

# Rethinking economics and taxation

## *The shift to a sustainable economic system requires radical changes in taxation*

Graeme Maxton

The “Report to the Club of Rome” which was published 2016 was entitled “Reinventing Prosperity”. At its core were 13 proposals which sought to improve social justice and ecological sustainability, as well as responding to the three major problems of rising unemployment, widening inequality and accelerating climate change. Nine of the proposals concerned taxation. The authors proposed new and different ways of imposing taxes, explaining how these could be used to boost state income without reducing well-being, directly reduce inequality and positively change social behaviour. Two years later however, none of the proposals made have been adopted, or even seriously discussed, while humanity’s social and environmental problems have worsened.

This essay provides an update. It draws on scientific experience, earlier publications and established academic standards and offers an insight into international governance practices. By its essayistic nature, this contribution does not try to reiterate or repeat what has already been said so often before, but to bind these insights together into an appeal for action by all those involved, namely each one of us.

The structure of this contribution is as follows: I start with a situational analysis, contrast it with the alternative economic sustainable system and then explain the role of taxation in getting there.

### Situational analysis

For most of the last 70 years, the world has experienced high rates of economic growth. While living standards have improved for many people in the rich world, this has come at a heavy cost, especially to nature. The gap between rich and poor has also widened, particularly in the last 30 years, and unemployment has increased, notably among the young. Species loss has accelerated (Ceballos et al. 2015) and climate change, which is a direct result of human activities, has become an existential problem.

These costs have been tolerated for two main reasons. First, the big corporations, the rich, as well as those in political power, and the finance sector, have benefited from the current system. This means that they have little incentive to change it. Second, most economists, lobbyists and think-tanks have continued to promote a Gramscian “common sense” (Crehan 2011) narrative across global society, which has encouraged people to think that it is economic growth that is the fuel powering human progress. Through this narrative, societies have been persuaded that it is economic growth that creates jobs, increases wages and boosts living standards. Coupled with current notions of democracy and freedom, economic liberalisation is depicted as the key to human development. If the market is left unrestrained and government interference is limited, goes the thinking, human progress will surge.

This narrative is false, however. Economic growth is not a precondition for human progress (Daly 2012). A focus on growth does not create jobs in the long term or reduce inequality. It mostly rewards the rich, and it creates enormous environmental destruction in the process.

Economic growth as a concept is greatly misunderstood. Growth is not the result of increased consumption, as many people think. Growth has two main sources: a rising population and increased efficiency. In the rich world, where population growth is very low, it is mostly the result of boosting efficiency. Growth comes from minimizing the value and volume of inputs (land, materials and labour) in order to maximise the value of outputs (production and profits).

One way to reduce the cost of the labour input is through higher levels of mechanisation and robotisation. Unless more work is created elsewhere for the people replaced by machines, which is difficult when there is free trade and jobs are moved to lower cost countries, long term level of unemployment rises. The surplus of people in the labour market also results in stagnant or falling incomes, as well as declining job security. As a result, the drive for economic growth has a tendency to increase the level of long term unemployment.

As the current economic system rewards the rich more than the poor, it also widens inequality (Piketty 2014). Those who have money already earn more by investing it, receiving dividends and asset appreciation in return. They also earn money by lending their wealth, through the banking system, and receiving interest.

These sources of income are not available to the poor. Rather, they are the ones who borrow, and so pay part of their wages to the rich, as interest. The result, according to the OECD (Michail et al. 2014), is that the gap between rich and poor in the developed world is higher today than it was in 1914. The gap between the rich world and the poor world has widened too, and is greater today than it was in 1820 (*ibid.*).

The drive for economic growth has proved especially destructive to the environment. As growth requires an ever greater throughput of raw materials, to dig these up, process them and transform them into goods needs ever more energy. As that energy is fossil fuel derived, the push for economic growth is the direct cause of the rising levels of greenhouse gases in the atmosphere. In other words, the current economic system is the cause of climate change.

This problem has become so urgent that, if humanity continues to emit greenhouse gasses at the current rate, it will kick off a chain reaction in the early- to mid-2030s which will be impossible to stop. The resulting change to the atmosphere will be so large that it will be extremely difficult for human life to continue in anything like its current form. According to the World Bank (Rigaud et al. 2018), the eventual rise in temperature will be 4°C by 2100, leading to extreme weather events and loss of biodiversity. This will have a profound impact on global economies and societies, potentially causing widespread poverty and conflict.

redistribute wealth and provide a social safety net and help in the transition to a sustainable economic system.

An alternative option for human development

But what is the end goal? What would a sustainable economic system actually look like?

To be genuinely sustainable, an economy needs to be able to prosper for many generations and respect the boundaries of nature. Its ecological condition has to be stable so that the human footprint does not rise even if the population increases. The needs of future generations, as well as all other species, have to be regarded as equal to those that are living.

**The characteristics of a sustainable “equilibrium” economy are the following:**

- Long term, with the capacity to endure for many centuries
- Within the bounds of nature
- Stable ecologically
- Capable of satisfying the basic needs of all people fairly, as well as the needs of other species, in an enduring way
- Fixed maximum human ecological footprint, regardless of the population
- Highly restricted use of scarce resources
- The rights of future generations and other species equal to those living
- Very low levels of pollution which can be absorbed quickly and easily
- Progress measured differently from today
- Planned leisure time
- Free and universal access to contraception
- No industrial weapons
- Low variability in economic activity - no boom and bust
- Inequality possible, but limited
- A right to privacy, but a limited right to freedom
- An upper limit on the population, though this can probably change a little
- Strict constraints to avoid exponential growth in non-renewable resource use and pollution generation

To deconstruct the current economic system, and stop the flow of damaging greenhouse gases, will require the quickest possible closure of the fossil fuel industry, as well as the cement industry and many other energy dependant business sectors. It will require restrictions on the use of conventional cars, aircraft and ships, until clean alternatives are available. Few people understand that emissions will need to fall by 35% in the next ten years, and by 80% by 2040 (Maxton 2018), if runaway climate change is to be avoided. Low cost flights will need to be banned, waste drastically reduced, reforestation plans accelerated and buildings better insulated. Large investments will be needed in the rail network and electrification, as well as carbon capture and storage technology.

When it comes to agriculture, the first goal would need to be maintaining the stability of the land for future generations. Food production would have to come second. The use of non-renewable fertilisers or pesticides which damage the land, erode the soil or pollute the atmosphere in their production or use, for more than a few years, would not be possible in a sustainable economy. Urban organic waste, cleaned of any chemical residues, would need to be the main source of soil nutrition. This would also remove it from towns and cities, reducing pollution there.

When it comes to physical goods, manufacturers in an equilibrium economy would need to be strictly limited in the resources they could use. The longer the society or civilisation wanted to last, the fewer non-renewable resources could be used, and the lower the level of pollution that could be

created. Most goods would need to be made from recycled or renewable materials. Equipment would also need to be designed and manufactured to last for as long as possible. This means that the amount of capital devoted to production would decline progressively. As producers increased efficiency, the gains would need to be offset through a reduction in manufacturing capacity, rather than an increase in production, so that the throughput of resources did not rise.

Energy would need to come from renewable resources, though even here there would need to be very heavy restrictions on how it could be produced. The current approach to the generation of renewable energy, and its storage, is highly resource intensive. Solar panels, wind farms, hydro power and wave machines all use vast quantities of non-renewable resources in their manufacture, as does current battery technology and the distribution network. None of this would be possible in an equilibrium economy.

An equilibrium society would still need to be innovative, to continually reduce waste, improve the rate of recycling, increase energy efficiency and in medical science. Societies would want to increase the lifespan of products, collect as much discarded material as possible, find new ways of capturing solar energy and increase harvests without the use of damaging chemicals. Developments would also be needed in medical science.

Despite such heavy restrictions, a stable economy does not mean a stable society. Humanity can still develop. Rather than boosting material consumption, as today, it can grow artistically, culturally, intellectually and technologically. It can focus on improving average well being, life expectancies, health and happiness. Sports and religion can flourish. It is only the resource flow that needs to be kept in a low and constant state, so that scarce non-renewable raw materials are not depleted to any measurable degree and the environmental degradation never breaches natural limits.

A steady state economy would not require equality. More important would be for it to provide equality of opportunity, to ensure that everyone contributed to development as much as possible, and according to their abilities. Once a sustainable society has met the basic needs of all its citizens, rewards for individual achievement can still be offered, as long as the gap between rich and poor is carefully controlled, and as long as these achievements are justly recognised. As well as a guaranteed minimum living standard, there would need to be a maximum standard too. It would, of course, be possible to maintain a society with very wide levels of inequality as well, as this has happened in the past. This eventually leads to conflict however, and so is unlikely to endure as long.

A stable economy can even enjoy economic growth, if that is thought useful. The GDP can continue to rise or fall, because the value of goods and services being produced can still change. As well as the provision of care and services, many of which use little or no non-renewable resources, a great many industrial sectors will still be needed in an equilibrium economy, to produce food, provide mobility and manufacture equipment, just as today. These will need to operate completely differently however, with more localised agriculture, more electric propulsion and by making equipment from recycled metals and other materials. All sorts of new business sectors will be required too, to manage the process of sharing what is produced, for example. The price charged for all these goods and services can still change, meaning that the monetary value of the economy can still grow. Even so, sustainable societies will probably need to be agnostic about economic growth, not make it the goal. What societies measure reflects what they value, and the pursuit of economic growth for its own sake is a pointless objective from the viewpoint of the vast majority of people.

For completeness sake, two more fundamental issues need to be mentioned when such a radical transformation is aimed for: Equilibrium societies will also need to reflect on the medium of

exchange used for the purchase and sale of goods and services, and its purpose. They will need to ask whether or not they need money. Much thought will need to be given the role of the finance sector too. Would it be possible, and better, for the societies of the future to function without both?

Similarly complex is the question of governance. Is democracy the best means to achieve progress? It is easy to think that it is, because that is the Zeitgeist. It is nonetheless true that the country which has achieved the most in the last 50 years, in terms of improving the well being of its citizens, is China. It is a country that is not democratic, at least in the Western-world sense. It is also true that the monarchies and military empires of the past were often more stable and longer lasting than the current economic system. Much thought will also need to be devoted to the role and purpose of the nation state. Linked to this will be questions about the role of the military. Any long-lived society would need to live without conflict, and also without weapons which require many resources to manufacture and which create, or threaten to create, devastating levels of pollutants.

### The Role of Taxation

Radical changes in taxation will be necessary to encourage change and, sometimes, to force a transition to a more sustainable economic system. Rather than taxing work, governments will need to tax resource use, the rich, the dead and big businesses. Taxes will need to increase the cost of damaging activities, to discourage them. They will also be needed to finance a welfare safety net, to support those affected by the changes, and provide a basic income to those in need. Taxes will be needed to redistribute wealth, to make the transition easier, as well as to provide a greater incentive to companies to employ people or share the benefits of mechanisation. If societies are to be brought into a less precarious place, there is a need to ensure that the majority of people get their fair share from the system. Tax changes will be also be needed to pay for the costs of adaptation due to climate change: to pay for sea walls, access to water, move towns and cities away from coastal regions, localise food production and cover the costs of caring for those affected by rising temperatures.

Taxing businesses more heavily will require a change in thinking as well as policy. In recent decades, many large businesses have become adept at evading taxes and, as a consequence, their social responsibilities. Few break the law, but many exploit highly complex legal arrangements, with a variety of holding companies based in places where oversight is limited, to ensure their tax burden is minimized. This is unfair because it gives these large, global companies a competitive advantage, in that they have lower costs than their smaller, nationally based, rivals. These big companies also benefit from the social infrastructure in which they operate—the roads, airports, and rail networks, for example, that are mostly paid for by governments—and yet they do not contribute to the cost.

Governments have increasingly supported this sort of tax-avoiding behaviour with the result that many multinational firms pay much less tax today than they did 35 years ago (Norris 2014). In 2013, business profits in the United States accounted for almost 10% of national income, breaking a record set in 1929, while employee compensation was at the lowest level ever (*ibid.*).

Governments, through their support for business, have progressively strengthened the bargaining power of these companies, making it harder for societies to cover the costs of the dispossessed, the unemployed, the elderly, and the environmental damage.

Tax revenue from business can be increased in many ways. The simplest way is to increase value-added or corporate income taxes, especially if this is done in a coordinated manner across the rich world. Other methods include the introduction of a financial transaction tax, the removal of certain privileges such as the ability to offset interest payments, levying higher charges on business

properties to boost regional government incomes, or by ensuring that businesses contribute to infrastructure through road taxes, for example.

Society could also choose to make businesses pay more for their carbon use and the environmental effects of their activities. The goal of these taxes should be to gradually change the behaviour and attitudes not just of businesses but of society as a whole.

The problem will be getting higher business taxes implemented. While the majority of people would benefit from higher business taxes—because higher business taxes shift income from the rich to the poor via the state—it is equally true that the majority of people do not welcome any sorts of taxes—even if they are levied on businesses. This is because societies have been brainwashed into believing that higher business taxes will lead to fewer jobs. In fact, business taxes can be used to shift jobs from the private sector to the public sector, to public goods and infrastructure, for example. To make the changes needed, societies will need to be better educated.

Taxing fossil energy can also be made welcome if it is done creatively. One way is to introduce a tax on carbon which starts from a low level and then increases until it is high enough to change investment behaviour and behaviour, and so reduce emissions. To make it easier to implement, 100% of the revenue could be given back to citizens—in equal amounts (Hansen 2009). Such a carbon tax would provide every family with a steady income supplement and give everyone an incentive to use less fossil energy. It would also increase the competitiveness of non-fossil energy sources such as solar, wind, and biomass, and so encourage further investment in those sectors. It also takes from the rich (who use more energy) and gives to the poor (who use less energy).

Of course the price of most goods would rise with such a tax, depending on the amount of fossil fuel energy needed to produce and deliver them. But it would also boost sales of local produce and cut imports of fruit and vegetables from distant places. As the economy became more energy efficient, the rate of tax could rise, maintaining the incentive to reduce fossil fuel use.

The principle of taxing something that damages society—to make it more expensive and reduce its use—and distribute the income to citizens in equal amounts—can be applied to other things too. It could be applied to road pricing, where people would pay more to drive privately owned cars in the rush hour, with the revenue paid out to everyone, so subsidizing those who only use public transport. This would be especially easy to implement in cities where congestion charging already exists, but where the revenues are currently retained by the local authorities.

As well as encouraging lower fossil fuel use, societies will also need to reduce their use of other resources and stop biodiversity destruction. It can do this by taxing what economists call “externalities” (International Monetary Fund 2010).

An externality is a consequence of an activity that is either unforeseen or deliberately ignored. A negative externality of burning fossil fuels, for example, is that pollutants enter the air. These cause respiratory problems and are one of the main causes of climate change. This cost is ignored because the price people pay for carbon-based fuel does not include any cost for the environmental damage caused when it is extracted and burned. Nor does the price of a barrel of oil, bag of coal, or therm of gas take into account the steady depletion of these resources, or the implications of this for future generations.

Current economic practice is for businesses to turn a blind eye to these costs when they calculate prices and their profitability. They are generally ignored by economists, too, who do not include them when they calculate GDP.

Yet the costs of these externalities can be extremely high and are often not very hard to quantify. Society knows what it costs to treat respiratory problems caused by air pollution. It is also possible to work out what climate change has cost so far and make estimates about the future costs. So it is possible to charge these costs back through what are known as Pigovian (or Pigouvian) Taxes (Roberts 2013).

These have many benefits. Pigovian and other resource and emissions taxes can be used to help society replace damaging economic activities with less harmful ones. They give businesses a powerful reason to reduce many of the damaging things they do, to take full responsibility for their activities. And they make everyone more aware of the problems caused by these businesses. Of course, a consequence of Pigovian taxes is that the price paid for almost everything will rise too, and in some cases substantially. So these taxes need to be applied gradually, to give societies time to adjust.

As well as allowing governments to cut taxes on work, which reduces the cost of employing people, the proceeds from resource and externality taxes could be used to improve living standards. Governments could reduce taxes on healthy foods, medical care, education, and some recreational activities, for example, to encourage people to live healthier, more fulfilling, and ultimately happier lives. They can also be used to invest in the rail infrastructure, to discourage the use of road transport, or in carbon capture, to reduce the level of damaging atmospheric gases.

Increasing death duties would provide another source of income for governments. These would also reduce the inequality caused by the gains that accumulate from one generation to another. They would ensure that fewer people start their lives financially far ahead of others and help remove an unwelcome social anomaly.

Before coming to an end, there are three further conditions which need to be met if humanity is to flourish sustainably. First, an enduring economy must obviously meet everyone's requirements for food, education, safety, purpose, mobility, communications and shelter, and it must achieve all this fairly. This is necessary to sustain life but it is also needed to eradicate injustice, which will greatly reduce the chance of conflict, and so war.

Second, the right to privacy will need to be reinstated because it is a necessary requirement for individual freedom, as noted by both John Stuart Mill (1869) and John-Jacques Rousseau (1762). Being watched and monitored limits people's ability to think and speak freely. Freedom would need to be tightly restricted in other ways, however. An enduring society would need to focus on the good of everyone and this requires individual activities to be constrained at times.

Third, a sustainable world will require leisure time. Technological improvements which increase output will have to be exchanged for greater leisure, so that a sustainable society can avoid excess production and waste.

In summary, to build a sustainable economy, societies will need something like a new Enlightenment, to redefine humanity's role and purpose. Properly thinking through the implications of an equilibrium economy will take a very long time. There will need to be extensive debate and a coalescence of ideas about what a better world should be like and how societies can construct it. It will require a change in mindset, in human values, not just a change in the economic system and ideas of progress and well being. Humanity will need to radically rethink almost everything it considers normal if it is to build a society which can endure. As very few people have given these issues much thought for a very long time, societies will also need to develop the capacity to do that too.

## Literature

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**Graeme Maxton** is an economist and author. He was the Secretary General of the Club of Rome 2014-2018 and remains a Full Member. He is the co-author of *Reinventing Prosperity*, which was the Report to the Club of Rome 2016, written with Jorgen Randers. His latest book, *Change! Warum wir eine radikale Wende brauchen* is published by KomplettMedia in October 2018.