American Journal of Sociology, Vol. 20, No. 6 (May, 1915), pp. 745-763

THE "WHY" OF INCOME

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I. THE DISTRIBUTION QUESTION

Few will dissent from the proposition that all incomes owe their origin to the productive processes. The question of vital importance to the student of income involves the reason for the payment of income. It is a truism that the incomes of different persons are different. Why are they different? It is a truism that different people receive incomes for different reasons. What are some of the reasons? As in any other scientific problem, so here the question "Why?" is of paramount importance.

The simplest and most obvious income relation would seem to be that existing between the participants in the productive process, and the returns which these participants receive in the course of distribution. "These individuals have taken a part in creating values. Now they receive a part of the values which they have created," makes good reading, but it is very far from jibing with the facts. An analysis of any productive operation (such as the production of a ton of coal) leads at once to the conclusion that the participants in production and the sharers in distribution are not identical groups. The theorem that all incomes owe their origin to the productive processes is not followed by the corollary that only those who participate in the productive processes receive income. Indeed, the receipt of income carries with it very different connotations. All goods owe their origin to the productive processes. Flour, sugar, shoe-laces, bricks, and the like, are made from some product of the land, by labor with the aid of capital. Services are likewise possible only while the person rendering service is being supported with food and clothes which the productive processes have created. Both goods and services owe their origin to land, labor, and capital. This is a very different thing from saying that the landlord, the laborer, and the capitalist should share in distribution.

The modern economic world presents this significant picture: many people striving to create wealth and enjoying a part of the wealth which they create; other people, who have never participated in the activities of production, receive income. Infants, idiots, cripples, normal men and women whose hands have been eternally incased in kid gloves, and whose heads have been forever engaged with social pettinesses, receive liberal incomes from stocks, bonds, mortgages, or other certificates of indebtedness which they happen to possess, or which are held in trust for them. All producers receive income; but all income receivers are not producers, since many of those who share in the distribution of values assisted in no way in the production of the values which they share. Economists have sidestepped the issue by insisting that "it is the task of the theory of distribution to explain what causes, at last analysis, determine the size of these different shares."[1] This question is in truth but secondary to the main issue which concerns itself with the reasons for the payment of income.

There can be no simple contrast between activity in production and participation in distribution. Rather the problem must be dissected from an essentially different viewpoint. Perhaps it can be stated in the form of a question, "Why do certain proportions of wealth, created in the industrial processes, go to landowners, to owners of capital, and to workers?"

II. "PARTICIPATION" AS AN EXPLANATION

The old explanation was naïve and simple. Economists stated that land, capital, and labor participated in production, and that they therefore shared in the values which were created through the productive processes. It was but natural, the economists maintained, that the participants in the creation of values should enjoy the values created.

The concept is well illustrated in the writings of Francis A. Walker, whose book on *Political Economy* was for years looked

[1] H. R. Seager, *Introduction to Economics*, New York: Henry Holt & Co., 1904, p. 167.

upon as authoritative. Walker thus explains the phenomena of distribution:

In a primitive condition of society, the problem of distribution is a simple one. Three hunters join in an expedition, and at the conclusion of the day's or the week's chase, divide their game into three equal parts. If boys or cripples, or men of less than ordinary force or skill, are taken into the partnership, it is easily determined what portion of a full man's share each person shall receive.

In a highly organized community, however, the division of the product of industry into shares corresponding to the number of persons who have taken part in production is a very complicated problem.

For example, let us take the case of a cotton factory, at Lawrence, which produces in a given time a million yards of cloth. We may suppose that this is all woven in one piece, and that each person who has, in any way, contributed to the making of this giant web, advances in a certain order to receive his share. . . . .

Under the industrial system which we have taken for the purpose of the present discussion, we have four classes of claimants upon the product of industry, and that product is accordingly divided into four grand shares. These classes and the shares respectively received by them may be expressed as follows:

1. The landlord, receiving rent.
2. The capitalist, receiving interest.
3. The employer, or entrepreneur, receiving profits.
4. The employed laborer, receiving wages.[1]

Seager, in his *Introduction to Economics*[2] (1st ed., 1904), writes of rent as "the share of income that is assigned or paid to owners of land, sources of water power, and other gifts of nature which assist in production, for the use of these factors" (p. 206); wages as "earnings assigned to men for their work" (p. 222); and interest as "the share of income that is assigned to capital goods, ... for the part the latter play in production" (p. 224).

The term "participated," as it was used by the early economists, really meant "were necessary to." The most cursory study of industry showed that no productive activities could be carried on without natural resources, tools, and labor. In primitive society, to be sure, there were no tools or machinery—no capital in the modern sense. For the present-day production, however, all three

[1] New York: Henry Holt & Co., 1884, pp. 161–67.

[2] 3d ed., revised and enlarged, New York: Henry Holt & Co., 1906.

factors are necessary. Therefore, because land, labor, and capital are necessary to, or participate in production, they share in the values created.

There are two ways in which this question may be approached. It may be asked, on the one hand, whether there is any justifiable connection between "participation" in production and a share in the rewards of distribution. On the other hand, it is perfectly fair to ask whether the division of the distributive factors into shares called rent, interest, and wages, or into shares called rent interest, wages, and profits, is a workable classification. The argument may be sound which assigns to each of the participants in the production a share in distribution. At the same time, the available economic facts may be of such a nature as to make virtually impossible an income study based on such a classification. As a matter of fact, the division of the distributive shares into rent, interest, and wages is not even justifiable on a historical basis, while for the purposes of the present discussion it is so much worse than useless that it is both misleading and mendacious.

There seems to be some faint historic justification for the division of distributive shares into rent, interest, and wages. There was under the feudal system a landlord class, which lived upon the rent of its properties. The rise of commerce and industry developed a capital class, which secured interest in return for its capital or money. There never was a time, however, when the return to the landlord was rent, pure and simple. There were improvements on the land, and, under any economic theory, the return on these improvements was interest. There never was a time when the capitalists did not depend to some extent, and generally to a very large extent, on natural resources for their "interest." No capitalist venture is conceivable that is not founded upon natural resources, and in every great capitalistic enterprise resources play a leading part. Hence a part of the return of the capitalists was rent. Crudely speaking, there was a landlord and a capitalist class. Accurately, there never has been a group in the community whose income was derived from rent exclusively, or from interest exclusively. The attempts to postulate such a situation as a basis for argument is historically unjustifiable.

The question of the historical justification of dividing distribution shares into rent, interest, and wages, is, on the whole, trivial. The real point in the discussion concerns itself with the questions as to whether there is any real connection between "participation" in production, and sharing in distribution.

On the face of things, there is no reason why the various factors which participate in production should share in the values created by production. The rain, wind, and sunshine which assist in the growth of an acre of wheat are not for that reason rewarded. The sheltering rocks and cliffs which surround a natural harbor make commerce possible, and yet even in modern civilization such rocks and cliffs do not participate in the profits of the commerce which they so ably protect. The Mississippi River and the Great Lakes are an invaluable aid to internal commerce; no reward is paid to them for their assistance. Indeed, we, in the twentieth century, do not even pour out libations and offer up burnt offerings to our natural benefactors as did our ancestors in Greece and Rome. We take the climate, the harbors, and the rivers for granted. Participation in production is in no sense a conclusive argument in favor of participation in the distribution of values created in the productive process.

There are, of course, circumstances in which these natural resources might be said to participate in distribution. A band of pirates, taking possession of a fastness, levies tolls on the merchantmen that pass by that way. The mediaeval barons perched their castles on promontories, overlooking the great highroads, and held up the caravans that used the roads. In modern times an enterprising fellow gets possession of a strategic bit of water, and sells it to the community as a source of water supply. A private company secures possession of a water-power site, which it is willing to dispose of for a consideration. Coal lands, on government tracts, are secured free by individuals, and promptly sold for a price. The tendency, in commerce at least, and probably in the use of water power as well, is to give the government control over navigable rivers, over harbors, and over water-power sites, leaving them open to public use, upon the payment of a cost price for the privilege. Civilization has outgrown the practices of piracy and highway robbery. The feeling is already strong against allowing the owner of natural resources to molest the community. Those natural gifts which are needed in industry, particularly in commerce, which was the earliest economic activity operated on a large scale, are looked upon as public or social property. In no sense do they share in the values which the productive process creates.

III. "PRODUCTIVITY" AS A MEASURE OF INCOME

The idea of an income paid for mere "participation" was so primitive that it was of necessity replaced by a more rational explanation. The newer school urged that land, labor, and capital shared in the distribution of values because of their "productivity"; furthermore, that under normal conditions productivity was the measure of the share which each received. Thus an acre of wheat, grown on land with the assistance of machinery by the application of human labor and ingenuity, would sell for a certain amount. This amount then would be apportioned between the land, the capital, and the labor in accordance with the value of the contribution made by each of these factors in the process of raising an acre of wheat.

The theorists who insist that "productivity" is the true cause for the payment of income have variously stated their positions. John B. Clark, one of the leading exponents of the doctrine, summarizes his position in these terms: "Where natural laws have their way, the share of income that attaches to any productive function is gauged by the actual product of it. In other words, free competition tends to give to labor what labor creates, to capitalists what capital creates, and to entrepreneurs what the co-ordinating function creates."[1]

Seager sets out to prove the thesis that "competition tends to secure for each factor in production a share of the product equal to what it itself creates."[2] The issue has been clearly defined and elaborately defended.

[1] *The Distribution of Wealth*, New York: Macmillan, 1899, p. 3.

[2] *Introduction to Economics*, p. 167.

The explanation is plausible, but it leads naturally to a question, namely, "What will be the measure of productivity?" Without the acre of land on which to grow wheat, there could be no wheat grown. Without the labor, no crop could be raised or harvested. Capital has become an essential in agriculture. How shall the productivity be determined? The answer made by the productivity school is that the measure of productivity is the difference between the product of a marginal acre, and of the acre under consideration. A marginal acre is an acre which raises a crop of wheat so small that if it were smaller the acre must necessarily be abandoned as a non-paying investment. This explanation does not in any sense explain why one piece of land returns a larger crop than another piece. The answer to that question is apparent. One piece of land yields a larger crop of wheat than another because it possesses greater fertility, or a better location with regard to the market. There is still no conclusive answer as to the measure of productivity in either land, capital, or labor. The distribution problem remains. Some pieces of land command higher rents (receive larger shares of the value produced) than others. Some investments of capital pay higher returns (receive a larger share of the values produced) than others. Some expenditures of labor energy are more highly compensated than others. Why should this be so?

Land shares in production in only one limited sense—it grows things. Wheat is planted in the ground; the moisture expands it; the heat encourages it; it sprouts, develops, and produces a crop. Thus the climate, the fertility and the texture of the soil aid actively in the production of a crop. The same thing is true to a less extent in the growth of forests. It is likewise true to an infinitesimally small degree in the deposits of minerals and fuels and the water-power and transportation facilities. Nature may still be making coal and iron; she is certainly carving out rivers and harbors. For the purposes of the present generation, however, the water power, the coal, the iron ore, the petroleum, and the soil fertility exist. They are not made from year to year, or from century to century. For ages they have retained their present form. In terms of human life, they are permanent and fixed.

Return for a moment to consider the case of a coal mine. Is there any sense in which a coal vein participates in production? To be sure, no coal could be mined if it were not already in the vein. On the other hand, if the American Indians still dominated this continent, the coal would lie inanimate, and would remain so while the Redskin civilization continued. The coal is a gift of nature, a resource—essential in the production of heat and power, and therefore to the continuation of industry; but surely no one can assert that the coal takes any active part in the productive process. Nevertheless, the owner of the coal demands a return for his coal because he is the owner. From the standpoint of production he has no other claim to a share of the values produced.

There is another point worthy of consideration. If the service performed by the coal (its productivity) is the provision of heat and power, it is hard to understand why the coal should possess more value at one time than at another, unless it furnishes more heat or gives more power. Obviously, the only contribution which coal can make to the productive process is its contribution to heat and power. Granted that these are not increased, its share in the values of production should likewise not increase. It is interesting to note, however, that the owner of coal properties has been taking a continually higher toll during the past two decades for the product of these properties. Men say that coal-land values have risen with great rapidity, yet the part which a ton of coal can play in production has not increased. The coal yields no more of the heat and power which are essential to production, yet it demands and receives a larger share in distribution.

IV. THE MONOPOLY POWER OF OWNERSHIP

The secret of the value of coal properties and of coal lies in this fact, that the owner of the coal properties demands and receives a rent for ownership alone. That is, he can say to all mankind, "Pay me what I demand or let the coal stay in the ground." If he fixes his demand at a point where the coal can be used profitably, he receives the rent demanded, the coal is marketed, and the rent, be it large or small, is charged into the price. This rent charge exists because the monopoly power which the title to coal lands gives to the owner of these lands enables him to fix a price and to receive a return for his ownership of the coal land.

The monopoly power which land ownership gives is apparent. The acre of wheat land in Dakota is valuable. Why? Because the number of acres of equally fertile land is less than enough to go around. Timber land is increasing in value with great rapidity. Why? Because the timber supply of the United States is being used up faster than it is produced. Warm breezes, rain, and sunshine are free to all without the payment of any return. Why? Because there is a sufficient supply of them to go around. Spring rain and sunshine participate in the production of wheat equally with soil fertility. The fertile soil possesses rent value because it is so limited in amount that there is not enough for all. Air and sunshine possess no rent value because they are so limitless in amount that after each one has secured his share an abundant surplus remains.

Should productivity or monopoly power be regarded as the chief reason for the payment of a return to land for its participation in production? If productivity is the answer, then unless the actual producing power of the land increases in bushels per acre, or tons per square mile, it should receive no increased return. If, on the other hand, monopoly power is the source of the values which the landowner receives from the productive process, then an increase in population and an increase in the wants of people, irrespective of the productivity of the land, should increase the share which the landlord receives out of the products of industry. This latter hypothesis fits the facts exactly. The more people there are on a given area, the higher the civilization, and the more wants which people have, the higher will be the value of natural resources, and the greater will be the share which the owner of them receives, provided always that they are limited in extent and may be monopolized under the laws of private property. Rivers and harbors receive no share in distribution. Air and sunlight receive no share in distribution. Neither is subject to private property. Coal lands, timber lands, city land, agricultural land, all of these forms of resources which are the subject of private-property law show increased values, and receive increased shares with the development of society and the increase in population.

The matter may be looked at from a somewhat different angle. Here is a ton of iron ore, and there a gram of radium. The iron ore is worth a few dollars; the radium is worth thousands. What is the cause of the difference in value? Nothing more than the scarcity of one as compared with the scarcity of the other. The gram of radium has not assisted in production any more than the ton of iron ore has assisted in production. Iron ore is more plentiful than radium, however; therefore the owner of the radium, because he possesses a thing which is very scarce and in great demand, may exact a high monopoly price for his product. Natural resources share in the values created in productive processes only when they are subject to the monopoly of private property ownership, and only in proportion to their monopoly power.

V. THE MONOPOLY PRINCIPLE APPLIED TO CAPITAL

Capital like land is necessary to production. In the form of tools it participates in the productive processes. In the form of money and credit it likewise participates in the activities of industry.

The capitalist, by transferring credit at the bank, provides for the erection of a coal breaker; he does not erect the breaker himself. He merely gives into the hands of another a sufficient amount of purchasing power to enable him to hire the labor and buy the materials out of which the breaker is to be made. Nevertheless, the capitalist expects to receive in return for the use of his credit a share in the products of industry.

A coal breaker standing alone could never produce anything. The production of coal presupposes the activity of labor. In one sense, therefore, the breaker is not productive. On the other hand, the presence of the breaker greatly facilitates the mining and marketing of the coal; that is, the breaker is an aid in production. The capitalist does not erect the breaker, however. He merely owns the power to erect a breaker, and by giving directions that bank credit be transferred and a breaker be erected, he secures that result. On what grounds does the capitalist take a share of the values created in the coal? Merely because the amount of capital in the community is limited, and because the ownership of capital gives the owner the right to exact a return for his ownership. The economists who insist that capital shares in distribution because of its productivity overlook the fact that during the past hundred years, while the productivity of capital has increased enormously, the interest rate, or return to capital, has declined. At one stage in the development of the country, capital was extremely scarce and interest rates were high. Yet at that time a given amount of capital invested in a shoe factory actually produced fewer shoes than it does today. Nevertheless, with the passage of time, interest rates have decreased considerably. The explanation is easy. The amount of capital in the community has increased. Its monopoly power is therefore less; the risk incident to investment is not so great; and although a hundred dollars' worth of capital is more efficient today, judged by the number of shoes it will produce, the cost of securing that capital is considerably less than it was a hundred years ago.

The capitalist, like the landlord, receives a share in the products of industry. He receives a share because he owns capital. His share, moreover, is in direct proportion to the scarcity of capital in the relation to the demand for it. The monopoly power of ownership, and not productivity, determines that the capitalist shall receive a share of the values created in industry.

VI. LABOR MONOPOLY AS A DETERMINER OF WAGES

Labor is necessary to production. Labor supplies the motive force which animates industrial activity. Labor is the energizing and directing influence in the productive processes. Used as a term covering all forms of productive effort, labor is the life force of the productive machine. The landlord and the capitalist shared in the products of industry because of their ownership of land and capital; labor shares in the products of industry because it is expending energy on the industrial processes. Thus rent and interest appear to be a return for the ownership of wealth, while salaries and wages are a return for the expenditure of energy.

The amount received by labor for its share in production, like the amount of rent and of interest, is determined by the extent of its monopoly power, or by its scarcity. The unskilled laborer in a section of the country where labor is very scarce receives a given wage. In another section of the country, where immigrants compete fiercely with one another for an opportunity to work, a laborer expending exactly the same amount of energy and producing the same commodities, will receive perhaps a half or two-thirds of the wage paid to his fellow in the district suffering from labor scarcity. On the other hand, a laborer bargaining individually with a great corporation or a large employer is at such a woeful disadvantage that he can receive a wage little, if any, above the bare cost of subsistence. Organized into a powerful union, this same laborer can add perhaps 50 per cent to his wages. The experience of the building trades in various cities where there are unions and where there are not unions amply demonstrates the difference between the two groups of men. The man who can draw brilliantly, and in a style which is readily demanded by the public, secures an extremely high wage for writing advertisements. If there were ten men of equal ability clamoring for this position, it would pay a bare pittance. Witness the high returns to advertisement writers, and the low returns to poets, both groups of men having equal skill in their crafts. The wages of labor are returns in proportion to monopoly in exactly the same sense that the interest on capital and the rent on land are returns to monopoly power.

VII. SOME EXPLANATIONS BY ECONOMISTS

The facts in the case are so clear that one wonders why they have been so persistently ignored. Yet for a generation, a grist of economic books has been poured upon the market in which the subject of distribution is discussed in terms that might be employed by men knowing little or nothing about the facts of income distribution. Economist after economist has broached the question of distribution, yet the reader looks in vain for a reason consistent with fact as to why income is paid to land, to capital, and to labor. Theories galore, purporting to explain the proportions of values going to land, capital, and labor give in detail reasons for the varying payments made for different pieces of land and for different units of capital, but there is scarcely an attempt in the pages of generally economic theory to tell why rent is paid for land, why interest is paid for capital, and why wages are paid for labor.

Proudhon, Owen, Thompson, Marx, George, and a few others have set forth the reason in no uncertain terms, but the great majority of economic writers cover the pages of their books with inconsequentialities about relation and proportion, when the real question at issue is concerned with the very existence of the thing under analysis. Well may Cannan describe such treatment as "unscientific and illogical."[1] It is difficult to leave the subject with so mild a characterization. Cannan, indeed, puts the matter quite strongly:

> Before J. S. Mill wrote, the economists had nothing to say about the distribution of rent among landlords and the distribution of profits among capitalists, and what little they had to say about the distribution of wages among laborers generally took the form of a somewhat indiscriminating eulogy of Adam Smith's illogical attempt to prove the equal advantageousness of all occupation. Mill paid more attention to these subjects, but even he had no idea of representing the explanation of the causes of the community's income among its individual members as what it obviously should be, the ultimate aim of all discussions on the subject of distribution.[2]

Whatever the final outcome of the controversy over distribution, which was waged during the nineteenth century, it seems pretty clear that it will not lead to any consequences of importance. Complexity, intricacy, abstraction, and artificially created difficulties are not sufficient to justify a theory. There must be some basis in fact, where fact is available, and ultimately some application to the affairs of the world.

VIII. THE REAL ORIGIN OF THE "PARTICIPATION" IDEAS

The economists, dating from the publication of *The Wealth of Nations* in 1776, originally ascribed "productivity" to labor alone. "All of the wealth of the world was originally produced by labor," writes Adam Smith (Book I, chap. v). When Karl Marx attempted to demonstrate the labor theory of value, he found a rich field of material in the writings of the early economists.

No one has more sympathetically interpreted the "labor theory" attitude of this early school of economists than Edwin

[1] Edwin Cannan, *Theories of Production and Distribution*, London: P. S. King & Son, 1903, p. 381.

[2] *Ibid.*, p. 383.

Cannan in his *Theories of Production and Distribution.* After showing that Adam Smith used the terms "wages," "profit," and "rent" to mean the wages of labor, the profit of stock, and the rent of land, Professor Cannan writes:

When it is settled that the whole revenue of the community is composed of three great parts,—wages, profits, and rents—and it has been decided what revenues belong to each of the three parts, the next question seems to be into the cause of the division of the whole revenue into the three parts. Why are wages, profits, and rents obtained by those who receive them? No one seems to have thought of formally asking why wages are paid, or why labor is remunerated. It was considered "natural" that labor should be remunerated, not only by a part, but the whole of the produce.

"The produce of labor," he says, "constitutes the natural recompense or wages of labor. In that original state of things, which precedes both the appropriation of land and the accumulation of stock, the whole produce of labor belongs to the laborer. He has neither landlord nor master to share with him. According to this view of the subject the laborer receives a part of the produce because he produces the whole of it, and what needs explanation is not that he gets a part, but that he does not get the whole. Wages are natural and original, while profits and rent are artificial and of later introduction. We are left to inquire how and why profits and rent come to be deducted from the natural recompense of labor."[1]

Apparently the real problem before the modern economist is not the explanation of the proportion of the products of industry which goes in the form of interest and rent, but a justification of interest and rent themselves.

Appearances indicate that the followers of Adam Smith found the obstacles in the way of justifying interest and rent much more serious than they had expected. Professor Cannan ascribes to Senior an interesting effort to explain interest:

Senior was too able a man to try to make profits into wages, but he was desirous of showing that profits, like wages, are the remuneration of something and hit on the idea that they are the remuneration of the conduct or the sacrifice involved in "abstinence." "By the word 'abstinence,' he says, "we wish to express that agent distinct from labor and the agency of nature, the concurrence of which is necessary to the existence of capital, and which stands in the same relation to profit as labor does to wages." And again: "The words capital, capitalist, and profit" express the instrument, the person who employs or exercises it, and his remuneration; but there is no familiar term

[1] *Op. cit.*, pp. 199–200.

to express the act, the conduct of which profit is the reward, and which bears the same relation to profit which labor does to wages. To this conduct we have already given the name of abstinence."[1]

Whatever the situation may have been in Senior's day, nothing could be clearer at the present day than that interest is paid, not for abstinence, but for the ownership of capital. Capital may have been begged, borrowed, or stolen—it draws interest just the same.

The stories which many economists tell about savages abstaining from the consumption of fish or rabbits while they built a canoe or fashioned a bow and arrow make good reading, but they are peculiarly inapplicable to the present generation. Two hundred years ago, when the early settlers were subduing the continent, such explanations could have been listened to. At that time, when capital was scarce and hardship was universal, interest constituted, in a large sense, a return for abstinence. Those who had received interest had frequently gone without the necessaries of life in order to accumulate savings. How different are conditions today! Interest is still a means of compensating savers. It is also a means which enables men to live without working. People formerly saved in order to lay by for a rainy day. Today they save in order to secure a share of the products of industry—an income—for which they need expend no direct effort.

Certainly no student of modern financial transactions would regard interest as a return for abstinence or for saving either. It is very clearly a premium paid by the man who wants capital to the man who has it. In the face of the facts which industry arrays on every side, so eminent an economist as J. A. Hobson can write: "This extra payment (interest) was regarded by classical economists as a cost or price paid for an effort or abstinence." Abstinence is the correct term, Hobson insists, because it does suggest a painful effort involving some human cost, some play of motives naturally averse to saving which requires to be overcome by a positive economic payment.[2] On a preceding page, Hobson explains the motive behind saving:

It is of the first importance that the ordinary business man, to whom "saving" is apt to mean putting money in a bank, or buying shares, shall

[1] Cannan, *op. cit.*, p. 213.

[2] *Work and Wealth*, New York: Macmillan, 1914, p. 94.

realize the concrete significance of his action. What he is really doing is causing to be made and to be maintained some addition to the existing fabric of material instruments for furthering the future production of commodities.[1]

Were this argument correct, only those who had "abstained" would get interest. As a matter of fact, people are living in every country of the western world who have never abstained all of their lives, and yet who have been extravagantly supported by an assured income. Babies, inheriting paternal fortunes, receive interest. Business houses, investing surplus, receive interest. Interest is paid neither for abstinence nor for saving, but for the use of capital, with no reference to the manner in which a man came by it. Hobson's saver is really laying by a fund which, drawing interest at the current rate, will enable him to live without working.

The defense of rent is even more futile than the defense of interest. Perhaps before Henry George wrote his *Progress and Poverty* there were some satisfied souls who were able to find a justification for rent payment. There were many questioners, however, even in the early nineteenth century. Professor Cannan finds that, in 1814, David Buchanan, in his edition of *The Wealth of Nations*, challenges rent.

But in 1814, when everyone was thinking of protection, prices, and rents, circumstances were much more favorable. In that year the question was definitely asked in David Buchanan's edition of *The Wealth of Nations*. In a note on a passage in Book I, chap. vi, Buchanan observes: "Dr. Smith here states that the landlords, like other men, love to reap where they never sowed, and demand a rent even for the natural produce of their land. They do so. But the question is why this apparently unreasonable demand is so generally complied with. Other men also love to reap where they never sowed, but the landlords alone, it would appear, succeed in so desirable an object."

Buchanan does not succeed in satisfactorily answering his own questions. The price of corn, he thinks, is settled entirely by demand and supply, and the state of demand and supply is always such that the price is sufficient to yield a surplus above the cost of production, but he does not show clearly why this should be so. He seems to have thought that it is because the supply of food is "limited by the quantity of land which can be taken into cultivation." Rent is thus made the result of the "monopoly" of land: "The profit of monopoly stands on precisely the same foundation as rent. A monopoly does artificially what in the case of rent is done by natural causes. It stints the supply of the market until the price rises above the level of wages and profit."

[1] *Work and Wealth*, New York: Macmillan, 1914, p. 92.

As he believed that rent existed in consequence of the scarcity of cultivable land, Buchanan, in refuting the physiocrat's theory that rent is the only taxable revenue, was naturally led to insist on the fact that if it is "advantageous to those who receive it," it "must be proportionally injurious to those who pay it."[1]

There is yet one criticism which must be considered. Bearing in mind the early theories regarding the origin of value solely in labor, it is interesting to note, as Jevons remarks, that,

although labor is the starting point in production, and the interests of the laborer the very subject of the science, yet economists do not progress faı before they suddenly turn around and treat labor as a commodity which is bought up by capitalists. Labor becomes itself the object of the laws of supply and demand, instead of those laws acting in the distribution of the products, of labor. Economists have invented, too, a very simple theory to determine the rate at which capital can buy up labor. The average rate of wages, they say, is found by dividing the whole amount of capital appropriated to the payment of wages by the number of laborers paid; and they wish us to believe that this settles the question. But a little consideration shows that this proposition is simply a *truism. The average rate of wages must be equal to what is appropriated to the purpose divided by the number who share it.* The whole question will consist in determining how much is appropriated for the purpose; for it certainly need not be the whole existing amount of circulating capital. Mill distinctly says that, because industry is limited by capital, we are not to infer that it always reaches that limit; and, as a matter of fact, we often observe that there is abundance of capital to be had at low rates of interest, while there are also large numbers of artisans starving for want of employment. The wage-fund theory is therefore illusory as a real solution of the problem, though I do not deny that it may have certain limited and truthful application, to be shortly considered.

Another part of the current doctrine of economics determines the rate of profit of capitalists in a very simple manner. The whole produce of industry must be divided into the portions paid as rent, taxes, profits, and wages. We, may exclude taxes as exceptional, and not very important. Rent also may be eliminated, for it is essentialy variable, and is reduced to zero in the case of the poorest land cultivated. We thus arrive at the simple equation: Produce =profit+wages.[2]

Care has been taken to cite the criticism of men who are ranked high as economists. From outside of the professional ranks there

[1] Cannan, *op. cit.*, pp. 221–22.

[2] W. S. Jevons, *The Theory of Political Economy.* London: Macmillan, 1911, pp. 267–69.

sounds a perfect babel of anathema. The rhetoric of Ruskin, the front attack of Karl Marx, and the vigorous assaults of Henry George are notable illustrations of the opposition that classical economics has encountered. That these criticisms have already had a marked effect in turning the main stream of economic thought from wealth and production to welfare and consumption. There remains one major task for the champions of economics as a science. The theories of distribution must be revised to correspond with distribution facts.

The exigencies of the situation demand a new classification of the sharers in the products of the industrial system. Heretofore economics has distinguished between landlords, capitalists, and laborers, for the very absurd reason that at some time in the past, under an agricultural civilization, such a classification was supposed to have been accurate. Such a distinction was never particularly valid. Its greatest justification lay in its traditional origin. It was, moreover, an objective distinction. The same man might be a capitalist and a landlord. Indeed, according to the writings of the later economists, he might be capitalist, landlord, and laborer, too, paying himself rent and interest in addition to wages.

The time has come when a new classification of the reasons for paying income must be formulated. This classification will be based on function rather than tradition. It will be made personal and concrete, rather than impersonal and abstract. The new classification, instead of contrasting the returns paid to the various forms of wealth and to those who expend energy in production, will make a new alignment between the returns paid to the owner of wealth, on the one hand, and the returns paid to those who expend energy, on the other. That classification exists in fact in the contrast between property income (the income from property ownership) and service income (the income from human effort). The distinction between property income and service income measures the relation of the income-earner as an individual to the productive process. The capitalist and the landlord receive returns for the ownership of property; they therefore receive property income. The laborer receives returns for the expenditure of energy; he therefore receives service income. The distinction is not absolute. The amount paid to the laborer will vary with his monopoly power, just as the amount paid to the landlord and the capitalist vary with their monopoly power. The classification is, however, more accurate than the old one, in the sense that it applies more nearly to American conditions, and it is more absolute in the sense that it recognizes the distinct forms in which income is now paid.