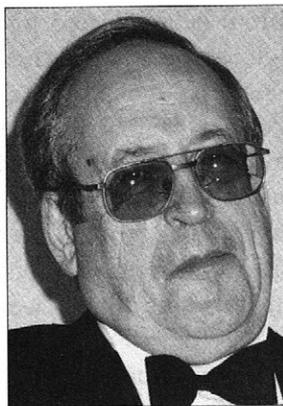


Rent as a Public Property

Dr Dmitry Lvov, Russia



Dmitry Lvov was Academician-Secretary of the Economics Branch of the Russian Academy of Sciences when he delivered this paper.

In an essay published in the Spring 2001 issue of *Geophilos*, Dr Lvov wrote that Russia can be rescued from its present desperate situation if she adopts a tax reform that was faithful to the nation's morality and land-sharing traditions.

Dr Lvov is editor of *Road to the 21st Century: Strategic Problems and Prospects of the Russian Economy*.

United Nations documents on the concept for sustainable development of society and the economy, known as “Agenda for the 21st century”, gained public recognition at international meetings of the highest levels. They state that civilization is in a crisis that could lead to environmental, economic and social disasters.

A diversified concept of sustainable development was worked out under the aegis of the UN in the last decades. The main emphases highlight the humanization of social and economic life to provide real control over the efficiency of the use of the natural resource capacity of Earth in the interests of mankind, observance of the rights and freedoms of citizens, social support and a more just and equal distribution of incomes, capital, etc.

Society *must* take responsibility for the condition of the biosphere (assuming the biosphere to be not only as an environment but as a system to which mankind belongs), and contribute to its positive development. But that could be possible only if life-supporting resources become the property of *the whole mankind*, rather than just a few representatives in society, or a group of countries. Only then will society be in a position to control and regulate the consumption of resources and maintain the fragile balance between society and nature.

Under present conditions there are neither national nor regional solutions to the problem of preserving the planetary environmental balance. The problems of less developed countries are becoming the problems of the countries of the “golden billion” people in the rich countries.

The step by step realization by all countries of a new social and economic model of human evolution could prevent the destructive impact on nature. Leading analysts, political leaders and scientists from many countries are thinking about it and searching for a solution. Progress is very slow and that is not by accident. It is the result of stereotyped thinking, the dominant mainstream being the liberal economic theory called the “Washington consensus”.

At the heart of this theory lies the idea of securing macroeconomic balance through the wide use of financial and credit tools and corresponding institutional mechanisms. The main failure of this doctrine is the lack of a correlation between economic development and its basic starting components – people and the environment. They are the foundation that determines the destiny of Mankind, which is neglected by the “Washington consensus” doctrine. That’s why it should be regarded as narrow and harmful.

For several years I and my colleagues at the Russian Academy of Sciences Central Economic and Mathematical Institute worked hard to propose a new concept of global social and economic development as an alternative to the Washington Consensus. This theory is called the *National Dividend Concept*.

At the heart of this concept lies the thesis that all natural resources, environment, territory, water and air basins are in the public domain, which is why they could and should be treated as public property (i.e. property that belongs to the whole population). That is the principle which makes it possible to bring into life the inalienable right of everyone to enjoy equal access to natural opportunities, those that are not created by any human being. These resources are actually God's gift to humanity.

Historically, the progress of Western civilization took the opposite course. The result is that all social formations, including capitalism, failed to eliminate the global contradiction between Society and Nature. There were other aims and goals among priorities either in their open or concealed forms: especially to raise and multiply revenue, the easiest and most "natural" ways being those based on appropriation of the revenue derived from exploitation of the carrying capacity of the planet.

Governments of Western countries used to emphasize that world capitalism guarantees freedom of exchange between the major factors of production. These guarantees rely on the laws and regulatory mechanisms that exist in the capital and labour markets. But there is one principal exception from these norms and rules – *prices for labour and capital are not counterbalanced by the prices for natural resources*. This violates the principle of equivalent exchange under competitive market conditions. Hence it is impossible to avoid differentiation in starting conditions for subjects of market relations that results in even greater income differentiation between individuals and countries.

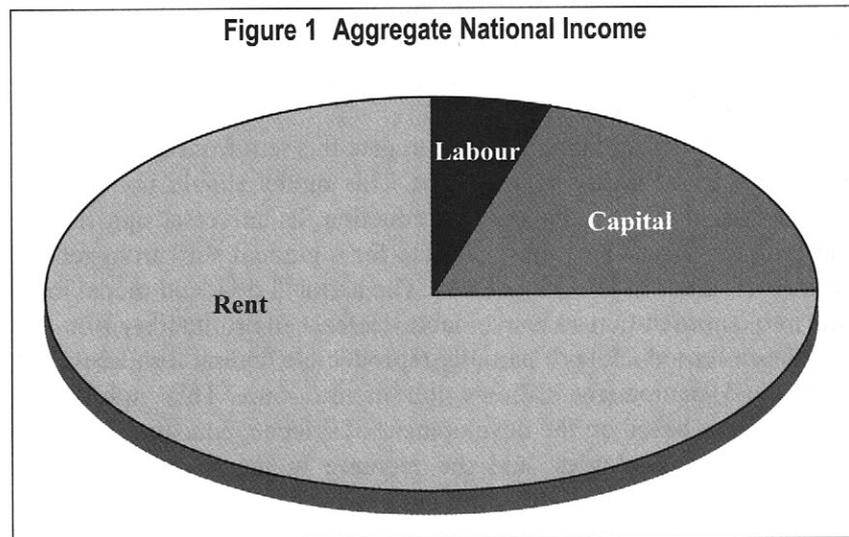
The primary cause of the emerging contradiction is the problem of property rights in land and natural resources, which has not been solved in capitalist society. No western government has tried to invade sacred private property rights in land and natural resources, which is the "sacred cow" of capitalism. That's why it is impossible to eliminate the global contradiction between human's social world and inequality in the basic conditions of his/her life. But advocates of the "Washington consensus" ignore the contradiction. They are sure that it is impossible to create in the market the "sense of master" without private ownership of land and natural resources.

We claim that it is urgent to coordinate private property rights with another essential feature of the market economy – freedom and equality in the process of exchange for everyone. That could be achieved only if owners of land and natural resources pay rent for the use of land and other natural resources. An individual has the inalienable right to the income obtained from his entrepreneurial activity or investments undertaken at his own risk. But *it is also natural that all surplus revenue that is not created by any human being (speaking in images, this is gifted by God) must belong to everyone.*

National Dividend

It is well known that the total income of society is the function of three generalised parameters – labour of workers (their total wage), capital (including business income) and rent (that is the income from the use of land, territory, onshore transmission lines, modern communication facilities, transportation networks and other monopolistic activities).

The share of rent in Russia's aggregate national income is about 75% (\$40-45 bn. annually). The share of capital is 20% and of labour – only 5%. In other words, nearly all that Russia receives today is rent from the use of its natural resources.



But under the immoral privatisation programme, natural resources were appropriated (practically for free) by a small group (not larger than 10% of the population). As a result, more than 90% of Russia's population was deprived of access to public goods, gifted to the peoples

of Russia by God. National income was diminished by 2-2½ times! The process that takes place in Russia today prefigures what happens throughout the world. What we call the Russian crisis and stagnation has as much to do with Russia as with the USA, Japan and other countries. Our economic crisis is a reflection of a global crisis of modern post-industrial civilisation. But we, as usual, have overleapt other countries with our ill-conceived reforms. We again act as whipping boys for the sins of modern civilisation. It is time for us to change this role and as quickly as we can!

To avoid the danger of global destruction it is necessary to secure constitutionally vested rights in society (as a sort of corporation of the highest level) as the primary owner of territorial and other natural resources. Such constitutional innovation creates the basis for *providing equal rights to access these resources for all members of society*. This would realise the principle of equality of starting conditions for everyone. Without this principle it is difficult to achieve peace and everyone's clear perception of their common belonging.

The way to actualise society's superior rights to natural resources would be to capture rent from all resources as public revenue. This total revenue, which forms a surplus after all other factors have been paid, would form the net public revenue shared equally among all members of society – *the national dividend*. According to the national dividend concept, rent must be captured by society and used for the goals of the whole society (via auctions, tenders, leasing and so on). It is the only profit that can be taxed.

We must establish fair ways to segregate this rent from the profit that belongs by right to the entrepreneur. This model should not be built around current ratios of factors of production. Its universal significance and long-term dynamics must provide for a gradual shift from rent of natural resources to intellectual rent. The national dividend model must take into consideration an unavoidable decrease in profitability from the use of non-reproducible or partially reproducible natural resources. The intellectual component follows the natural one. This intellectual component is based on the development of science, education, modern information technologies, and the increase in the knowledge-based sector of the economy. New society is a society of effective interaction between Humanity and Nature where the total intellectual capacity of the community enables us to solve global contradictions that were accumulated over evolutionary time-scales. Then society would be able not only to defeat man-made impacts on Nature, but would also enable Humanity to understand that there is a historical necessity to eliminate

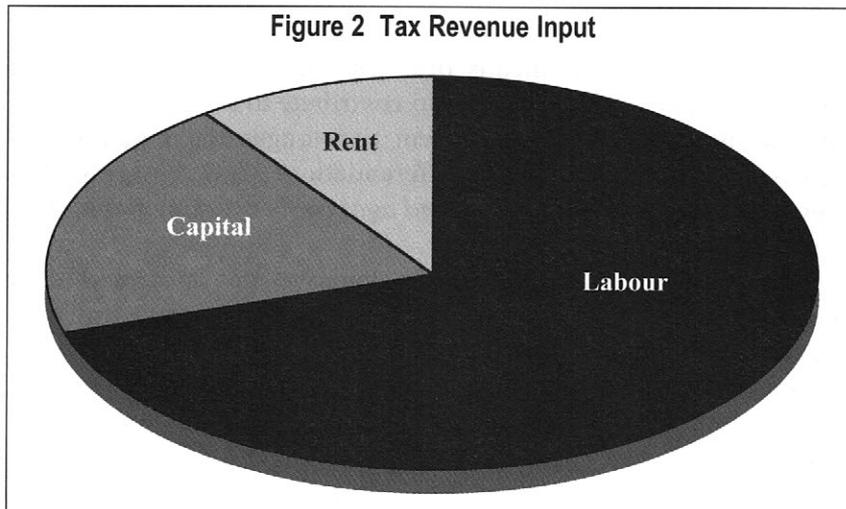
the fundamental causes of biological and social destruction. This would lead to the creation of a new moral economy of the 21st century.

In several simple situations it is possible to separate rent out through leases and the corresponding use of tenders (the market mechanisms). Rents established by these auction are the economic rent that constitute the national dividend. The winning bidder would become possessor of the resource, but not its owner. Now it is relatively easy to calculate his profit and he pays profit-based taxes. Note that a special committee that acts on behalf of society may cancel the deal or delay the auction if the rent is lower than it should be.

But the main thing is that society, being the owner of natural resources (with the government as its trustee) is able to control the activity of possessors and impose particular rules and regulation on the exploitation of resources. If these rules are violated, society has to have the right to cancel the lease (through due process in court). Rent that is paid by the possessor is neither tax nor part of the budget. It is the national dividend that must be spent in the interests of the whole society. The sum of this rent is a public contract.

Rental Income and the Current Tax System

The existing tax system is based on the taxation of labour. Our prices, calculations and profit accounting systems, and therefore the tax base, are built around it. Here lies the main paradox of the current tax system. On the one hand the share of labour in GDP growth is not more than 5-7%, on the other hand we try to get up to 70% of taxes at the expense of this oppressed factor of production (*Figure 2*).



It is well known that Russian wages are inadmissibly low and the exploitation of employed workers is impermissibly high. That's why



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under current conditions wages must not be the principal base of taxation. Moreover labour taxation increases costs of production by two times. That's why our domestic production is extremely expensive and therefore uncompetitive compared with imported goods. But that is not the only problem. By raising the price of labour, the tax system makes it unprofitable for businessmen to employ people, and encourages them to *fire* and not to *hire*. As a result we cannot avoid growth of unemployment, an increase in the "declassed" and homeless population, growth of poverty and income differentiation. This

is followed by the increase in social and psychological burdens and mortality. This problem has another very dangerous edge. The current tax base allows our monopolists to appropriate unaccounted rental income very easily. This income is then allowed to flow abroad.

As we now can see, the tax system acts as a suppressive factor for industries that are domestically oriented and which try to solve the problem of domestic demand and to contribute to a higher quality of life. At the same time this system encourages the migration of capital, corruption, and social differentiation. *Thus the tax system works against national business and against the working population of Russia.*

It is conceptually impossible to improve this system with a number of additions and corrections. It took vast amounts of time and resources to develop the new Tax Code. And taking into consideration all the above problems, we must acknowledge that these resources were wasted. We need to change the basic principles of taxation. It doesn't matter that these principles are widely used in Western economies.

Unlike many other countries, Russia's main source of wealth is its rental potential. But that is the present situation. In the future we will have to shift from natural rent to intellectual rent. To achieve this we must concentrate on science and technological progress and develop the knowledge-based sector. We have all the necessary preconditions and possibilities for that. And we must shift the tax burden from wages and capital onto rent.

Government must avoid prophylactic shifts of the tax burden from one tax to another. It has to correct the main contradiction of the tax structure, by shifting from wage taxes to resource rents. All taxes on wages should be eliminated. This major need remains unacknowledged. In fact we should do the following:

- ◆ Remove all taxes and charges on wages, and eliminate VAT.
- ◆ Taxes on profits should be stabilised as a fixed share for the budget. Currently, this share could be about 55-60%.
- ◆ Capture nearly 100% of rent, which would be consolidated in public natural dividend funds.

We would then be able to lower the costs of domestic goods, increase their marketability and compete against imported goods in the domestic market. This would create additional incentives to use



Left to right: Irene O'Connor, Neil Gilchrist, John Nairn, Victor Allen, Hilary O'Donovan, Mike Curtis, Bruce Michels, Alex Hardie

machinery more effectively and to hire more workers. The economy would start to grow, and wages would rise.

To conclude, I must say that the transition to the rental system would lead to a more effective interaction between Humanity and Nature. This is unavoidable. This would base itself on the use of the planet's carrying capacity. To reach this we should implement both rental payments and compensating ecological taxes that would work against the depletion of natural resources.

Ecology taxes would not lead to an increase in the tax base. There is no methodological problem. The only challenge is to prepare an appropriate legislative basis for the transition to a National Dividend System. I consider this issue to be not very complicated and think that it can be solved at an early date. The main difficulty is the vested interests of those who made their great fortunes out of the appropriation of the country's rental income, and by the uncivilised exploitation of the country's natural capacity. This should be taken into consideration, especially because a significant number of our rent-receivers are representatives of big business and authorities. But the price is very high. The bet is our future and the future of our country. For the sake of the future we must fulfil a transition to the rent-oriented tax system.

It is necessary to prepare and pass several legislative bills to develop a national dividend concept:

- ◆ We need to create the Future Generations Fund (which would accumulate rental payments) and constitutionally fix its total as an inviolable financial resource of society.
- ◆ We should create legislative procedures that regulate rent charges. (The US State of Alaska is a good example: one half of oil royalties are charged and forwarded to the Future Generations Fund).
- ◆ We have to establish a progressive system of collecting payments from income of companies, charging for every additional dollar above some normative price.

It is necessary to set up rules and principles on how to share rental income between federal, regional and local tiers of government.

It is important to develop a clear and legal order for the Future Generations Fund expenditure.

The national dividend system is a new model of social, economic and ecological development for Russia. It would enable us to solve contradictions and issues that prevent our economy from propulsive growth. This model could be used by other countries to rebuild the

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world economy on the basis of principles of joint protection of the future, prosperity in developing countries, and the elimination of the root causes of global crises that have struck a world at the dawn of the third millennium.