Henry George School

6

Political Economy

This lesson will analyze the results of taxes levied on income and wealth.

TAXES WITH A FRONTIER: As long as there is free land, and wages are above subsistence, and interest is greater than an amount below which capital would not be loaned, and the tax is levied on production or distribution where the land is free, then it will diminish that which is taxed. The income tax, under these circumstances, will lower rent, wages and interest, so will a tax on products.

AVG. WEALTH EXPECTED	36	32	28	24	20	16	12	8
AVG. WAGE & INTEREST Income tax takes 25%	~~16~~ 12	~~16~~ 12	~~16~~ 12	~~16~~ 12	~~16~~ 12	~~16~~ 12		
POTENTIAL LAND RENT Income tax takes 25%	~~20~~ 15	~~16~~ 12	~~12~~ 9	~~8~~ 6	~~4~~ 3	—		
	land already owned					free land		

AVG. WEALTH EXPECTED tax on wealth takes 25%	~~36~~ 27	~~32~~ 24	~~28~~ 21	~~24~~ 18	~~20~~ 15	~~16~~ 12	12	8
AVG. WAGE & INTEREST	16	12	12	12	12	12		
POTENTIAL LAND RENT	~~20~~ 15	~~16~~ 12	~~12~~ 9	~~8~~ 6	~~4~~ 3			
	land already owned					free land		

TAXES WITHOUT A FRONTIER. As we have seen in previous lessons, the wages of the least productive workers tend to a bare subsistence. Simple logic tells us that if the government takes anything from them in taxes, they will starve, nothing will be produced, and the landowner will get no rent. Therefore, the landowner must compensate for taxes with higher wages.

Workers who are superior in their level of productivity, such as skilled artisans, chemists, and professionals, are paid whatever it takes to induce them to acquire greater knowledge and skill and perform at a higher level - not a penny more. It is not the gross pay, but the disposable, or spendable, pay that creates the incentive.

If taxes are levied on wage income, as they are in many cities, they will similarly be compensated for in higher gross wages and lower rent; or lower residential rent in cities where only residents pay the tax; or, under combined applications, some variation of the two.

The general rate of interest, with no free land, will fall to a point below which the supply of capital would not meet the demand (incentive to loan). Any taxes which diminished the incentive to store up and loan capital would diminish its supply, reduce production and therefore rent. So, interest must be raised to compensate for taxes on it.

In the following models these minimums taken together are represented by an average of 4 units of wealth.

Refer to the model below: the income tax is 25%. If on the best land, the owner gained 32 units of wealth, government would take 8, leaving the landowner with 24, and so on

AVG. WEALTH EXPECTED	36	32	28	24	20	16	12	8
AVERAGE WAGE & INTEREST: Below which production tends to stop - equals 4								
POTENTIAL LAND RENT Income tax takes 25%	~~32~~ 24	~~28~~ 21	~~24~~ 18	~~20~~ 15	~~16~~ 12	~~12~~ 9	~~8~~ 6	~~4~~ 3

The income tax also falls on wages and interest, but since wages and interest can't go any lower without removing the ability and incentives to produce, the landowners must compensate for taxes with higher wages and interest, and accept lower rent.

AVG. WEALTH EXPECTED	36	32	28	24	20	16	12	8
AVERAGE WAGE & INTEREST: Below which production tends to stop - equals 4								
POTENTIAL LAND RENT **Income tax takes 25%** **25% tax on labor & capital**	~~32~~ ~~24~~ 23	~~28~~ ~~21~~ 20	~~24~~ ~~18~~ 17	~~20~~ ~~15~~ 14	~~16~~ ~~12~~ 11	~~12~~ ~~9~~ 8	~~8~~ ~~6~~ 5	~~4~~ ~~3~~ 2

Taxes on wealth: buildings, sales, excise, imports, fuels, etc. These taxes simply confiscate part of production. In effect, they raise the cost of production. Without free land, these taxes simply diminish rent; wages of the least productive workers must equal subsistence, and as an incentive, all superior workers must be paid more. Only if the increase in the cost of production diminishes the demand for superior workers, or the amount of capital in use, can the tax diminish their wages or interest. It might be argued that taxes on luxuries, such as alcohol or tobacco, may actually discourage their consumption. They don't, however, discourage the overall desire to consume.

AVG. WEALTH EXPECTED **Tax on wealth takes 25%**	~~36~~ 27	~~32~~ 24	~~28~~ 21	~~24~~ 18	~~20~~ 15	~~16~~ 12	~~12~~ 9	~~8~~ 6
AVERAGE WAGE & INTEREST: Below which production tends to stop - equals 4								
POTENTIAL LAND RENT	~~32~~ 23	~~28~~ 20	~~24~~ 17	~~20~~ 14	~~16~~ 11	~~12~~ 8	~~8~~ 5	~~4~~ 2

In some cases, taxes which fall on production more than cancel the rent. This makes the land uneconomic for use. This is not often the case, but it can be seen within the slums of our large old industrial cities. Because the potential rent (potential profit of the landowner) is already very low, the added weight of taxes on wages, buildings, sales, etc. add up to more than the land is worth. That is to say: the total product after taxes will will be less than the prevailing rates of net take-home wages and interest throughout the economy. This is sometimes called a negative land value. We see evidence that it exists in cases where land is given up in lieu of taxes.

QUIZ:

1. Suppose that the United States could reduce military spending, and taxes were lowered by $200 billion a year. Would everyone's gross pay remain the same? (yes)( ); (no)( )
2. Suppose that the professional workers, those that earn over $40 thousand per year, were given a large reduction in taxes, to be made up by a commensurate increase in the corporate income tax. Would those professional workers ever get to spend the savings? (yes)( ); (no)( ).
3. Suppose we eliminated import taxes and because of a commensurate increase in exports it didn't put anyone out of work. Would the American worker enjoy a higher standard of living? (yes)( ); (no)( ). *Answers on top of previous page.*

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