

Convergence Criteria for Sustainability



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IN EVERY COUNTRY of the world, taxation now provides systemic incentives – even compulsions – to unsustainable development in almost every field, including those proposed as the six major themes of European sustainable development strategy:

- Climate change and clean energy;
- Public health;
- Management of natural resources;
- Poverty and social exclusion;
- Ageing and demography;
- Mobility, land use and territorial development.

Changes in public finance and the monetary system could, by their effects, add up to an effective sustainable development strategy in all those fields.

The nature of the necessary changes outlined in this essay are spelt out in greater detail in published work for the European Commission (Robertson 1999) and elsewhere (Robertson 1998 and 2000, and Huber and Robertson 2000). The changes are more far-reaching than EU member states will be able to agree upon collectively by

intergovernmental agreement now. Their agreement on them at a later date, if intergovernmental agreement is still needed then, will depend on increasingly insistent pressure of public and political opinion, as

At a conference in the European Parliament on 2 May 2001, organised by the Club of Rome (Brussels Chapter) with support from Information Society Directorate-General of the European Commission, JAMES ROBERTSON challenged European governments to link public finance with policies for sustainable growth

the need for the changes becomes more widely understood. But that does not mean that EU institutions should do nothing about these changes now. Almost all EU governments are already taking small steps in the correct direction. There are many ways in which EU institutions could help and encourage them to go further and faster.

The point to recognise is that the overall pattern of public revenue and public spending influences the outcomes of economic activity very heavily. In most EU member states, something like 35% of GDP is taken out of the market economy in taxation and other public revenue, and then put back into other parts of the economy as public spending. This has a massive impact on relative costs and prices throughout the economy – taxes adding to the cost of what is taxed, and

public spending reducing the cost of what it supports. In other words, not interfering with a "free market" is a conceptual impossibility, and the proverbial "level playing field" is a mirage. The total composition of public revenue combined with the total composition of public spending will always provide a framework which skews the price structure of the economy some ways rather than others. At present it skews it powerfully in favour of unsustainability.

To recognise this is not to argue in favour of a command economy based on detailed central planning by governments, or in favour of ongoing *ad hoc* interventions by governments in the workings of the market economy. Absolutely not. Both those are damaging – economically, socially and environmentally. It is to recognise that governments' fiscal and monetary institutions and policies should be designed to provide a framework of public revenue collection and public spending that provides powerful incentives to all participants in the economy, operating as freely as possible within that framework, to produce outcomes which contribute to economic efficiency, social justice and environmental sustainability.

Existing taxes are not sustainable

GROWING AND foreseeable pressures for change include the fact that today's tax systems are becoming too complicated and expensive for tax authorities and taxpayers to cope with.

Mobility of capital and mobility of highly qualified people in a competitive global economy presses national governments to reduce taxes on incomes, profits and capital.

In ageing societies, the declining proportion of working-age people will oppose being taxed on the fruits of their work, in order to support the growing proportion of "economically inactive" people.

Growing internet trading will make it more difficult for governments to collect customs duties, value added tax (VAT), and other taxes and levies on sales – especially

on products and services that can be downloaded from the internet, such as music, films, pictures, games, and advice and information of every kind. The internet will also make it easier for businesses and individuals to shift their earnings and profits to low-tax regimes.

Under existing tax systems, governments are increasingly losing tax revenue to tax havens. International efforts – for example by the EU and OECD – to deal with this will grow. But the most effective way to deal with it may be for national governments to shift the tax burden "away from mobile tax bases to immobile tax bases" like land and sources of energy (Gaffney 2000).

Existing taxes and public spending are perverse

TODAY'S TAX SYSTEMS are badly designed. They damage economic performance, social well-being, and environmental sustainability. They discourage employment, savings, success in the growing markets for smart technology, and adding value. They encourage over-use of natural resources, including the environment's capacity to absorb pollution and waste, and under-use and under-development of human resources. They encourage social exclusion and divisiveness, and they encourage people to subtract value by using more than their fair share of resources.

Today's public spending programmes are estimated to provide perverse subsidies, costing taxpayers worldwide US\$1.5 trillion, to promote unsustainable activities (Myers, 1988). This total includes: agriculture, \$460bn a year; fossil fuels/nuclear energy, \$110bn; road transportation, \$639bn; water, \$220bn; and fisheries, \$22bn. The real total, if other sectors were included, would be higher. This figure of \$1,500bn to promote unsustainable development can be compared with the proposed Agenda 21 global budget of \$600bn to promote sustainable development. When that was put forward after the 1992 Rio Earth

Summit, world governments rejected it as wholly unrealistic!

Need and scope for a tax shift

THIS SITUATION creates the need and the opportunity for a tax shift (see, for example, Durning and Bauman 1998, and Hamond *et. al.* 1997). This will be a shift towards a new tax structure which will:

- stop taxing people and organisations on the rewards they earn by adding value for other members of society by useful work, skill and enterprise;
- make people and organisations pay (into the public revenue) taxes or charges reflecting the value they subtract by "enclosing" for themselves the value of common resources – i.e. value which they themselves have played no part in creating, but which has been created by Nature and society as a whole; and
- share out among all citizens the "free lunches" which the value of these common resources offers, instead of continuing to allow landowners, big corporations, big shareholders, top managers and others to "enclose" it for their own profit.

Examination of the existing pattern of taxes in Britain shows that over 80% of tax revenue comes from taxes on work and enterprise, about 11% from taxes on resources, and about 7% from other taxes (including "sin taxes" – on alcohol, tobacco, etc). There is thus plenty of scope for a tax shift. Worldwide the scope appears to be similar – perhaps even greater.

The following are among the "common resources", the value of which has not been created by individual or corporate endeavour and which could provide sources of public revenue, either in the form of taxes or in other ways such as user charges and auctions of licences or permits:

- land sites,
- unextracted energy, i.e. energy in its natural state,
- the environment's capacity to absorb pollution and wastes,
- space (e.g. for use by air and surface transport),

- water (e.g. for extraction),
- the electro-magnetic spectrum (e.g. for communication, broadcasting – licences for the next generation of mobile phones,
- bio-diversity and genetic resources,
- intellectual and cultural resources (taxes on patents?), and
- the money supply.

The money supply

PROVIDING SOCIETY'S money supply could and should become a substantial source of public revenue. That source would not be tapped by a tax, but by changing the present method of creating new money – as proposed in a report published last year on *Creating New Money: A Monetary Reform for the Information Age* (Huber and Robertson 2000).

That report calculated that allowing commercial banks to put the overwhelming majority of new money into circulation as profit-making loans to their customers, as at present, gives the UK banks a hidden subsidy of over £20bn a year. If all new money, and not just cash (banknotes and coins), were created by the central bank (as central monetary authority), credited to the government, and put into circulation debt-free as public spending, that would provide additional public revenue of over £40bn a year. (Comparable figures for the Euro area are not yet so easy to calculate, but appear to be of the order of €60bn and €90bn.)

Apart from providing an additional source of public revenue – allowing substantial tax reductions, increases in public spending, repayment of public debt, or a mixture of these – a monetary reform on these lines will contribute to economic stability and social equity. It will also encourage environmental sustainability. Meeting the costs of having to use money that has been put into circulation as debt and has to be repaid with interest, as at present, compels higher levels of production and sales than would otherwise be necessary. Removing that compulsion will have many beneficial effects, including a contribution to environmental sustainability.

Ecotaxes must not be regressive

IT IS GENERALLY accepted that the part played by environmental taxes must grow. But it is also accepted that, if existing taxes on incomes, profits and savings were replaced by environmental and resource taxes imposed directly on consumers (i.e. at the end, rather than the beginning, of the "economic pipe"), the change would hit poorer consumers relatively harder than richer. For example,

- value-added tax (VAT) on household energy hits poorer households harder than richer ones;
- fees and charges to reduce urban congestion hurt small tradespeople more than users of chauffeur-driven limousines; and
- very poor people have to pay ecotaxes, at least to some extent, but do not benefit from reductions in taxes on incomes, profits, capital gains, etc, which they do not now have to pay.

If environmental taxes and charges are to become a really significant source of public revenue, this will have to be remedied. How?

First, environmental taxes and charges should be levied upstream whenever possible. A key example is a tax on carbon-energy (or on fossil fuels and nuclear energy), *collected at source*.

- It will reduce pollution, because pollution arises predominantly from energy-intensive activities.
- It will be administratively simple.
- It will be seen to impact richer people's incomes and wealth by reducing the salaries, dividends, pension contributions, stock options, capital appreciation, etc, from energy-intensive businesses.

But that will not be enough. The regressive effect on consumers will remain, and will have to be offset in other ways. Environmental taxes will have to be part of a larger package of changes.

Second, then, land value tax should be part of this package. It is, in fact, an environmental tax – a "sprawl tax" (Durning and Bauman 1998: 57-65). Land value tax is clearly progressive. It is not the poor but

the rich who are enriched by "enclosing" the value of land.

But even this will not offset the regressive effect of the tax shift for people who now pay no tax except value-added tax (VAT). They will have to be helped to offset in some other way the new costs of the higher environmental and resource taxes.

So, third and crucially important, it will be necessary to use revenue from the new environmental and resource taxes progressively, as an element in the total package of measures included in the tax shift. There are many ways this can be done. One is to use it to help poorer people to reduce the higher household energy costs arising from energy taxation. Others include using eco-tax revenue to distribute eco-bonuses as contributions to a basic income (von Weizsacker, E.U. 1994: 76). This earmarking of the revenue from a particular tax to be spent for a particular purpose (hypothecation), raises questions about the philosophy of taxation (Commission on Taxation and Citizenship, 2000: 154-185). These need to be worked through, as an aspect of a strategy for sustainable development.

Tax shift and redistribution of incomes

IT IS GENERALLY accepted that one of the functions of taxation should be to redistribute incomes and wealth. It is often assumed that this function requires incomes to be taxed *directly*. A shift away from taxes on incomes and profits will run counter to that assumption. This needs to be examined more closely.

A shift from taxes on the rewards of work and enterprise to taxes on resources like land and energy will be a shift from taxes on economic *outcomes* to taxes on economic *inputs*.

That means it will be a shift from *after-the-event redistribution* of value that has been created by economic activity, to *before-the-event predistribution* of the value of inputs on which economic activity depends.

Today it is widely taken for granted that the state should counteract the *outcomes* of

economic activity and redistribute value at the end of the economic "pipe". Predistribution, on the other hand, will act at the beginning of the "pipe" – to share more widely the value of essential *inputs* to economic activity and, in that way, to generate more equal outcomes from it.

Whereas redistribution tends to reinforce dependency, predistribution will better enable people to achieve economic wellbeing for themselves.

Predistribution will address the underlying causes of economic injustice, inequality and exclusion that arise from the private and corporate "enclosure" of common resources. It can be seen as an essential feature of a prosperous economy in an inclusive society.

In practice, the redistribution-of-incomes approach has not proved very successful either within nations, or between them. In principle, the arguments for predistribution would seem to be powerful. But more detailed calculations about the redistributive effects of the tax shift will no doubt be necessary before the social arguments, as well as the economic and environmental arguments, lead to its adoption as a sustainable development strategy.

The global dimension

THE PRINCIPLES we have been discussing for national public finance and the creation of new money apply at the global level too.

The Commission on Global Governance recognised five years ago that global taxation is needed "to service the needs of the global neighbourhood". Global taxes, based on the use each nation makes of global commons, could include taxes and charges on use of international resources such as ocean fishing, sea-bed mining, sea lanes, flight lanes, outer space, and the electro-magnetic spectrum; and taxes and charges on activities that pollute and damage the global environment, or that cause hazards across or outside national boundaries, such as emissions of CO₂ and CFCs, oil spills, dumping wastes at sea, and other forms of marine and air pollution (Commission on Global Governance 1995).

The Commission also pointed out that international monetary reform is becoming urgent: "A growing world economy requires constant enlargement of international liquidity". The principle underlying the proposal to put new money into circulation as debt-free public spending at the national level could equally well be applied at the global as well as the national level.

Revenue from global taxes and putting a new global currency into circulation could then provide a stable source of finance for UN expenditures including international peace-keeping programmes. Some of the revenue might also be distributed to all nations according to their populations, reflecting the right of every person in the world to a "global citizen's income" based on an equal share of the value of global resources.

This approach would encourage sustainable development worldwide. It would generate a much needed source of revenue for the UN, and provide substantial financial transfers to developing countries by right and without strings, as payments by the rich countries for their disproportionate use of world resources. In addition, however, it would help to liberate developing countries from their present dependence on aid, foreign loans and institutions like the World Bank and the International Monetary Fund, which are dominated by the rich countries. It would reduce the risk of another Third World debt crisis; and it would recognise the shared status of all human beings as citizens of the world.

International fiscal and monetary harmonisation?

IS INTERNATIONAL harmonisation more likely to help or hinder the conversion of national fiscal and monetary policies and institutions into agencies of sustainable instead of unsustainable development? Should every EU member state have to agree to this conversion, before any one state can be expected to embark on it?

It can be argued that, as a general rule, in an increasingly "weightless" information-based and knowledge-based world

economy, the faster a national economy can shift towards sustainable development the greater the competitive *advantages* it will achieve against national economies that shift more slowly. As that becomes apparent, it will provide an incentive to government, to accelerate the introduction of their own new fiscal and monetary and regulatory incentives for sustainable development. Once this process gets moving, progress towards a sustainable development path worldwide and in the EU as a whole may be generated more effectively by piecemeal competition between states seeking economic advantage than by harmonised intergovernmental decision-making.

In that case, to wait for internationally agreed convergence and harmonisation would simply give opponents of sustainable development – such as the energy-intensive, resource-intensive and high-polluting industries – a better opportunity to gang up with their counterparts in other countries to resist the changes it calls for. They would argue that a member state should not introduce new regulatory and fiscal incentives until all member states had agreed to do the same. Moreover, the convergence targets eventually agreed would almost certainly fall short of what is actually needed.

On the other hand it is clear that, even in countries where most people will clearly benefit, powerful sectors will oppose the fiscal and monetary changes required to encourage sustainable development. The energy-extractive, energy-intensive, resource-intensive and high-polluting industries will argue that, if their government shifts the burden of taxation on to pollution and energy faster than governments of other countries, they will be at a disadvantage against their competitors in those other countries. So internationally agreed measures may be needed to ensure that certain sector-specific *disadvantages* arising from the shift to sustainable development should equally affect the relevant industries in all EU member states. These measures can, for example, take the form of import tariffs and export rebates,

which will offset the tax difference between the various countries concerned.

Another example of the need for international agreement will be when EU member states begin to realise that shifting some of their tax burden off Value Added Tax and on to Land Value Tax will serve the cause of sustainability – and economic efficiency and social justice – and decide they want to make that change. This will involve renegotiating the existing arrangements for financing EU institutions.*

In addition to situations of that kind which necessarily require agreement between EU member states, there are many other ways in which EU institutions can help member states to shift towards sustainable development. They could, for example, encourage member states to study and discuss the proposals I have outlined for a new approach to public finance and the monetary system.

More specifically, they could compile an EU-wide set of economic, social and environmental sustainability indicators for member states. These would be concerned with things like :

- reducing CO₂ emissions, reducing total energy use and raising the percentage of energy needs met from solar sources;
- reducing the transport of goods (e.g. by reducing “food miles” – the distance food travels from producers to consumers), by increasing the proportion of local consumption met from local production, and reducing imports and exports as a proportion of GDP; and indicators of a physical nature.

But they could also include relevant fiscal indicators, such as

- reductions in perverse subsidies;
- reductions in perverse taxes;
- reductions in the proportion of the total

* In that context, if the Eurozone adopted the reform proposed in *Creating New Money* (Huber J. and Robertson J. 2000: 63), its member states would probably no longer need to make an annual contribution to the EU budget but would receive an annual dividend from the European Central Bank.

- tax burden falling on rewards for work, enterprise, value added, and savings; and
 - increases in the proportion of the total tax burden falling on the use of resources (including pollution).
- Annual publication of an EU "Progress Towards Sustainable Development" Index based on many different indicators of this kind – broadly on the lines of the UNDP Human Development Index – would make it possible to compare the progress made by EU member states with one another and with the rest of the world. This could provide a useful spur to national improvement.

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