Europe's Fatal Affair with the Value-Added Tax

In August, 2011, S&P lowered the credit rating of the US Treasury. We held our breath, thinking this might be the tipping point before a flight from the dollar. Congress, deadlocked and dysfunctional, seemed to deserve it — but it didn't happen. Mobile international capital saw something, spited S&P, and stayed with US Treasury securities. It seems that the USA must be doing something right — or at least less wrong than other nations. I would not breastbeat about "American Exceptionalism." I deplore our nation's faults, and our failure to face them and reform them. Nevertheless, it is foolish to preach that we must emulate Europe, when Europe is sliding downhill faster than we, and floundering as it slides.

I build a thesis around a simple, if partial, answer: the USA is the only major nation lacking a national-level sales tax (or VAT or GST). We raise a higher fraction of our combined national, state and local revenues from taxes on property, and income from property, and bequests of property. The fraction is not just a little higher, but plain to see even without the microscopes of modern theory and econometrics. (These myopic tools, indeed, often divert analysts into straining at gnats while they "swallow a camel.") True, our fraction of revenues raised from property has been trending downwards for half a century, but even so is still many times higher than in Europe,

or in most nations of the world.

We'll consider how things got this way historically, in Europe and in the United States, and then explore the economics of just how bad an idea the VAT is.

History of a dumb idea

Before the Enlightenment, and the Ages of Reason and Benevolent Despotism, Europe raised revenues from excise taxes, tariffs, and tolls. It built roads with drafted *corvée* labor. In England, Thomas Hobbes, a leading influence on the Stuart Kings, had pushed hard for taxes on what he called "consumption" (although neither he nor any later sales-taxer, to my knowledge, has defined "consumption" carefully enough to give the concept a clear meaning). Slavery, serfdom, peonage, and indentured labor were common. Prison labor was not unknown. Underpaid religious staffed schools and hospitals, hospices and asylums.

French King Louis XVI, briefly playing the benevolent despot, in 1774 appointed Jacques Turgot his Finance Minister. Turgot was fresh from his triumphs as *Intendant* of *The Limousin* (Limoges), where his physiocratic reforms, intelligently conceived and conscientiously executed, had converted a stagnant province into a thriving one. The Physiocrats wrote and preached, and Turgot the statesman acted for untaxing commerce and industry and raising revenues from land taxation. They coined the slogan *laissez faire* for their philosophy.

While at Limoges, Turgot published his *Reflexions sur la Formation et la Distribution des Richesses* (1766). This short, compact work contains much of the essential wisdom that Adam Smith soon was to popularize and expand with *The Wealth of Nations* (1776). Turgot stressed the important roles of capital, and free markets. He favored letting the market determine interest rates. He would combat poverty by relieving the poor of taxes, while raising revenues instead from taxes on the value of land — including lands traditionally exempt or undertaxed. He correctly observed that taxes based on land

values raise revenues without twisting and suppressing incentives to produce and invest. Smith visited France in 1766 and consulted extensively with Turgot, a man whose practical turn of mind made him a congenial tutor for Smith.

Adam Smith went on to ask why Spain, jump-started with gold pilfered from the New World, lagged in economic progress. He laid it on the Spanish *alcabala* and *cientos*: heavy sales taxes, their nominal rates magnified by cascading, that spared the grandees from taxes on their lands while stifling Spanish commerce and industry. They were just the sort of "broad-based" taxes which modern sales-taxers tout for raising more revenue, but under Philip II's *alcabala* and *cientos*, Spain declared national bankruptcy three times.

Many of America's "Founding Fathers" visited France as diplomats, and learned from Turgot. America's revolution against England meant friendship with France and Frenchmen. Turgot tried but failed to reform France in his day, but this French thinker and leader was one of our Founding Fathers in influence. The Commerce Clause of the US Constitution did for the new USA what Turgot had tried to do for France: it guaranteed free trade among the states. It created and has preserved our domestic market, the greatest free trade zone in the world, an essential ingredient of American productivity and prosperity.

However, in the new USA the Federalists under Hamilton first took control, and began levying excise taxes. In 1794 farmers of western Pennsylvania rebelled against a tax on their corn, which they marketed as whisky to cut down on transportation costs. Hamilton called on Federal troops to put down this uprising. The voters, when they found him dominating the subsequent cabinet of John Adams, and leading the country into the depression of 1798, retired his party and installed Jefferson, whose Virginia dynasty shaped the nation for the next 36 years.

These Virginians knew their Physiocracy. Jefferson, Madison and Monroe had all hobnobbed with philosophers in Paris and picked up their ideas. Monroe led the fight for the Commerce Clause,

freeing internal trade from excise taxes. Jefferson's physiocratic agenda was extensive: he wrote the Northwest Ordinance dividing public lands for privatization in small parcels, bought Louisiana, brought the Physiocrats Gallatin and DuPont into his circle, welcomed Tom Paine back from France and extended easy credit to small buyers of western lands. It was Madison, with all his faults, who masterminded the Constitution, and then, in the War of 1812, used the Federal power to tax property (a power he had so carefully circumscribed). They got the new nation off to a flying start.

The Confederate states, even though fighting to survive, stood on their states' rights against their own CSA government, and bucked an attempted CSA property tax. Jefferson Davis had to finance secession with excise taxes. So Davis put a 10% tax on all farm production, paid in kind — a crushing burden on marginal farmers. Winn Parish, LA, for example (the home of Huey Long) in 1863 petitioned General Grant to save them from this "oppression." The CSA repudiated its bonds and currency, and lost the war catastrophically. Following attempted Reconstruction, however, came Hayes, Reunion and Restoration of the old ruling class which ever since, first as Democrats and now as Republicans, has saddled the old Confederate States with the most regressive tax systems in the nation, featuring heavy reliance on sales taxes.

Before lands acquired in the Louisiana purchase were sold out, President James K. Polk acquired more lands clear to the Pacific, our "Manifest Destiny," as he called it. The USA became the biggest free trade zone in history, and prospered mightily — albeit erratically and prodigally, with giant-swinging cycles of boom and bust. We tied the parts together with ambitious long rails, but financed them with land grants that spared us from taxes. When the nation annexed lands from France and Spain and Mexico it left the private titles intact, but freed them from the repressive tax systems of those nations. Americans old and new grew accustomed to low federal tax rates, over a long period. State and local governments performed most public functions, and lived mainly on

property taxes, a kind of tax with no "taxable event" in its base and thus little, if any, disincentive effects.

Not until 1909 did the US turn to a corporation income tax, spurred by domestic demands for reform — and naval and military ambitions. The personal income tax from 1913 was carefully focused by Progressive Congresses on property income. Not until 1942 did Congress turn seriously to taxing wage and salary incomes, and withholding the taxes, and even then rates were graduated so steeply that property incomes, being in the top brackets, bore much of the brunt.

Since 1945 the tide has turned sharply back towards taxing labor more and property less, and yet even so America still taxes labor less, and property more, than most other nations. We stand alone — so far — as the nation with no national sales tax.

From Common Market to European Union and VAT

We pick up Europe's story in 1948. WWII left Germany devastated, but not for lack of money demand or purchasing power. Wartime rationing and price controls had left Germans with piles of cash in Reichsmarks. Ludwig Erhard, minister of finance under Konrad Adenauer, demonetized Hitler's Reichsmarks and replaced them with Deutschemarks as the new legal tender, lowering the effective money supply by 93%. German families lost not just capital goods, but their life savings. They were "ruined" — so it seemed. They didn't even have rationing tickets.

Erhard observed that the only rationing tickets they needed now were Deutschemarks, and they would work hard to get them. The same reasoning implies that they would also put their assets to work, if they owned any — and someone did own all the lands of Germany, and the surviving capital as well.

What followed was proclaimed a *Wirtschaftswunder*, but let us not call it a *Wunder* (miracle) for that suggests a supernatural cause, and stifles inquiry into real causes. It was unaccustomed

Armut (poverty) that drove Germans to perform. The first cause of poverty was the obvious: paying taxes to prepare for war, the total war itself, losing it, being bombed, then humiliated, occupied and plundered. Second, less obvious, was Erhard's repudiating Hitler's Reichsmarks. Economists who sympathize both with Erhard and private property may cover up the contradiction it by calling it "currency reform," but the naked fact is that Erhard's State simply stiffed its creditors, the German people, thus confiscating their private property without compensation. It came from recognizing that incentives come from *Morgen* (tomorrow) and are only dulled by the security and comfort of holding property in the accumulations of *Gestern* (yesterday). Yes, Erhard believed in free markets and incentives; decartelization and Walter Eucken and the Freibourg School were in vogue. Yes, Social Democrats discredited themselves by opposing Erhard, and it is good press to mock them for their doctrinaire myopia. But generations of conservatives since then have spun the story to blank out the role of state confiscation of private property.

Few would deny today that the desperate circumstances of the times necessitated radical "currency reform." Now that Erhard's policy is a *fait accompli*, safely in the past, few would deny its spectacular success. But let us learn the economic lesson. Taxes have two opposite kinds of effects. There are the marginal effects, the kinds that Laffer and a thousand anti-taxers preach, the disincentive effects of diluting the rewards of work and enterprise. But there are also the wealth effects, such as Erhard's "Miracle" demonstrated. Germany's experience suggests that the wealth effects may be stronger than the marginal effects. Certainly they are if we "play our cards right" and choose wisely among tax alternatives. The secret of raising revenues without damping incentives is to select kinds of taxes with powerful wealth effects and weak marginal effects. Property taxes come close to filling the bill, and even closer if we exempt capital improvements and movable capital (personal property) from the tax base. VATs, at the other pole, fit the Laffer model like a glove: strong effects on marginal incentives, and minimal wealth effects.

With the Marshall Plan the USA helped to rebuild Western Europe and Japan, with great success. "Social Democracy" was the slogan, to enlist proletarians in the common struggle against the Red Menace. Former belligerents buried the dulled hatchets of nationalism. French leaders like Jean Monnet and Robert Schuman proposed a United States of Europe, which would include the old Axis Powers, but not the USSR or its allies. France needed Germany to stop the USSR, and Germany was too big and robust for France to let go its own way again.

As the processes of European unification were getting underway, in the 1950s, the tide was turning back toward the attitudes of *l'ancien régime* with its taxes on merchants and their customers. Maurice Lauré, an engineer turned tax-man, got France to adopt VAT "to meet a fiscal crisis" (although that kind of spin accompanies most political moves). France introduced the first national VAT in 1954. It was not general, but was destined to become so, in 1968.

Charismatic Charles de Gaulle succeeded Coty, founded the 5th Republic, and presided from 1959-69. A fabled hero of *la résistance, Le Grand Charlie* could get what he wanted, and was President in 1963 when a Common Market committee on tax "harmonization" issued the landmark (Fritz) Neumark Report that found the French VAT to be superior to Germany's cascading turnover tax. The Committee agreed to make VAT the basis of tax harmonization within the growing EU. In 1968 France changed its VAT from partial to general.

Initial steps like European Coal and Steel Community and European Common Market grew to become the European Union. The 1957 Treaty of Rome created the European Community (EC), aka "The Common Market." In 1990 a commission led by former French Finance Minister Jacques Delors broached a single currency, a step short of political union. French President Francois Mitterand forced the Euro on a reluctant Germany as the price for France's support of German reunification after the Berlin Wall fell in 1989. The Maastricht Treaty of 1992 created the European Union (EU),

which adopted the Euro. Soon the EU doubled in size, to 27 nations, including eight former members of the Soviet bloc.

VAT spread quickly around the world. To enter the European Union, member states were required to adopt it. Latin America also went along. In a second push around 1990, industrial states like Canada, Australia, Switzerland and Japan came on board too, along with many "developing" economies in Africa and Asia, until today some 140 nations use VAT. They were pushed along by newly empowered international organizations like OECD, the IMF and the World Bank — probably not what their founders had in mind at Bretton Woods in 1944.

The USA has played an anomalous role. The Shoup Mission to Japan in 1949 had tried to pioneer VAT there, although in vain. USAID has spent huge sums promoting and subsidizing VAT in small nations. Only the USA itself has rejected VAT. Evidently there is a wide gap between our international representatives and the voters at home.

Europe after VAT: troubles and setbacks

Today, in 2013, Europe is staggering. Many of its nations face bankruptcy. Its stronger members, and institutions they dominate, seek to impose "austerity" on the resentful weaker members. Its banks hold mostly its governments' securities, crowding out the small businesses that create most jobs. Its unemployment rates are breaking records. Its tax collections fall ever farther behind the needs, threatening both the governments and their bank-creditors with insolvency. Real estate manias in nations like Spain and Ireland, new to the perils of prosperity, have collapsed, bringing banks down with them.

The debts of Greece, Italy and Spain are in the headlines, but many "stronger" nations also owe more than their revenues can well handle. Greece owes $315 billion, but here are the debts of some "strong" nations, in billions of $US: Finland, 101; Austria 230; Belgium 374; Netherlands 427; and France 1,835. Even Germany, supposedly the EU's economic bulwark, began showing signs of

stagnation in the 1990s, leading to the sarcastic epithet "The German Disease." Its debts are highest of all, at 2,086. The path of Germany's "Miracle" seems to be from unity and strength-through-defeat to disunity and weakness-through-success. Germany's claimed debt of about $2.1 trillion is rigged downwards by omitting huge pension obligations, estimated to add another $3 trillion to the total.

Governments' creditors are mostly banks, but these in turn are bailed out by the same governments to whom they lend, a spiral that will wind only downwards until and unless European governments find a way to raise tax rates without stifling tax bases. The whole structure rests, finally, on tax revenues; without them, it is just a house of cards. However, most tax bases fall when they are needed most, and the VAT base is falling fastest. In Greece, for example, public revenues have fallen 5% in the last year, while VAT revenues have fallen 15%. As credit ratings fall, required interest rates rise, so debt service rises, deficits rise, and debts keep growing, a disastrous vicious spiral. The expansion of the EU stopped late in 2012 when Bulgaria refused to adopt the Euro for fear it would be called on to bail out even weaker nations.

How did Europe and its fellow VAT nations reach this sorry state?

The economics of sales taxes: dubious virtues and real burdens

The idea keeps resurfacing that a sales tax is made neutral by virtue of being "general." Many great economists have refuted it, only to be inundated by floods of lesser voices in mass textbooks. Retail sales taxes, however "general" or universal in their apparent coverage, tax capital for turning over. Turnover is measured by the sales/capital ratio, which is highly variable among different firms, products, locations, stages of the cycle — and tax regimes, which economists influence. Sales taxes depress it heavily. This is not a mindless grouch at all taxes, for we need public revenues, and some taxes have positive effects. This is a rifle-shot at sales taxes, of which

VAT is one.

A major talking point among corporate spokesmen is that we must lower our corporate income tax rate, to make us "competitive" (today's buzzword). They give the impression that the income tax base is *gross* income. However, any income tax, personal or corporate, is less depressive, and has less excess burden, than any sales tax or VAT, however "general." That is partly because labor costs are deductible from taxable income. In addition, deducting capital outlays may lower the effective income tax rate on investing in new capital goods, often to zero and even below. As Turgot wrote, long ago, investing is "the beneficial and fruitful circulation that animates all the work of society...."

It is true that nominal corporate income-tax rates in the US have moved recently to the #1 rank among major OECD nations. That is not, however, because our rates have risen; rather, others have fallen. Italy's, for example, has dropped from 52% in 1962 to 27% in 2012, while Italy replaced the revenues by raising its VAT. If Italy had prospered, it might bolster the corporate lobbyists' argument. However, Italy has fallen to beggar status in the EU.

Today, US economists and pols of left and right are moving toward a pessimal consensus that lowering tax rates on business incomes (whose *rentier* components are not identified or quantified) is acceptable so long as Congress also closes "loopholes." Hardly anyone says *what* loopholes. It's important to realize that many loopholes, like fast writeoff and expensing of investing in creating new capital goods — genuinely "income-creating" spending — are exactly what made high rates of income taxation compatible with high rates of investing during the mid-20th Century.

Europe generally uses the "consumption-type VAT," meaning that capital outlays are expensible. This may have the effect of exempting the income of capital from the tax, although it is hard to find a comprehensible definition of "capital." If it includes land it is extremely discriminatory, and in any case favors more durable over less durable capital, and fixed over circulating capital. This should be

a major issue, but it is untouched, to my knowledge, in the literature.

Modern writers deplore the exemption of "services" from the sales tax base. These writers and teachers refer in their contexts only to labor services, ignoring the service flows of land or capital. This is not from ignorance: they know that the "service-flow" of an owner's home has long been included in NIPA as a form of income, income consumed by the owner-occupant as the real estate yields it. They just blank that out when it comes to taxing services to the "final" consumer.

The Mill Effect

John Stuart Mill in 1848, citing an even earlier finding by John McCullough, showed that a seemingly "general" sales tax would tax capital for turning over, and thus induce investors to favor the kinds of capital goods that turn over slowly. In Austrian terms, the tax induces investors to lengthen the "period of production," and thus distort the "structure of capital" in favor of "high order" capital goods, such as buildings. In Austrian cycle theory, this is a cardinal sin of public policy. Modern Austrian writers, however, almost unanimously, blame the problem entirely on low interest rates enabled by misguided central bankers. Something is missing there, and that something is tax policy.

Here is Mill's proto-Austrian case against a general sales tax:

> *"… if there were a tax on all commodities, exactly proportioned to their value, there would,… as Mr. M'Culloch has pointed out, be a 'disturbance' of values,… owing to … the different durability of the capital employed in different occupations. … In two different occupations … if a greater proportion of one than of the other is fixed capital, or if that fixed capital is more durable, there will be less consumption of capital in the year, and less will be required to replace it, so that the profit, if absolutely the same, will form a greater proportion of the annual returns. To derive from a capital of £1,000 a profit of £100, the one producer may have to sell produce to the value of £1,100, the other only to the*

> *value of £500.* (I.e., where capital is less durable, you must sell more gross to get the same net profit.)
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> *"If on these two branches of industry a tax be imposed... the one commodity must rise in price, or the other must fall, or both: commodities made chiefly by immediate labor must rise in value, as compared with those which are chiefly made by machinery.... "* (Principles of Political Economy, *1848, Book V, Chapter IV)*

How memorable is Mill's word "*Disturbance,*" 150 years before Darth Vader sensed a Disturbance in The Force! In Mill's and McCulloch's usage, "The Force" is value as determined in a market before or without taxes based on gross sales.

What Mill means by "capital" is clear from his memorable saying, "Capital is kept in existence from age to age not by preservation but by continual reproduction." Capital is not a specific concrete good, like a chair in the furniture shop. Rather, it is a quantum of value that we can, and normally do, keep existing by using the cash from sales to "meet the next payroll," as they say, to replace the chair. It needn't be an identical chair, or any chair at all, for capital in this transition is totally fungible in form and location.

Within each business there are also differences among kinds of capital. In a retail bakery, for example, there are pies and pie-shelves. The pies come and go, perhaps several times a day; the shelves last for years; the ovens for decades; the buildings even longer; the sites forever. Many a needy widow with hardly any capital has earned her mite by baking, while renting the site, building and hardware. Her sales/capital ratio is high in contrast with that of the landlord, and orbital in contrast to, say, Georgia-Pacific or Weyerhaueser or Simpson or Ford's Roseburg timber corporations.

The case is even clearer when we compare two uses competing for the same land. Compare a parking lot with a cafeteria. Suppose both to be taxed on gross sales, including services. The inventory of fresh food in the cafeteria is taxed daily, as it sells out and turns

over. The payrolls are taxed daily too, for they add to the gross value of sales. The value their labor adds to the purchased stock of food is capital, too: "working capital" — thus, the sales tax is mainly a tax on labor. The gross sales of parking lots, at the other extreme, include no turnover of capital at all, unless perhaps a minuscule Capital Consumption Allowance (CCA) on the paving and striping.

The business with more turnover pays more sales tax per dollar of capital invested. The tax drives away capital that turns over fast, and reallocates the land to capital that turns slower, or to uses requiring less capital, or no capital at all, like the parking lot. As to the lot itself, it never turns over in the relevant sense of wearing out and being replaced.

Curiously, many Georgists, though they are relentless critics of holding land idle, as well as of taxes with excess burdens, do not connect these two goals in one consistent system. Sales taxes inhibit using land intensively, if at all. Chemists have a good vocabulary for it. Land in production is like a chemical "catalyst" — it facilitates a process without disappearing into the product. Its "quantum of value" remains intact in the land. Working capital is, at the other extreme, like a "reactant." Its corpus and its quantum of value go into the product. That means they get sales-taxed with each turnover — the basis of the Mill Effect.

Hydraulic physics and engineering provide an excellent illustration, ably expounded by Robert Dorfman in a 1959 article I cannot praise too highly. Dorfman whimsically calls it "The Bathtub Theorem," and properly acknowledges Knut Wicksell's priority with his "grape-juice model." The average transit time of a molecule of liquid through a reservoir is basically the fund/flow ratio: in economic terms, the capital/sales ratio. For the lady baking pies and selling out daily the annual ratio is 1/365. For the boreal forester the annual ratio is 70 or more. The difference of 26,000 times starkly illustrates the Mill Effect. For doubters and masochists Dorfman provides many equations, but ends them delightfully saying "It is nice that this elaborate calculation is really unnecessary."

J. S. Mill hid this light under a bushel, offering just one example of a small difference, which was easy to overlook in passing — as later standard-brand economists have done. We should, rather, set this light in a tower on a hilltop as a beacon sending its gleam across the wave to save the foundering ship of state.

VAT and the Ramsey Rule

Most standard textbooks tell us that a truly general retail sales tax, unlike an excise tax, is neutral as between one commodity and another. A national tax is also neutral between locations, since it is the same in one region as another. Those conditions are never approached in practice, but in the sales-tax canon that merely means reformers should extend the reach of the tax, as the EU does with its push for tax "harmonization" among member nations, meaning in practice that all should adopt a VAT. Sales-taxers in the USA keep pushing for ways to override the Commerce Clause in the US Constitution and let each state tax imports from other states.

However, the Ramsey Rule says that in order to be allocationally neutral, sales tax rates should not be uniform at all, but inversely proportional to elasticities of supply and demand. As A. C. Pigou put it:

> *If there is any commodity for which either the demand or the supply is absolutely inelastic, the formula implies that the rate of tax imposed on every other commodity must be nil, i.e. that the whole of the revenue wanted must be raised on that commodity.*

Pigou's reasoning leads straight as a guided missile to levying taxes ***exclusively*** on the value of land, because its supply is inelastic. Whether Pigou knew what he was saying we may never know, for he was guarded and cautious and often coded, like so many academics fearful of witch-hunters.

Richard Musgrave avoids the issue by leaving Ramsey completely out of his classic *Theory of Public Finance*. Many, indeed most modern academics square the circle by first citing and then misquoting the Rule. They apply it only to *demand* elasticities — even though

supply elasticities are clearly the more important part of the original rule. Allyn Young started this ball rolling in reviewing Pigou in 1929: "I shall assume that costs are constant. It will be unnecessary, therefore, to take account of elasticity of supply as something apart from elasticity of demand." The notable exception is Joseph Stiglitz, who often writes sympathetically of taxing land values.

More generally, sales taxes penalize high-volume low-markup marketing strategies as against their opposite.* Lest one turn up his nose at, say, Walmart, its low prices do not reflect low markup so much as low labor-service per dollar of inventory. It also provides acres of free parking, a service of land, like other big-box stores. Sullivan also notes that sellers in better locations, say Rodeo Drive, can have higher markups, so sales taxation favors pricier locations. New businesses with high startup costs can deduct them from taxable income, but not from gross sales. Clifford Cobb notes that ghettos have many barber shops and beauty parlors but few shops carrying commodities.

Down with sales taxes and VAT!

We are left with this: retail sales taxes tax capital for turning over. Turnover means replacement; and replacement sustains demand for labor. Replacement does not just depend on sales, it anticipates them, and thereby generates the consumer incomes that finance them. Turnover is the autonomous variable that takes the lead in the otherwise circular, and now vicious, circle of macroeconomics in which employers wait for consumers, while consumers wait for employers to hire them. Turnover is measured by the sales/capital ratio, which is highly variable among different firms, products, locations, stages of the cycle, and tax regimes. By taxing turnover, sales taxes shrink their own base. Arthur Laffer discredited this idea by letting his patrons apply it to all kinds of taxes; Murray Rothbard mistakenly applied it just to the property tax, the

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* Dan Sullivan points this out in his article "Sales Tax Destroys Commerce, http://savingcommunities.org/issues/taxes/sales/destroyscommerce.html

one major tax to which it does *not* apply because it taxes capital and land for standing still, not for turning over.

Jobs depend on turnover. Sales taxes, rampant and rising in our times, depress turnover heavily, and this depresses demand for labor — both the number of jobs and their pay rates. Property taxes have the opposite effect, and so may some aspects of income taxation. Taxes on pure land value are the best of all. Our main point here, however, is that if the objective is to make jobs and raise pay rates, sales taxes (and their twin, VAT) are among the worst possible choices.

The idea that Europe has reached the limit of its taxable capacity is nonsense. The Cold War wound down from 1989. Today the USA, the only nation with no VAT, bears the cost of policing and defending Europe, and most of the world too. For centuries, Europe poured its treasures into a series of internecine wars from which the EU has rescued it. Europe now enjoys a colossal Peace Dividend, one of the biggest and longest in history. The idea that this should lead to national bankruptcies is absurd and ridiculous on its face. The alternative hypothesis is that Europe's woes are endogenous. A major cause, as shown earlier, is heavy reliance on VAT — the main tax to which Laffer's warnings might apply — and the lack of substantial taxes on property or its income. The evidence of Europe's solvency and untapped taxable capacity is the high level of its land prices compared with ours. International buyers are paying record-smashing figures for homes in world-class neighborhoods like Woodside and Los Alto Hills, San Mateo County, for example, because our prices, steep as they look to us, are still cheaper and the quality of life may be better than in counterpart regions of Europe.

— Working paper, www.masongaffney.org.
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