# Taxing Dis-harmony

## Mason Gaffney warns tax havens: Beware the thought-control police

THE TINY Cayman Islands in the West Indies is championing the right to employ tax policies of its choosing in a David and Goliath battle with the giant nations, *writes Fred Harrison.*

The OECD countries want to curb what they call "unfair competition", and they brand the Cayman Islands as a tax haven because it does not tax people's incomes. Not surprisingly, it does a roaring trade in financial services. Money is attracted from high-tax regimes. This has annoyed North American and European governments, who have banded together to try and straitjacket the deviant low-tax economies.

Last year the Paris-based OECD published *Harmful Tax competition: An Emerging Global Issue*. This states that a tax haven is "a place to be used by non-residents to escape tax in their country of residence". With the electronic age making it possible to circulate money around the globe at the push of a few buttons - $1.5 trillion every day - governments are losing a lot of revenue. That is why they want to clamp down on the havens.

This has led to curiously contradictory positions held by the British government.

- It is pressuring the havens within its domain - the Channel Islands of Jersey and Guernsey - to toe the UK fiscal line.
- But Chancellor of the Exchequer Gordon Brown has read the riot act to Germany, which is exploiting the tax harmonisation theme to try and force increases in corporation taxes in other EU countries. Germany wants to shift taxes off labour and on to capital, but the overall effect would be an increase in the tax burden. Mr. Brown warned that he would use the veto. "As far as Britain is concerned, tax policy is made in Britain not in Europe. It is by cutting taxes, not raising them, that is the way forward to create jobs."

FINANCE minister Oskar Lafontaine is using Germany's presidency of the EU to try and standardise tax rates. One target is the relatively lower tax regime in Ireland. But the debate is confused by the use of value-laden words which do not necessarily correspond to the consequences of intended actions. For example, the harmonisers say they want "to avoid harmful tax competition".

But who is being harmed? When it comes to national interest, the meaning of words become plastic. Take, for example, the statement offered by *The Financial Times* in an editorial on November 24. It acknowledged the need to eliminate distortions in tax policy, and then noted: "But where a country chooses to have a different tax structure from its neighbours, because it is considered more equitable or more efficient, that cannot be regarded as unfair competition. It is perfectly legitimate".

This definition invites a consideration of what constitutes a fair and efficient tax. Unfortunately, government advisors do not engage in an open review of all the options in the quest for harmony in tax policy.

TAX EXPERT Mason Gaffney, a professor of economics at the University of California, flew to the Cayman Islands to debunk the rhetoric employed by the tax harmonisers. He warned a packed meeting of the Society of Trust and Estate Practitioners: "When a powerful international political organisation officially brands you as 'harmful', look out".

He said that the OECD's proposals "call for more enforcement, and to scapegoat small tax havens. To enforce an income tax today calls for nothing less than a worldwide intelligence network with vast powers of search and seizure. It also calls for worldwide thought-control to give it moral authority and general support. The end of this thought-control is to criminalise income".

Words like *uniformity* and *fairness* were employed to disguise vested interests which advocated taxes that were discriminatory between payers and abusive in their impact. As an example, Dr. Gaffney cited the sales tax: "A 'uniform' sales tax is not uniform in its effects. Retailers in rich locations can bear it and survive; those in marginal locations cannot. The result is especially to penalise poorer neighbourhoods and regions and communities".

He also exposed the hypocrisy of the harmonisers. For example, the OECD branded as "harmful" a nation which allows a person to deduct costs when the corresponding income is not taxed. "That sounds reasonable," said Dr. Gaffney, "and yet that is the standard treatment of most real estate income in the USA, the largest member of the OECD."

Lurking behind the rationale for harmony were the governments of richer nations which employed policies to attract inward investment at the expense of poorer nations. Dr. Gaffney pointed out that attracting skilled labour and capital was possible by offering superior public services. This was possible for nations that were fortunate to occupy the best lands on the planet, and "It seems rather miserly of them to deny to nations occupying less favoured lands the only compensatory measures available".

Less well-endowed nations could attract resources by offering "a magnetic tax structure". Declared Dr. Gaffney: "The OECD report was written by people wearing blinders that keep their eyes and minds fixated only on kinds of taxes that penalise and repel mobile activities. There are taxes that...positively attract them. The OECD does not like them".

The professor identified revenue-raisers which benignly supported economic activity. These measures raised revenue directly from the rental income of land and natural resources. The alternative, said Dr. Gaffney, was "a worldwide inquisition by the revenue agents of every nation into the records of every other nation".

SPURIOUS though its logic may be, and harmful the consequences, the OECD report has initiated a debate which could be turned against the high-tax harmonisers.

In paragraph 29 of its report, the OECD talks of poaching from "the tax base [which] 'rightly' belongs to" another country, which can be labelled harmful competition. This thesis rests on the implicit claim that there is a unique property in a country's total revenue. This is

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OECD Secretary-General Donald Johnston claims that tax policy plays an important role in achieving "the triangular paradigm of social progress. That means keeping economic growth, social cohesion and good governance in balance with each other".*

This balance is achieved through education and social programmes which needed to be financed through taxation. But he claimed: "However, taxation is not an easy area to get right. It never has been and it probably never will".

In a review of the constraints on public finance, the head of the leading think-tank representing the industrial nations made no concession to the one fiscal policy that would automatically synthesise the three corners of his paradigm: the policy that emphasises the need for governments to charge people for the benefits they derive from possessing and using land and natural resources.

The OECD is worried about the "mobility of national tax bases" without offering any guidance to member countries on the tax base that is immovable: land. Consequently, the OECD is drafting a stack of conventions that narrow the freedom of people to earn incomes under the conditions of their choosing.

* Donald Johnston, "Taxation and social progress", *OECD Observer*, Jan. 1999, p.3.

creating a new socio-economic order ("...in order to form a more perfect union...").

This principle provides self-reinforcement: the greater the success of the identity or purpose the more people identify with and commit to the system.

**7. Secure tenure for members**

Small groups in which individuals enjoy stable tenure are more productive. At the organisation level, highly stable companies such as Lincoln Electric and Haworth Industries (a leading US office furniture manufacturer) officially promised secure employment (membership). In most communities, citizenship guarantees standing. Losing one's citizenship (membership) requires deliberate (and usually highly provocative) action by the individual and the community. Any attempt to remove citizenship meets with inquiry about the nature of citizenship. This principle provides a setting in which the exercise of true inquiry can flourish and where members secure their role in creating collective values. Secure membership provides a balancing effect in the social system by ensuring membership for those who challenge the system with dissenting opinions.

WHILE EACH of these principles may add value individually to a social system, their robust power comes when taken as a group. As a group they interact, self-reinforce and self-regulate.

For example, the quest for proportionate distribution of synergistic value creates a potential tension when related to the principle of equitable distribution of individually created value. Mutually satisfying resolution of this tension may only come through the democratic process. The means of distributing the collectively created value may also vary with the purpose of the collective. For example, communities might choose to provide services while organisations may provide direct payment to members.

Similarly, introducing a new privilege without adding collective value might instigate a participative "voice" process to correct the injustice combined with an inquiry about the nature of the privilege and its potential to contribute to collective value. However, without equal distribution of synergistic value system members may lose their will or incentive to engage in democratic voice. Without the corrective effect of participative voice authorities might grant additional privileges. The formal recognition of principles or processes does not ensure their use.

Given the assault on academic tenure, the apparent non-responsiveness of many governmental agencies, and the losses of companies once noted for their secure tenure (e.g., IBM and Digital Equipment Corp.), one might question the appropriateness of secure tenure for sustainable social systems. Here, again, the principles appear to function as a group. What academic environment or government agency functions in self-aware inquiry, provides differential rewards for differential performance or shares in the collective value that they create? Tenure alone does not (nor do any principles alone) provide effectiveness and sustainability.

The groups, organisations and communities cited in the studies maintained their sustainable qualities for long periods, but this raises the question of the depth to which the principles are embedded. Work groups can be vulnerable to managers and sometimes to the larger organisational culture. For example, in the classic studies on motivation at the Western Electric Hawthorn Facility, workers who were not included in the studies sought to undermine the results, in part because those in the experiments became very happy and excited about their work.

At the community level, Fairhope has seen the imposition of county, state and federal taxes along with layers of government intervention which dilute the principles of sustainability. While its first half century of relatively pure application of the principles cited here provided a running start, the last two decades have seen increased class polarisation, increases in business failures, and a strong out-migration of its youth.

ENTITIES that intend to remain stable must manage these principles, but they must also manage the boundaries of their social systems. Perhaps the best individual strategy would be to create and protect one's local, sustainable system while working to transform the next higher level of social system. Until we are all free, freedom embedded in an unsustainable system is tenuous at best.

## References


1 In *The Losses of Nations* (ed: F. Harrison), London: Othila Press, 1998; reviewed in *Land & Liberty*, Spring 1998, p.15.

2 Jerry Porras, *Built to Last*, New York: Harper & Row, 1994.



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# Brussels □ Priced off land

BRITAIN'S consumers wonder why they pay higher prices than their European partners for goods bought in the shops. One explanation is offered in *The Economist* (Feb.6), which reports that returns on capital invested in supermarkets are as much as 5% lower than for their European counterparts.

"The average supermarket in Britain is roughly half the size of an American supermarket, and two-thirds the size of a typical French store, which limits economies of scale.

"High land prices make it harder to build mega-stores in Britain. But even small retail outlets face high costs. Bizarrely, it is more expensive to rent shopping-space in the nondescript south London suburb of Croydon than in the plushest shopping streets of Milan, Stockholm or Dublin. A study by an estate agency, Healey & Baker, conducted last year ranked London's Oxford Street as the third most expensive shopping mile in the world after New York's Madison Avenue and Hong Kong's Causeway Bay. A recent McKinsey report on productivity found that, on average, selling-space in Britain was 40% more expensive than in America and 20% more than in France."

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claimed by the sovereign government as its property, to the point where it wishes to coerce other governments which dare to deprive it of its legitimate revenue.

This raises serious questions which ought to engage fiscal philosophers, in an attempt to pin down the high tax regimes which presume to intrude into the affairs of sovereign nations. For example:

- Exactly which parts of a nation's income "rightly" belongs to the government? Do the citizens know that part of their income does not "belong to" them at all?
- What is the size of the tax base that "rightly" belongs to the government?
- On what grounds do governments claim the right to reserve that revenue for its exclusive use?

The language in which the OECD conducts its analysis lays the foundations for international conflict which could move from fiscal to force of a different character. For example, in paragraph 31 it talks of governments being able to conclude that some countries could be "poaching other countries' tax bases". In the past, nations have gone to war for less. But again the high-tax harmonisers need to be challenged on their property claims. Poaching pre-supposes ownership, which needs to be defined and legitimised in the court of world opinion.

The coercive philosophy behind the views expressed in the OECD report are revealed by the comment that "countries should remain free to design their own tax systems as long as they abide by internationally accepted standards in doing so" (para. 26). The basis of those standards needs to be critically examined before sovereign nations are intimidated into complying with the strictures of those who dominate the public discourse.

**Sources:** Mason Gaffney, *International Tax Competition: Harmful or Beneficial?* (Aug. 1998), and "Taxation of mobile Capital in a Global Free Market", speech, 2.9.98, Grand Cayman.