percent
 \$1,000,000 and above: 0.30 percent

Wolff has estimated the expected revenue from this tax regime for different income and wealth groups based on 1989 population and economic statistics. The estimates are shown in the right most column of Table 5. In addition, Table 5 shows the estimated income tax for each group and the percent of families in each group. The bottom row of the table displays the total income tax revenue for 1989 and the total expected revenue from the proposed wealth tax. While the US personal income tax produced \$446 billion in revenue (representing 11.7% of total family income), a wealth tax at these very low rates would have yielded only an additional \$32 billion (0.8% of total income). Nevertheless this is considerably more than the \$8.7 billion collected from estate and gift taxes in 1989.

TABLE 5
Who Will Pay the Wealth Tax?

	Percentage of Families	Average Income Tax	Average Wealth Tax
All families	100.0	4,790	347
Wealth class			
Under \$100,000	67.7	2,081	0
\$100,000 to \$249,999	18.2	4,978	176
\$250,000 to \$499,999	7.6	8,332	279
\$500,000 to \$999,999	3.6	12,421	848
\$1,000,000 and over	3.0	47,081	8,865
Income class			
Under \$5,000	6.1	0	17
\$5,000 to \$9,999	11.1	82	21
\$10,000 to \$14,999	12.1	388	57
\$15,000 to \$24,999	16.7	1,038	130
\$25,000 to \$49,999	30.1	2,875	154
\$50,000 to \$74,999	13.7	6,776	231
\$75,000 to \$99,999	4.6	11,478	614
\$100,000 and over	5.6	39,904	3,728
Addendum:			
Total revenue (billions)		445.9	32.3

Source: Wolff's calculations from the 1989 Survey of Consumer Finances. The figures are in 1989 dollars and based on the US population in 1989.

As is to be expected, the wealth tax is very progressive with respect to household wealth. Less than 4% of households, those with a net worth of \$780,000 or more, would pay more than \$1,000 in wealth taxes. It is also highly progressive with respect to income. Only the top income class

(\$100,000 or more of income) would pay more than an extra \$1,000 in tax. Wolff considers these beneficial equity considerations one of the main advantages of a wealth tax. The other plus is that the tax would be simple to implement because it could be integrated into existing income tax declaration forms. In other words, much of the administrative infra-structure already exists for a wealth tax.

It is primarily the efficiency considerations of wealth taxation that are disputed. Wolff argues that a wealth tax would induce individuals to transfer their assets from less to more productive uses in order to pay the tax. For example a wealth tax which included expensive cars might induce individuals to invest in income-yielding assets rather than cars which yield no (money) income. The counter argument is that wealth taxes discourage saving because the assets that result from saving cost more to own. Put another way, they earn less. Therefore a wealth tax encourages consumption or the holding of wealth in non-taxable forms. It is not clear *a priori* what the balance of these two effects would be, that is, more consumption or more efficient use of savings. Wolff argues that his calculations show “no compelling evidence that wealth taxation would strongly inhibit savings”. Stretton [1999, p 628] also supports the wealth tax and notes that Swedish capitalists paid a rate of 2.5% all through the decades when they established themselves among Europe's most successful manufacturers and exporters. One indicator of reduced saving would be reduced economic growth. A recent (2002) study by Hansson [2002] concludes that wealth taxes in the eight countries shown in Table 3 do indeed reduce growth, but the effect is very slight - about a 0.03 percentage point decrease in growth for each one percentage point increase in the tax rate.

Appendix 3: Five Principles of Prout

1. No individual should be allowed to accumulate any physical wealth without the clear permission or approval of the collective body.
2. There should be maximum utilization and rational distribution of all mundane, supramundane and spiritual potentialities of the universe.
3. There should be maximum utilization of the physical, metaphysical and spiritual potentialities of unit and collective bodies of human society.
4. There should be a proper adjustment amongst these physical, metaphysical, mundane, supramundane and spiritual utilizations.
5. The method of utilization should vary in accordance with changes in time, space and person, and the utilization should be of progressive nature.