

Rent as Public Revenue

The strategy for Russia's breakthrough to the future

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ECONOMIC science does not offer proposals for an effective economic system because it is based on principles that ignore the moral and spiritual development of society, claims Dmitry Lvov.

Social and economic development is possible only when the public conscience forms the basis of the will of government. People should be supported by their native culture and spirit. This is the only way to avoid the transmutation of human beings into a physical "labour force" that waits to be exchanged for lifeless animal comforts.

The moral and political challenge facing Russia's leaders can be summed up in one statistic: more than 90% of the population is excluded from the rent of natural resources. This destroys the historical ideas about peace and

justice that are embedded in the sacred legends of the nation.

Russia loses \$15 billion annually to corruption, according to Alexander Kulikov, deputy chairman of the State Duma Security Committee. He reports that organised crime controls around 40% of private firms and 60% of public-sector enterprises. The share of banks under its control is even greater, at around 85%.

The single most important instrument that would enable Russia to break through to a future based on justice, writes Dmitry Lvov, is to place taxation on a moral foundation. People's wages should be untaxed, and the rent of nature's resources should be devoted to financing public services. Every citizen should receive a share of rent through a National Dividend.

IT IS FASHIONABLE to say that ineffective labour is even worse than permanent unemployment. That is the reason why full employment is sacrificed to the so-called principle of "the maximisation of exchange value wealth". In Russia, this thinking leads to the abandonment of decaying industries, territories and cities, the extinction of professions, the dying out of national productive forces on a giant scale.

Modern economic theory justifies this. Maybe the words of Friedrich List could serve as the best answer to this theory: "There is no world of Wealth! The concept of the world can only be spiritual or alive ... How can we talk about the world of minerals, for example? Eliminate the spiritual basis and everything that is called 'wealth' will become a lifeless substance. Remember what happened to the treasures of Carthage and Tir, to the wealth of Venice palaces when the spirit had gone from these heaps of stone?"

The spiritual and moral renaissance of the nation is the starting point for the breakthrough to the future. Power should be used to consolidate society, to eliminate the root causes of injustice which prevent peace and harmony. Above all, those causes are revealed in the context of property problems.

The main factor that affects a nation's prosperity and its moral component is the way in which it shares public wealth. Public wealth is a function of three main factors of production – waged labour, capital and the entrepreneurial risk-taking associated with it, and rent (i.e. income from land, the territory's natural resources which include air space, radio frequencies and other monopolistic activities). Under present conditions, Russian public wealth, the rent of nature, constitutes about two-thirds of the nation's income. The remaining third is divided between labour and capital. In other words, *almost everything that Russia obtains today is the rent from the use of its natural resources.*

The economic essence of rent is that it's not the "creation of mankind". Figuratively speaking, this is God's gift to Russia. That is why if we look from the moral, ethic, humane and spiritual points of view we can clearly understand that rent should belong to everyone (i.e. to the whole society). The current distribution system corrupts this principle. Only a quarter of rental income is being accumulated via taxation as public income to satisfy public needs. The rest (75%) passes by the treasury and stays in the pockets of financial magnates and a huge number of middlemen. The estimated annual value of that part of rental income is about \$40-45 bn. That rent is amassed in the hands of the richest people – nearly 10% of the Russian population. Those people have access to power, and they can influence the making of the most important strategic decisions. As a result, more than 90% of the country's population is deprived of access to public goods gifted by God!

This immoral situation destroys historical ideas about social peace and justice that can be found in the sacred legends of the nation. Absence of equal access to the goods gifted by God is a deadly sin.

Immoral privatisation of public revenue THE IMMORAL appropriation of rent is compounded by the immoral appropriation of the biggest part of the income from capital that was formerly owned by the population. As a result of three waves of privatisation – the voucher and mortgage schemes, and artificial (false) bankruptcy – state property was passed to private persons (the so-called “new management”) and not to new shareholders. The “new management” came to control and use the rights of all shareholders without their permission. Managers freely distributed not only profits but also total revenue from economic activity, including depreciation. Thus privatisation did not increase productive efficiency. The only result was the theft of public and collectively-owned property and the immoral appropriation of national income by the upper 10%. Government, one of the main owners of enterprises with mixed-ownership rights, kept itself aloof from administering its assets. To a great extent this made the situation even worse.

The criminalisation of the economy, the extraordinary social stratification of the population based on the distribution of income, the huge scale of poverty, the all-consuming monopoly of power and production, the wave of illegal bankruptcies, unjustified accumulation of financial resources in the banks accompanied by impoverishment of the productive sector, mediation and barter – these are the direct outcomes of the immoral privatisation of public revenue. That is the reason why there are two different images of Russia: *poor Russia – for everyone*; and *rich Russia – for the privileged few!*

To break through to the future, Russia should change the system of public revenue distribution. Only by returning financial resources to everyone can we achieve sustainable economic growth and prosperity for every citizen. That is the way to create a real market economy based on moral principles: *equal starting conditions for everybody and opportunity to express himself/herself*. If we solve that problem our future will be bright. If we fail – we will continue to live and vegetate like beggars!

Strategic directions of income policy DRAMATIC CHANGES in the social conditions in Russia are bound up with wages. The reforms “liberalised” all factors of production, but labour persists as the most “depressed” factor.

It is true that labour productivity is much lower than in the Western countries. But the level of wages cannot be excused by reference to lower productivity. Our average worker produces three times more output per dollar of wage than a worker in the USA. Our average

wage in industry is 5-7 times smaller than the one in the West. The UN has acknowledged that a wage less than \$3 per hour is inadmissible. Such a wage pushes the worker below the "red line" of vital activity. Below that line the labour potential is destroyed. And how much does our skilled worker get each hour? 3-4 times less! And our worker has to exchange his labour for goods and services that are almost as expensive as in Western countries.

In the market economies the income of a worker is broken down in the following way: direct taxes make up 20-40%, housing payments – 25-30%, deductions to private pension funds – about 5%. Insurance adds another 5%, purchase of different goods and services – up to 30-40%. Those rates are considerably different in our economy. The costs of goods and services make up almost 70-80% of wages. An enormous number of workers can hardly find money for food. If the current extremely low level of income persists the government would not be able to refuse to finance normal vital activities of the population.

The doubling or tripling of average wages is realistic; in fact, it is unavoidable, if we are to overcome the gap in incomes between the rich and the poor, which has opened up to a very dangerous degree.

We should eliminate the economically empty category of a minimum monthly wage. It should be replaced by an assured minimum per hour wage. That wage must gradually reach a point that covers the cost of living (\$2.5-3).

At the same time it is necessary to revise tariffs and charges, which prevent the increase in the efficiency of production and obstruct an active investment policy. The current level of tariffs imposed on scientific institutions and organisations that determine scientific and technological progress seems to be out-of-date. It is necessary to equalise the remuneration for labour. Priority should be given to science-intensive industries. If government is concerned about the future its primary task should be to raise wages in those industries, which should then become a starting norm for other sectors.

It is necessary for every Russian family to share in the flow of income from state property and above all from the natural resource potential of the country. That strategic aim should be achieved through a special income distribution policy. The essence of those measures is to socialise the income of the "upper 10%" and to use it to support social groups that need help to kick-start economic activity. The way to achieve that goal is taxation of real estate and luxury.

From the economic and political points of view the main tax burden should be shifted from incomes to people's real estate. Real estate should become the tax basis for local and state budgets.

It is necessary to declare the principle of free housing for people on the

lowest incomes, free land plots (for personal use as gardens and for dachas), and other social guarantees.

State guarantees should be expanded to the other social, scientific and technological spheres: a fixed share of GDP must be reserved for education, medical care and science.

On pensions, there are wide discussions about a shift from the Soviet "solidarity" pension system to the so-called "accumulative" system. Under Soviet conditions, the social security of pensioners was provided by deductions from the wages of working people. If we talk about free-will deductions from wages for the future pension payments, we must welcome these accumulations as additional sources of pension security. We need to consider how to encourage the creation of private pension funds, and to promote money and investment flows into the economy. *But if a shift towards the accumulative pension system means the gradual reduction of state support for older generations and the disabled, and forcing people to support themselves in their old age, then we must unconditionally give up such a strategy.* Many countries have already abandoned the "attractive" accumulative system of the American kind.

**Failures of
the voucher
privatisation
scheme**

ONE OF THE STRATEGIC goals of Russian economic development is to correct the distortions that occurred as a result of the voucher privatisation scheme.

Government reformers have failed with privatisation. That is true if we judge from the point of view of national interest rather than from the point of view of the groups that have greatly benefited from squandering the wealth of the country.

The justification for privatisation was that the market would allocate resources. This is either a malevolent hoax or a dangerous mistake. The division and re-distribution of state property will last as long as current and new participants continue to have extraordinary abilities and extraordinary incentives to play the game. That process had and still has nothing to do with real market mechanisms in the sphere of property rights.

And this is not an accident. We still do not have clear definitions of property rights and rules on how to apply them to all kinds of property. We still have to elaborate procedures for subdivision, joining and transfer of property rights.

The essence of the current situation may be expressed by two observations.

- Economic power is being redistributed with the help of political power.
- Political problems are being solved by alienating "tasty morsels" of public property.

We have to acknowledge that it is impossible to return to the situation

that prevailed before the start of privatisation. What is the solution? First, we should not allow government to lose its status as the major owner (selling out, issuing stocks, shares, etc.). We must avoid governmental loss of the right to control the activities of corporate enterprises and to share their profits (via state share holdings). An exception applies to housing. Existing rights obtained through privatisation should be retained by persons and companies (except for the most scandalous cases of destructive or half-criminal privatisation).

AFTER THE RIGHTS of government are secured, it is necessary to perform a transition to the new system of state property. The major elements of this system are:

A new system of state property

- Securing, through the Constitution, a significant part of the nation's natural resources in the ownership of society;
- Open competitive market regulations should apply to the management of state property;
- A National Dividend – part of the income of entrepreneurs and all rent from commercial use of national property – must be used as the main source of revenue for the social guarantees fund.

Government as the supreme power, and its corresponding infrastructure (non-profit public enterprises, services and social organisations), should be supported by direct and indirect taxation. This is the first part of national assets.

The second part – natural resources, energy, transport and communication enterprises, extracting sectors and other property that still belongs to the state after privatisation and which can provide income – should be made available for commercial use to achieve maximum economic efficiency. The main legal form should be *leasehold* (which requires a developed market of rights to use and extract income from property). The *open auction of property rights* is one of the possible methods to determine the most effective users of national property.

The effective user of national property is able to pay a rather high price for the property rights (and the benefits he extracts) allocated to him by the Government as a result of an open market procedure. The revenue from these assets belongs equally to every citizen and must be rendered to them in different forms, such as a *national dividend*.

Its distribution must be regulated by the Law and only by the Law. Independent decisions by the executive power should be excluded.

Accordingly, the national dividend as a financial resource should be separated from the tax system and other elements of the revenue part of the state budget.

As a matter of principle *the whole national dividend must become the revenue for all members of society.*

National dividend funds could become the main branch of the social guarantees system. Those funds must be protected from the all-devouring administrative mechanism of governmental charity. Payments from those funds could provide a guaranteed level of living that grows with the growth of revenue from national property.

Thus, the strategic goal – the creation of a system of national property – can help to solve the most important macroeconomic issues: overcoming the enormous disproportions in wages, and the development of a system of social guarantees.

National property and national dividends in combination with the new tax system designed to ensure the effective use of natural resources would serve as a prototype for the new economic model. Progressive mankind is desperately looking for such a new model.

The paradox of taxation on wages THE ADVANTAGES of natural resource taxation are well documented in almost every serious book on market economics. But the examples of implementation of such taxation can be counted on the fingers of one hand. The main reason is not to be found in organisational or technical obstacles that prevent such a transition to the taxation of natural resources (though there are some).

The reason is rooted in the vested interests of those who made great fortunes out of the appropriation of natural resource rents. They do their best to prevent such a transition. That social group is not numerous. But at present it has access to the highest political power. It is important to be aware of those interests; it is dangerous to ignore them. But Russia has no other way.

Today the country gets its revenue mainly from business and labour by direct or indirect taxes and charges. Our systems for pricing, cost accounting, benefit calculation and income taxation are formed in this way. Here lies the main paradox. On the one hand the contribution of labour to the growth of GNP is about 5-7%. On the other hand we try to get up to 70% of all taxes at the expense of this mostly abused factor of production.

We must understand that our wages are inadmissibly low and the exploitation of labour is extremely high. That's why under current conditions wages cannot serve as a basis for taxation. By taxing labour we almost double the costs of production. This makes our goods uncompetitive compared to foreign goods and services of higher quality in the world markets. But there are other important issues.

By overestimating the cost of labour, the tax system makes it unprofitable for entrepreneurs to use labour in production. This doesn't encourage growth. It results in unemployment, homelessness, poverty and further polarisation in income levels. These then add to the social and

psychological burdens of the population, leading to further increases in mortality.

Another dangerous aspect of current taxation is that it makes it easy for our monopolists to accumulate and move abroad a huge part of rental income. That's why when we talk about contradictions between the current tax system and business we mean mainly small business and enterprise. They are the ones that are most overloaded with taxes. Of course taxation also has a restrictive impact on big business, including our natural monopolies. But those that export receive considerable compensation from the state in the form of untaxed rent.

It is fundamentally impossible to improve that system by passing amendments and additions to the present laws. That's what our law-makers try to do today. We must consider as wasted the time and huge resources spent on the creation of a new tax code. It is necessary to change the basic principles of taxation. Governmental efforts should be aimed not at moving the tax burden from one tax to another but at the correction of contradictions within the tax system. This correction is the *shift of the tax burden from wages onto rent*.

GOVERNMENT must understand that the socialisation of rent is both a real opportunity to provide sustainable public revenue and a condition for Russia to remain an independent geopolitical unit and competitive participant in the modern world. To a great extent the solution of that problem depends on whether the population manages to maintain the spirit of participation. This spirit should preserve not only state and political integrity, but also (this is even more important) the unification of the social space that is composed of the territory, economy, culture, history, spirituality and morality.

Society must be declared to be the highest legal entity that owns territorial and natural resources. Such a constitutional innovation would create an operational basis for providing each member of society with equal rights of access to territorial and other natural resources. This would be a substantial addition to the *principle of equal starting conditions for everybody*. Without this principle we cannot achieve social harmony and the perception of common interests shared by all social groups.

Using rent as the source of public revenue can be the material realisation of the highest rights of society to territorial and natural resources.

Thus rent becomes the basis for the constitutional development of society and of the state. The socialisation of rent could serve as a uniting force that provides a worthy future for Russia.

Rent-sharing is the basis for equality