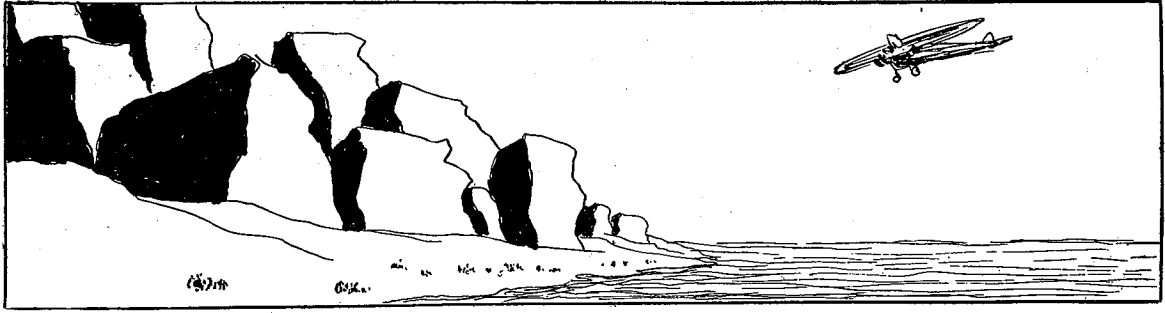


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The Discovery of Pragmatia in 1952

A Pragmatic Experiment with Taxes

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Drawings by Hendrik Willem Van Loon

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A Pragmatic Experiment with Taxes

By HAROLD S. BUTTENHEIM

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IN 1952—twenty years hence—two leaders in political and economic thought set forth from the United States on an airplane trip around the world. Somewhere in the vicinity of the lost Atlantis they were blown off their course an indefinite number of leagues, and awoke one fine morning in sight of a continent hitherto unknown except to its own inhabitants.

By an almost Providential coincidence the arrival of these American notables was at the height of one of the most significant Parliamentary election campaigns which that land of Pragmatia—for so it was called—had ever held. The story was first published in detail in the *Survey Graphic* of December 1952. Its authorship may be credited to the two political scientists just mentioned—the president and the secretary that year of the National Municipal League. Their report follows in full text:

By Radio from Pragmatia to America

THE discovery of Pragmatia, as is already known, created a profound sensation among geographers and ethnologists unable to believe that a continent in a high state of development, a thousand by five hundred miles in area, had hitherto eluded their knowledge. The rest of the world can learn much from Pragmatic civilization. In the opinion of the authors of this report, however, by far the greatest benefit to mankind from the fortuitous draft of wind which impelled the airship America into sight of the Pragmatian shores is that to be derived from the experiment in taxation whose story is now told for the first time to the outside world.

Back in 1932, its historians tell us, Pragmatia was suffering from an industrial depression no less severe than that which our histories record for the same year in the United States and other lands. Big business and big finance, emboldened by their sturdy individualism, had turned up their sturdy palms in supplication for enormous

governmental loans. Simultaneously embattled taxpayers demanded deep cuts in governmental costs and much lightening of what they dolefully called their intolerable tax burdens.

Gradually the belief became widespread among leaders in business and government that drastic changes in the incidence of taxation might prove to be vastly more beneficial and practicable than drastic reductions in public expenditures.

Two schools of thought—or opinion—became the chief contenders for popular support: the school of the sales tax, and the school of the land tax. Fortunately Pragmatia was blessed with a pliant constitution which made experimentation easy; and its citizens were not constitutionally averse to the pragmatic method of testing governmental theories.

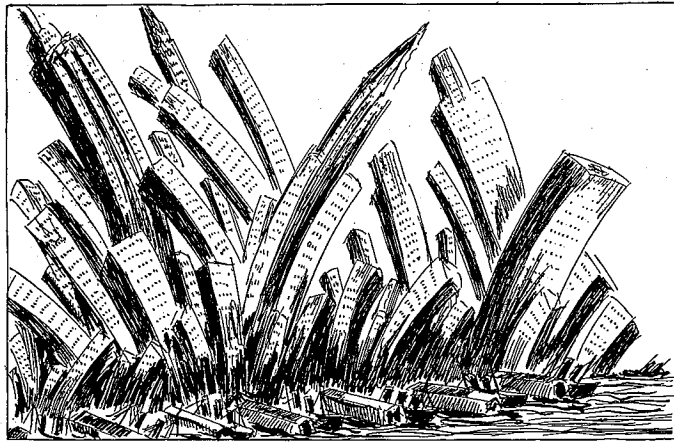
THE nation consisted of two great provinces, each having some 250,000 square miles of area, with approximately equal advantages in climate, fertility, and natural resources. In the Province of the Right, which had been the earlier settled of the two, the population in 1932 was about twelve million, as against some eight million in the Province of the Left. The Right had much the greater accumulation of capital wealth; but investigation does not reveal that for the mass of the people any higher average of happiness or prosperity had been achieved—even in normal times—than for the workers of the Left.

Before the year 1932 had ended, the Legislatures of the two provinces had reached an agreement, with the consent of the National Parliament, to apply a twenty-year test to the two dominant theories of taxation. Most of the solons of the

Right favored the sales-tax theory; while the land-tax idea had won pre-election pledges from a majority of the Left. It was decided to allow each province to raise its revenues by the method it preferred; the new system to come into effect gradually over a period of ten years, and to continue in full force for another ten years thereafter. To make the experiment as conclusive as possible, it was

Land Tax vs. Sales Tax

***P**RAGMATIA, whose position on the map is known only to Harold Buttenheim, divided itself in two parts and tried out two tax systems over a period long enough to get results. And here is a report of the political campaign in which they came to a head, scheduled for *Survey Graphic* in 1952, but pulled out of the magician's hat twenty years ahead of time to serve the troubled taxpayers.*



In 1932 their civilization had grown top-heavy

decided that the National Government would be financed, during the second ten-year period, not by federal revenues, but by contributions from the two provinces, 60 percent from the Right and 40 percent from the Left. Thus the only taxes imposed on the people of Pragmatia during the second decade of demonstration would be those authorized by their respective Legislatures.

Taxation being the main issue in the campaign for election of members of the 1932 Legislatures, the political parties had been authorized to furnish, for printing on the official ballots, brief statements in advocacy of the tax method to which their respective candidates were pledged. Fortunately these documents of the two leading parties have been preserved. Their text follows:

THE CASE FOR THE SALES TAX

No man can live in a modern civilized society without buying some of the products of other men's work.

An *ad valorem* tax, therefore, applied at a uniform rate to all sales, would provide a sure source of revenue and compel every individual to bear his share of the costs of government.

If such a sales tax were made high enough to cover all governmental costs—national, state, and local—it would have three very beneficial results:

1. As the tax would be paid and reported by the seller, the collection of such a tax would provide maximum certainty and minimum expense for the government.
2. A sales tax would make possible the repeal of all income and property taxes, thus removing intolerable burdens from real estate and from capital earned or inherited.
3. Because every purchase would be taxed, it would encourage the practice of thrift, thus insuring individual reserves for periods of sickness, unemployment and old age, and discouraging present-day trends toward socialistic taxes for welfare funds.

All taxes being in the last analysis consumption taxes, the simplest and least burdensome tax which could be levied by any unit of government is the consumer's or sales tax.

THE CASE FOR THE LAND TAX

Given the existence of funds, created and renewed inevitably by natural law, the collection of which would ultimately tax no individual's labor or savings, the first duty of government is to prevent the diversion of these funds for private use, and to collect them for the public benefit. Thus we may:

- (1) Pay for governmental services out of the land values which governmental services create;
- (2) Pay the community's costs of population growth out of the land values created by population growth;
- (3) Collect for the benefit of the public the economic rent

resulting from the bounties and beauties of nature, to which no man has a natural right; and

(4) Conserve for the community increased land values resulting from the social services and beneficences of public-spirited citizens.

These funds—created by nature, by government, by population growth, and by community benefactions and services—would be ample to pay all the costs of local public works and governmental services, and perhaps ultimately all non-local governmental costs as well.

Meanwhile, during the period of adjustment to the rational method of providing public revenues, justice demands that the evils of existing extremes of wealth and poverty be ameliorated. This can be done, and provincial and national governmental costs be largely met, by income and inheritance taxes bearing heavily on surplus funds which would otherwise be hoarded or used for speculation or for the unneeded expansion of competitive manufacture or trade.

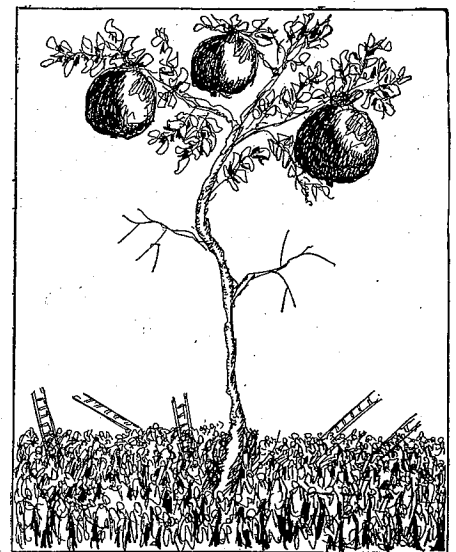
Our arrival in Pragmatia just twenty years after the epoch-making campaign for the election of candidates pledged for one or the other of the two foregoing statements of principles, has been one of the outstanding experiences of our lives. For we have been able to study what has happened in the interval and shall learn tomorrow the results of a second epoch-making election, when legislative candidates will have been chosen to determine whether, based on this twenty-year pragmatic test, the sales tax or the land tax or some other system of taxation will be adopted by the two provinces as their future method of providing public revenues.

The election now being held, however, though thrilling to us, is calm in the extreme. The results are a foregone conclusion. A Parliamentary committee representing both parties brought in some days ago a unanimous report of what has happened, Right and Left, during the two decades of demonstration. This document, also, is worth quoting in full.

The Parliamentary Report of 1952

THE experiences of our two provinces with the contrasting methods of taxation adopted in 1932 are so well known to the people of Pragmatia that a recital thereof seems almost superfluous. As a matter of record, however, and to comply with the Parliamentary mandate, the following statement of facts is made:

It will be remembered that the year 1932 saw the depth of a previously unexampled industrial depression. The gradual improvement in employment which took place throughout the nation during the next three or four years cannot be credited primarily, in either province, to the new methods of taxation. An upswing was overdue anyway. It was aided in part by the depletion of stocks on the retailers' shelves and in part by many other factors, including the stimulus given to public works and



The Boom Period

to slum clearance and large-scale housing projects by the availability of federal loans for those purposes. Moreover, the shift in the incidence of taxation, occurring as it did over a period of ten years, was too gradual to have any very sudden effect in greatly stimulating or retarding business recovery. But after two or three years, business barometers in the two provinces began to behave quite differently. For both, the employment index in 1932 had shown man-hours of work 50 percent lower than the previous peak. In the Province of the Right employment in 1935 had risen in three years to 75 percent, while the corresponding index figure in the Province of the Left had risen to 80 percent. Economists in both provinces pointed out that the 1932 depression was not the ordinary cyclical disturbance which the business world had previously accepted almost as an "act of God." Statistics showed that boom-time employment for several months preceding the crash of 1929 had been noticeably below the peak of 1926. Something more effective than recovery by what someone has called the "lazy fairy" method seemed essential to the unfettered thinkers of the day. Otherwise, said they, the business world must confess its impotence to prevent permanent unemployment on a large scale in the midst of plenty such as industry and agriculture had never before been capable of producing.

It had been hoped, of course, by the sales-tax advocates of 1932, that conditions would somehow right themselves. They had a blind faith, too, that their tax panacea would offer no obstacle to one of the sacred tenets of the "lazy fairies"—the mysterious "law," so-called, of supply and demand.

Yet in 1937—five years after the new tax systems in the two provinces had been started—the barometer of employment in the Right still stuck at 75, while that of the Left had gone up to 90. The world of business and finance began a serious study of what had happened.

The alleged certainty and equity of the sales tax proved most elusive. Many complications had arisen. Much of the time of the Legislature and the courts was consumed for several years in attempted solutions of problems such as these:

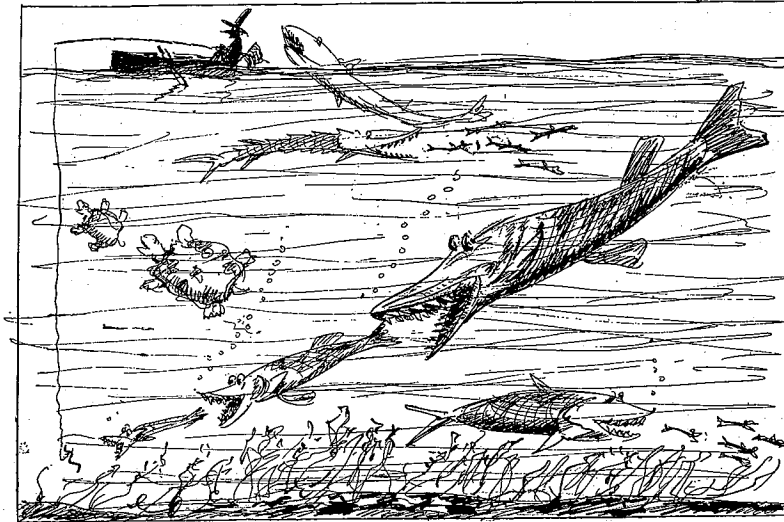
With tens of thousands of merchants and millions of farmers subject to the sales tax, how could bootlegging be prevented and honest tax rates be secured? How would it be possible to prevent bartering as a means of tax dodging?

Should the sales tax apply only when sales were made to the ultimate consumer? If so, should tools and materials of manufacture be taxed, or only the finished product? What if the finished product became a tool or material of manufacture for another factory?

Would tires, for example, be free from tax if sold to an automobile manufacturer, or dealer, but be taxable if sold to an automobile owner? Would a used automobile be subject to taxation as many times as it changed owners? Would furniture bought by a jobber for his own use be taxable, but if bought for re-sale to a dealer be free from tax? If not, how would double taxation on such furniture be prevented?

When it was suggested that some of these problems could be solved by assessing the tax not against merchants or consumers, but solely against producers, puzzling questions of administration arose. How, for example, would the tax be applied in the case of merchants who are also to some extent producers or repairers—bakers, jewelers, automobile service stations and beauty parlors, to cite only a few such? Why should the non-producing merchant escape all taxation?

The taxation of non-commodities proved puzzling also. Should railway freight charges be taxed? and theater tickets? and taxicab fares? and hotel bills? Should sales of bonds, stocks, mortgages and insurance policies be taxable? Should banks escape all taxes? Should the *use* of land be free from taxation, but *sales* of land be taxed?



Laissez-faire

The sales tax at the half-way mark had risen to 10 percent or more of the cost of all products of industry and agriculture reaching the ultimate consumer. Theoretically the producer or retailer paid the tax, but it was, of course, passed on to the consumer in higher prices. The consumer's ability to purchase being reduced by the taxes passed on to him, total potential sales shrank and employment remained at a practically stationary percentage of employable workers.

There being no tariff barriers between the two provinces, the manufacturers of the Right (the sales-tax province) strove to increase their business in the less taxed and more prosperous markets of the Left (the land-tax province). But the attempt proved abortive. The manufacturers of the Right had, of course, to pay the sales tax imposed by their own province before their goods could be shipped to consumers in the Left. Manufacturers, there, however, had no sales tax to pay, and could therefore outbid their competitors of the Right by at least 10 percent with equivalent wage scales. This differential increased to 20 percent by the end of the ten-year period of tax readjustment.

Prior to 1932 the Right, as the older and more densely settled province, had produced about two thirds of the manufacturing output of the country. Gradually, however, as the sales tax increased from year to year, manufacturers and capitalists from the Right began to establish factories in the Left. This was done not merely to escape the sales tax imposed in the Right; another differential of great importance to trade in the Left was becoming more and more apparent. A surprising contrast between the two provinces was developing in the cost of factory sites and in the rents of workmen's homes.

These trends reached their maximum, of course, as did the other effects of the new fiscal policies, after the ten-year period of tax readjustment ended in 1942. The promise that their land would ultimately be freed entirely from taxation had won from landowners in the Right influential support for the sales tax in the 1932 election. But the great unlanded masses in the province soon discovered that they were out of luck, concurrently as land taxes were lowered, land prices and rents

soared, and owners of vacant land, when tax-free, held such sites indefinitely for speculative profit.

In the Left, however, taxes by 1942 had been removed entirely from the products of labor and had come to absorb about 80 percent of the economic rent of land. It thus ceased to be profitable to hold land out of use, and vacant land was available in abundance at about 20 percent of its former asking price. This stimulated better housing on more spacious sites for the mass of the population than ever before; and it enabled the municipal governments to acquire ample sites for parks, playgrounds and public buildings at low cost.

As the years went on it was still contended in the Province of the Right that, once the factory owner or householder there had bought his land and erected his building, he would thereafter be free from taxes on them. Is he not, therefore, better off in the long run, it was asked, than if under the laws of the Left? This argument, of course, overlooks three facts:

- (1) In the Left, also, all real-estate and property taxes have been abolished except the tax on the land, according to its value.
- (2) Sales of building materials and equipment in the Left not being taxed, it has become much cheaper to erect factories and homes in that province than in the Right.
- (3) Since 1942 anyone who has rented or purchased land in the Right has contributed to the seller, in monthly payments or their capitalized value, the entire economic rent—wealth which the seller never created. On top of this the purchaser pays sales taxes on the improvements he creates. The citizen of the Left, to be sure, also pays the economic rent of the land he uses, but instead of paying all of it to the previous owner he pays only 20 percent of the amount to him, and pays the remaining 80 percent to the government for all local taxes.

But the land tax alone cannot be credited with the freedom from poverty and unemployment which have become characteristic of the Left, nor for the many fine public and community buildings, parks, playgrounds, water fronts, unpolluted streams, absence of slums, and abundance of good low-cost housing to be found throughout that thriving province. An important factor in bringing these conditions about has been the method adopted in the Left of diverting unneeded capital into public services or consumption goods. As indicated in the 1932 statement of principles, leading economists of the Left had shown that what was then needed was not greater ability to produce, but greater ability to consume. They had shown, too, that over-investment in competitive manufacture and retailing, and under-investment in non-competitive public and cultural improvements, was a major cause of the then existing depression.

Step by step, therefore, with the adoption of the land tax and the abolition of all other taxes, the Left imposed higher super-taxes on incomes, especially on those in excess of \$50,000 a year, and on inheritances in excess of \$500,000. The revenues thus secured were applied towards the types of improvements just enumerated, thus not only increasing employment, but providing assets for the province much more valuable than an excess supply of semi-idle factories, farms, retail stores and gasoline stations.

Meanwhile, in the Province of the Right, less happy conditions were prevailing for the so-called working classes—and, indeed, for most of the wealthier classes too.

As soon as business conditions showed a noticeable improvement, following the depression of 1932, the mistakes which had been largely responsible for that depression were repeated by captains of industry in the Right. Big business and big finance lacked the vision or compulsion to distribute a generous share of their profits through increased wages and shorter hours for the workers, and through gifts for cultural and

recreational activities which would divert excess savings from competitive industry and trade.

Landowners, too, freed from taxes and able to charge higher rents, were accumulating unearned surpluses for which they sought profitable investments. As the landowners of the Right obviously could not all get rich and stay rich by selling or renting land to one another, they put much of their money into factories, hotels, skyscrapers, high-pressure salesmanship and other instruments of production and trade of which there was already an unprofitable excess. They also continued to throw men out of work through technological advances in methods of production; and the dole, reluctantly adopted as a temporary expedient in 1932, became the only alternative to starvation in the midst of plenty.

These conditions brought their inevitable result—the panic of 1947 in the Right, out of which that province is now only slowly emerging. That the Left has been wholly free for twenty years from any serious business setback gives conclusive testimony to the wisdom of its economists and civic leaders, who advocated and secured the adoption of its present system of taxation in 1932. For several years now no able-bodied man in that happy province has been idle by compulsion. Industry and trade and farming have so flourished as to offer new jobs speedily to all workers displaced by technological causes—or if any such have difficulty in readjusting themselves, the public service and public works offer temporary or permanent refuge. There has been little difficulty, also, in absorbing the two million or more unemployed workers who have emigrated from Right to Left in search of jobs during the last fifteen years.

Labor is so steadily and increasingly in demand throughout the Left that wages have risen higher and higher from year to year. This in itself has been a vital factor in the prosperity of the province, for the steadily mounting purchasing power of labor has furnished the only market abundant enough to absorb the increasing output of factories and farms.

AN INCIDENTAL benefit of freedom from business depression in the Left has been the almost total relief to government and industry in that province of the costs of insurance against unemployment. In the Right the rigors of the recent panic from which that less progressive province has recently been suffering have been somewhat mitigated for the workers by the reserves to meet such a contingency previously set up by industry and government. Practically all of the employers in the Right, however, are now voicing a strong preference for the economic justice of the Left as much better both for themselves and their workers than what they now describe as the charity heretofore necessitated by an outworn economic system.

Another advantage, not yet an actuality, is confidently predicted by economists and political scientists of the Left for the early future. This is the gradual scaling down, and perhaps the ultimate abolition, of the income tax.¹ The level of prosperity is so high, the short work-day and work-week have become so general, foolish thrift has become so scarce and wise spending for comfort and culture and pleasure has become so general, that there seems to be little danger that consumption in future will not keep pace with productive capacity to the full extent that the public interest requires. Moreover, the province and its counties and municipalities have acquired so much of the land from previous owners, and the remainder is so fully

¹ There is a footnote here added by the American observers, stating that the reduction or removal of income taxes in Pragmatia will be greatly facilitated by the fact that Pragmatia is a peaceful land, with no debt burdens and pensions arising from past wars and no current expenses for armies and navies to fight future wars.

used, that the economic rent which could be collected in taxes—and paid without burden—seems likely soon to rise to an amount nearly great enough to cover all the necessary costs of government. As a result, most of the candidates now running for the Parliament of the Left have endorsed a proposal not only to continue the land tax in force as at present, but gradually to scale down the income tax to a possible vanishing point during the next ten years. The present inheritance taxes will be continued as a discouragement to excess saving; and it is also proposed to provide by act of Parliament that if at any time the index of unemployment should exceed one percent, the income tax will be restored or increased by executive order long enough to finance a previously planned public-works program, on a scale and with a speed great enough to make a depression impossible.

WHEN this committee began its deliberations its members, from their knowledge of conditions in the two provinces, were certain that the Right would do well to adopt the tax system of the Left. One problem puzzled some of us—the question of justice to the landowners. But we are convinced that most landowners of the Left who in 1932 had improvements on their property of value substantially greater than that of their land, have been gainers by the freeing of such improvements from all taxation. Many landowners had improvements and personal property the combined assessments of which, when the new system of taxation began to be applied in 1932, were substantially the same amount as their land-value assessments. Such owners found little or no change in the amount of their tax bills; for as their land taxes climbed on one flight of steps, their other assessments descended with equal speed on the parallel flight. And when they improved their homes or their farms, they were not penalized by additional assessments.

Many owners of vacant land promptly improved it, or sold it for improvement, when the land tax began to be applied, and thus had little or no loss. It must be admitted, however, that many owners of vacant or of poorly improved land in populous centers were unable or unwilling to pay the increas-

ing land tax, and either sold their land at a sacrifice or donated it to the government. But because a great reform bears heavily on some who through legal fiction hold title to part of the surface of the planet, shall we say that mankind for all time to come must pay tribute to them and their "successors or assigns"? Suppose the entire area of any large city to have been originally "owned" by its founder, and that the title deed has passed intact from father to son as absentee owners for a hundred or a thousand years. Is it believable that the residents of that city would consider themselves morally bound in perpetuity to pay the entire economic rent of their city's land to heirs whom perhaps not one of the citizens would ever see, and who had never rendered the city any service? Would not a land tax, equivalent to most if not all of the economic rent, be the just and rational solution? And where there are thousands of landowners rendering no service *as owners*, does the principle differ?

No new tax can apply with entire equity to all affected by it. But surely the most equitable of all taxes is that fund which, to quote the land-tax manifesto of 1932, is "created and renewed inevitably by natural law" and "the collection of which would ultimately tax no individual's labor or savings."

HERE endeth the report of the Parliamentary Committee. To catch the December number of Survey Graphic, this document is being transmitted by radio from the airship America. Tomorrow we will send a brief supplementary message as to the result of today's election.

There follows a dispatch dated at sunrise the next morning:
HB 77 RADIO-PRAGMATIA
LCD SURVATES NEW YORK
OVERWHELMING VICTORY FOR PRAGMATIC
BLEND OF LAND TAX WITH INCOME AND
INHERITANCE TAXES STOP PERCHANCE
THERE IS HOPE FOR SIMILAR ADAPTATION
IN UNITED STATES OF THE DOCTRINE OF
HENRY GEORGE.