Debt Death and Deadweight

CHAPTER 3

The making of a new Scottish Enlightenment

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THE restoration of a Parliament to Edinburgh has yet to reverse the fate of the people of Scotland. This is not a failure of the principle of the devolution of power. It is the failure of the political will to exercise the power that has been transferred from Westminster to Holyrood.

Under the terms of the Scotland Acts 2012 and 2016, members of the Scottish Parliament have the right to initiate a positive transformation of culture and society north of the border. This must begin with a national conversation about the need to reduce the damage caused by taxes such as those on their *earned* incomes.

By now (2017), the people could have granted a democratic mandate for that reform. And that would have empowered their elected representatives to plan the expenditure of additional billions on the welfare of the population.

The value of output could be increased by at least £6bn a year by swapping income taxation for a new levy on the rents of all Scottish sites. A proportion of those gains would be collected to fund public services. How this might yet be enacted at Holyrood is oulined in Box 1.

Instead, with the decline in oil revenues, people are repeatedly reminded that Scotland will endure an ever-increasing dependency on the fiscal generosity of Westminster. Must Scotland continue to mourn the loss of a bounty that is within its grasp – the additional revenue that would be created by the ingenuity of a population which, in the past, has demonstrated its creative powers under the most extreme adversity?

The current state of affairs has bequeathed a legacy of declining public services and continuing deprivation. Government refusal to collect wealth that is generated by the efforts of society necessitates the implementation of Austerity.

Government refusal to collect socially-created wealth is the single reason why we are, in Scotland today, constantly exposed to such headlines as:

'Westminster austerity hits poorest Scots families hard'
Single-parent families face losing more than £4,000 a year in benefit because of the UK government's austerity drive, according to a study by the Scottish government. Angela Constance, Scotland's social security secretary, said those on low incomes had been "targeted" by welfare changes since 2015, with families with children hit hardest. (*The Times*, 2 September 2017)

'Fewer than half of 13 and 14-year-old Scots pupils can write properly after decade of SNP government'
Figures from the Scottish Survey of Literacy and Numeracy (SSLN) showed "The deprivation gap in writing attainment did not change significantly between 2012 and 2016".
(*The Telegraph,* 9 May 2017)

'**Scotland's child health "among worst in Europe"'**
The State of Child Health – Scotland report compiled by the Royal College of Paediatrics and Child Health (RCPCH), found more than 210,000 children live in poverty, 28 per cent are overweight or obese, and around 400 die each year in Scotland – with a significant number of deaths potentially avoidable. The report also shows almost 30 per cent of pregnant women in the most deprived areas are smokers. (*The Telegraph,* 26 January 2017)

Box 1

Holyrood's route to Scottish renewal

The opportunity to cancel the first 1/6 of Scotlands £36bn annual deadweight losses has been open to Holyrood since April 2016 when the Scotland Act 2016 devolved to the Scottish Parliament the power to vary all rates and bands of Income Tax by any amount.

Since its inception, the Scottish Government has had the power to introduce a Bill establishing a reformed local government tax.

Taking these powers together, the option has been open to MSPs since April 2016 to substitute all or part of Income tax with locally-collected AGR (Annual Ground Rent aka LVT).

The reason why steps in this direction are a good idea is that at least £6bn of Scotland's deadweight losses (economic damage caused by Income Tax; but from which AGR is immune) would be cancelled, boosting Scotland's economy by that sum each year.

'Deadly health divide: Mortality rate in Scotland's deprived areas is double that in the wealthiest parts of the country'

A total of 1661 people per 100,000 died in the poorest areas compared with 815 deaths in the most wealthy. Figures released yesterday showed there is still huge inequality in Scotland with the death rate strongly linked to deprivation.
(*Daily Record*, 23 March 2016)

Box 2

Scotland's 1:1 deadweight taxes

Current taxes that drag down Scotland's economy and impoverish its citizens and culture are listed here. They inflict deadweight losses on Scots of at least £1 for each £1 of revenue raised. Which is how Scotland's annual deadweight loss may be estimated at £36bn (a conservative figure in the light of assessments by economists such as Harvard's Martin Feldstein, who put losses at more than double that).

Holyrood's devolved powers to reduce Income Tax in favour of AGR offer MSPs an epoch-defining opportunity to set out on a course which would turbo-charge wealth creation and start the process of equalising life chances in Scotland.

Revenue 2015-16	Scotland (£m)	UK (£m)
Income Tax	12,195	168,451
Capital Gains Tax	309	7,060
National Insurance	9,392	113,701
VAT	9,638	115,415
Corporation Tax	3,106	43,872
Corporation Tax Offshore	439	538
Bank Levy	222	3,392
Inheritance Tax	266	4,650
Stamp Tax on Shares	177	3,320
Insurance Premium Tax	226	3,293
Customs Duties	240	3,089
Swiss Capital Tax	3	32
Total	36,213	466,813

The following current UK taxes are not included above as, whilst they may include a measure of rent, their equivalents would be retained within or alongside AGR (Annual Ground Rent) because of their desired reducing effects on consumption, use of resources and pollution: Fuel Duties, Stamp Duty Land Tax, Annual Tax on Enveloped Dwellings, Tobacco Duties, Spirits Duties, Beer Duty, Wine Duties, Cider Duties, Betting and Gaming Duties, Air Passenger Duty, Landfill Tax, Climate Change Levy, Aggregates Levy.

Source: A disaggregation of HMRC tax receipts between England, Wales, Scotland & Northern Ireland, HM Revenue and Customs, October 2016.

Box 3

The Land Tax in the Treaty of Union

Act Ratifying and approving the Treaty of the Two Kingdoms of Scotland and England, January 16, 1707

Clause IX

> **'That whenever the sum of £1,997,763 8s 4 1/2d shall be raised in... England, on land... by a land tax... Scotland shall be charged... £48,000... as the quota of Scotland... by any tax on land.'**

It need not have been like this. Today's conditions are the legacy of a course of events that originated 300 years ago, at the time of the Treaty of Union. When the parliament in Edinburgh signed that treaty in 1707, Scotland was raising revenue with the aid of the Land Tax.

Seventy years later, Adam Smith, a professor of moral philosophy in Glasgow, recommended that the Land Tax should be the major revenue raiser (see box 4). He called it the (annual) ground rent. The reason why he advocated the rent-as-public-revenue strategy remains as true today as it was in the 18th century. Revenue from this stream of income would not damage the economy, and it would accord with the moral sensibilities of the population.

If Smith's advice in *The Wealth of Nations* had been followed, the Scottish Enlightenment of the 18th-century would have been protracted through to the modern era. Instead, as Westminster legislated to privilege the landlords, the people of Scotland saw their landscapes and native cultures contorted to suit the powers south of the border (see box 5). The interests of the peoples of the highlands and islands were sacrificed to the culture of Rent-seeking. The most visible immediate expression of this was the militarisation of the lines of communication for the purpose of pacification of the clans.

> **'The period of military building in the Highlands began in earnest in the 1720s following an assessment conducted in 1724 by, the then, General George Wade. Wade's analysis recommended the construction of roads, barracks and proper bridges to provide both north to south, and east to west access through the Highlands, with an aim to respond to, and suppress, local rebellions and uprisings, as had occurred during the Jacobite Uprising of 1715.'**
> (Hill and Gamble 2017).

The Highlands needed infrastructure to modernise the economy and to increase people's incomes. But the highways turned out to be one-way streets for the majority of people: they facilitated the exodus as communities in the islands and uplands were decimated by the lairds who claimed the clan lands as their own.

The Great Exodus

Historians describe the social transformation in suitably impersonal terms:

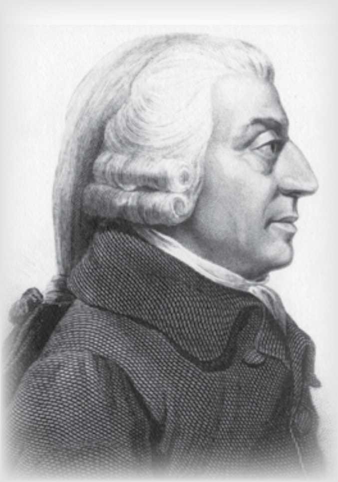
> **'Ultimately the new military roads were one aspect of the changing social and cultural state of the Highlands, with governmental, economic, and agricultural policies being responsible for depopulation, cultural assimilation, and changing social order.'**
> (Hill and Gamble 2017: 15)

But the great transformation had a singular purpose: privatising the rents that could be extracted out of the highlands and islands, and the impoverishment of the people. As the new elites moved in to build their villas and hunting lodges and pursue their country sports, the indigenous inhabitants were forced to abandon their ancient settlements for the lowland towns and cities, staging posts for many of them who shipped off to seek livelihoods on the other side of the world.

The Enlightenment of the 18th century, concentrated among a few intellectuals in the universities, occurred despite the channelling of the country's *net income* into the pockets of the lairds and the new class of gentry. What might have happened if those rents had been recycled back into the communities to benefit everyone (i.e. those who generated them)? We can begin to imagine what would have been possible by what happened in Australia.

Box 4

Adam Smith on Annual Ground Rent



'Both ground-rents and the ordinary rent of land are a species of revenue which the owner, in many cases, enjoys without any care or attention of his own. Though a part of this revenue should be taken from him in order to defray the expenses of state, no discouragement will thereby be given to any sort of industry ...Ground-rents, and the ordinary rent of land, are, therefore, perhaps, the species of revenue which can best bear to have a peculiar tax imposed upon them.'

The Wealth of Nations (1776) Bk V: 370

The loss of Scottish ancestral land rights triggered mass migration to the colonies. Not all of the migrants were voluntary exiles. Many Scots, driven to petty crime by their state of impoverished desperation, were among the 162,000 people who were despatched as convicts to Australia in the 80 years up to 1868 (McCarthy and MacKenzie 2016). But Australia was enriched by those Scots. Their impact on the emergent Australian society has been elegantly summarised to demonstrate the formative roles they played in discoveries and achievements in disciplines ranging from medicine to botany, geology to engineering; and then there was their contribution as pastoralists and civil administrators (Wilkie 2017). They helped to create what became, by the end of the 19th century, one of the most prosperous nations in the world. What might have happened in Scotland, if all of that talent had enjoyed the freedom to remain in their homeland communities?

- **The Islands** instead of being denuded of their peoples, would have flourished under positive influences. The islanders' full share of socially generated wealth would have been collected and re-invested in comprehensive local infrastructure, education and health services. The new revenue burden (AGR) would have reduced their liability to what they could afford to contribute – their surplus. Positive forces would have combined to boost their enterprises instead of destroying them, thus permitting islanders the freedom to continue to live there. Their enterprises and culture would have thrived instead of being crushed. Sustainable fisheries, including the herring fishery, would have continued to support island communities because managed licenses would have been auctioned to the highest bidders annually.
- **The Highlands** instead of the ancient forests being cleared to make way for sheep, would have thrived with the growth of villages into towns at scales suited to serve their inhabitants. The myth that populations were too high would have been exposed when highlanders were freed to supply one another's needs with unrestricted enterprise. The sporting fraternity would have been compensating society in full for the land reserved for its activities. Country sports would have evolved to live in harmony with communities instead of conspiring to render them piles of stones.
- **The great cities of the Lowlands** instead of being dumps for the transient populations displaced from Scotland's margins, would have expanded into ever more productivce centres of industry, art and culture. The absence of taxes on earned incomes, site improvements or trade would have initiated an unrestricted and growing wave of invention, innovation and technological

> advance. The attraction of investing in enterprise would have led to competition for sites for homes and businesses. Growth in site rental values would have provided a growing public purse available to re-invest in improved amenities and services in the interests of Scottish society at all levels and locations. Slums, poverty and social disintegration would have become unknown because citizen outcasts everywhere would have been reconnected to the stream of wealth they themselves create. Pollution would have been minimised by the forces of AGR.

These prospects were all contingent on the rents of Scotland being recycled back into the communities that created them so that life chances could be equalized across Scotland. Instead, that stream of income was congealed in the palatial dwellings constructed to serve the social status of the lairds, or funnelled into real estate and the stock market in London.

And so, instead of the emergence of an authentic Scottish culture in response to the aspirations of the population in general, through the continuous evolution of ancestral life into modernity, we observe the constructed mores

Box 5

The first privilege of UK membership

Joining the UK granted Scotland the privilege of investing in London and the Southeast. Scotland has continued to do so since 1707 in whatever proportion its tax contributions were of total UK revenue (currently between 7% and 8%).

Those annual investments by Scots tax payers helped raise site values in the wealthiest part of the UK far in excess of the periphery. Those substantial returns would have been collected and returned for use in Scotland via the Land Tax enshrined in Clause 9 of the Act of Union (Box 3). In which case the *UK Idea* would have worked for all its members, bringing prosperity to all areas.

Sadly the first privilege of UK membership was nulified by landlords in control at Westminster. At an early date the benign Land Tax was reduced. Then abolished and replaced with taxes that demanded more than could be paid at the margin. Life there was extinguished. The returns on the invested Scottish taxes were diverted into the pockets of London site owners.

People around the edges of Britain instinctively knew something had gone wrong. By this little-understood process – devised at Westminster – UK society was broken. Today large sections of the population at the economic periphery, including many Scots, remain effective outcasts. But the damage could even now be reversed by the adoption of AGR/LVT.

that accommodated the ambitions of the rent-seekers. Today, popular support for political independence is one expression of the quest for a new identity based on the legitimate demands of a population that instinctively knows something went very wrong a very long time ago with the mechanical workings of the UK.

What's to be Done?

The fiscal system of Scotland is not fit for a nation that wishes to renew its social contract. Attempts by the Scottish Government to reshape the taxation of property in Scotland have not proven fit for purpose.

The Land and Buildings Transaction Tax (LBTT) introduced in 2015 to replace stamp duty, has been blamed for its negative impact on the housing market. And a review of the methods used to forecast how much the levy would raise has been criticised as 'ill-suited' for analysis. The tax raised £156.7m instead of the predicted £235m. As a result, budget forecasts for tax from residential transactions were halved from almost £1.8 billion to £962m in total over the next four years (Sanderson and Bennett 2016).

A new beginning is needed, directed at reducing the artificial constraints on the creative powers of the population. That can mean one thing only: the untaxation of people's wages, savings and investments, and raising revenue from the socially-created rental value of each site. Scotland desperately needs Adam Smith's Annual Ground Rent.

With regard to the reform of Scotland's Council Tax, Andy Wightman MSP (a member of a cross party Commission tasked with researching its potential replacement) noted in a speech:[2]

> **'So this Parliament must be bolder...on...issues...such as the perennial imperative to reform local taxation. A cross-party commission recommended the end of Council Tax. The Scottish Government's own adviser on poverty and inequality, Naomi Eisenstadt, told the First Minister that she needs to be bold on local tax reform, introduce a new system that is, in her words, "genuinely progressive" and to focus on the bottom 40% of the income distribution in order to effectively tackle income inequality.**
>
> **Instead we still have the grubby, miserable and iniquitous Council Tax which even after recent Government changes will remain probably the most regressive tax in the UK where, according to analysis by Scottish Parliamentary Information Centre (SPICe), the bottom 10% of households by income will be paying around 9% of their equalised household disposable income in Council Tax, while the top 10% pay a mere 3%.'**

2. Politics, Parliament and Power: The case for a renewal of Scottish democracy. The Scottish Council for Voluntary Organisation's (SCVO) Stephen Maxwell Memorial Lecture delivered by Andy Wightman MSP, 8th December 2016 http://bellacaledonia.org.uk/2016/12/16/politics-parliament-and-power-the-case-for-a-renewal-of-scottish-democracy/stephen-maxwell

One of the voids in the statistical record is an assessment of the annual net income generated in Scotland. This calculation needs to be located in a survey of how the negative taxes reduce the sum total of rents that would otherwise be produced in Scotland.

Armed with an intelligent assessment of existing levels of net income, it becomes possible to explore the transitional measures towards creating a national budget that stands on the twin pillars of efficiency and equity.

Economists can initiate research projects that help people to visualise the possibilities of a bonanza emerging out of the lands of Scotland (Sandilands and Harrison 2015). Robust estimates are needed of the deadweight losses inflicted by the mainstream taxes favoured by Holyrood and Westminster. Such a measure would be the measure of the stream of value that is Scotland's most productive: the wealth created by all of us working together – the surplus identified by our earliest ancestors which made cooperation and social evolution worth the effort. It was and is worth the effort. Right up to the point where a subset of that society finds a way of diverting a part of that stream of value into its own pockets.

Box 6

Government analysis points to the mechanics required to achieve Scotland's renewal

It's not a secret. A candid Scottish Government document[2] outlines the potential economic harm that would come from increasing Income Tax.

If *"artificially shifting income, relocation, migration from Scotland, rearranging domestic affairs, loss in revenues, reduced attractiveness of locating in Scotland in the future and reduced potential economic and tax growth rates"* are *not* what we all want for Scotland, then it is clear that solutions lie in a direction other than that of inflicting additional burdens on (earned) incomes.

If, on the basis of the analysis in their document, the Scottish Government *reduced* its income tax rates, there would be *a reverse flow of people and investments into Scotland from the rest of the UK*.

This process would not be prejudiced by the simultaneous introduction of AGR (immune to deadweight losses), because the new fiscal-led economy would be a growing one, alive with the new opportunities for which investors are desperately searching. The AGR option is at hand, an option that promises to boost economy and culture at every level. So we are bound to ask:

> **Why does Holyrood fail to insist on a full declaration of deadweight losses attributable to existing taxes – compared to the impact of collecting AGR?**

2. *The impact of an increase in the additional rate of income tax from 45p to 50p Scotland* (March 2016). http://www.gov.scot/Resource/0049/00497818.pdf

The nation's surplus/net income far exceeds the value of Scotland's diminishing oil rents and is inexhaustible while the population lives. The surplus *includes* the oil rents. Not only does it take in the improved site values attributable to taxes invested in amenities, it also includes all of nature's services and resources, including those yet to be discovered or invented. As Adam Smith pointed out, its full collection 'to defray the expenses of state' cannot negatively impact on anyone's wealth-creating enterprise or (earned) income.

Were the Annual Ground Rent collected and harmful taxes ditched, the discourse over the future of Scotland would be transformed. At present, the London-based commentariat routinely ridicules Scotland for being in debt to England for financial transfers.

Spending per person in Scotland was £12,800 in 2015-16, compared with £11,500 for the UK as a whole. The problem is that Scotland's tax base is too small to pay for this, which means that it is racking up a massive budget deficit (funded by the English taxpayers) (Heath 2017).

Such observations are a statistical comment on the ugly realities of a fiscal system that has traumatised the nation for the best part of three centuries. If the philosophers of Scotland – those who would inhabit the glens of the highlands and the foreshores of the islands if the taxman got off their backs – can visualise a life of fiscal freedom, Scotland would not be in debt to England. It would pay its way, either on its own or as an equal partner in what would finally become a united kingdom.

That is why it was deeply disappointing to hear Scotland's First Minister Nicola Sturgeon announce on 5 September 2017 that her government will give serious consideration to increasing the rates of Income Tax. Such increases have been proposed by other parties. Increasing the tax burden on earned income would only damage Scotland further, inflicting yet more deadweight losses on Scotland, carrying the country further away from the potential the people could achieve under a humane fiscal policy. Yet, in the same speech the First Minister also looked in a different direction:

> **'We will continue to implement the 2016 Land Reform Act and shortly approve the first strategic plan of the new Land Commission. It will outline a programme of research to inform options for future change – for example, possible measures to tackle constraints on the supply and cost of land for housing, and possible tax and fiscal reforms, including the potential for some form of land value based tax.'[3]**

This is the way to go.

3. https://beta.gov.scot/publications/programme-for-government-2017-2018-first-ministers-speech/

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