JUSTICE IN DISTRIBUTION

"What is truth?" -- Pontius Pilate

The classical political-economists made distribution of wealth and income the centerpiece of their discipline. This led smoothly, if unintentionally, into the socialist slogan, "The problem is not production, but distribution." From about 1890, "neoclassical" economists preferred to downplay distribution. Distribution is troublesome, they said, because beliefs about it are often subjective and value-laden ("normative"), and there are numerous conflicting value-systems, hard to reconcile. They should have added, there are powerful interested parties monitoring and subsidizing scholars.

The neo-classicals redefined the discipline as "the study of the allocation of scarce resources among competing ends." Thus "efficiency," which few can oppose, becomes the universal performance standard, acceptable and helpful to all but the undeserving. A rising tide lifts all boats; contesting the distribution of gains is counterproductive squabbling. Interpersonal comparisons of utility are impossible. The only distributive changes allowable (from the status quo) are "win-win" exchanges. Private property rights, individual and corporate, must be firmed up, clarified and extended to as many aspects of life as possible, so the price system can operate universally. Modern Chicago School economists generally hew to that tradition. Some of them believe they have achieved a "scientific" basis for social science, "positive" economics, free of subjective value judgments.

The cutting edge of the philosophy is its implication for tax policy. "Uniformity" and "neutrality" are the criteria of taxes compatible with the performance standard of efficiency. These criteria informed the Tax Reform Act of 1986 with which we are now living.

Critics say the neo-classicals sneak in their own value judgments under the guise of objectivity, especially the judgment that existing individual claims on property (the status quo) should be validated. There are other questions, too. How can privatization of commons proceed without promoting inefficient "rent-seeking" behavior? Why must rent be taken privately? Why is individual gain-seeking the only acceptable driving motive of human behavior? Why is common-pooling of resources acceptable inside corporations, partnerships and private clubs, but not otherwise? Is neo-classical economics "objective" for everyone, or just for a propertied elite?

The critics have good points, but even were they wrong, a tax system cannot promote efficiency without also achieving equity (economic justice). The basic reason is this. People demand equity; the great religions preach justice, an ideal by no means limited to professed socialists. If the people don't get justice through the tax system they will demand it through other devices, most of which are highly inefficient and counterproductive. These devices include looting, graft, price controls, handouts, open access, debt repudiation, and cross subsidy.

There follows a list of 17 ideas of distributive equity, most of which you will recognize, at least vaguely. There may be more, and certainly the elements are mixed into dozens more combinations. 17 basic ideas, however, are enough to help you understand the Pontius Pilate position. There are also common threads, and our effort, rather than multiply combinations, will be to reconcile these where possible, and downgrade some, and suggest a package that is consonant with the demand for equity and the needs for efficiency, capital formation and productivity.

After listing them I will give more detail on each.

1. Functional equity: reward effort, productivity and capital formation.

Lemma I: tax or otherwise socialize unearned (non-functional) wealth and income.

Lemma II: Bigger pie, or "rising tide" theory.

2. Free market equity: justice results from perfect competition and free exchange

3. Egalitarian equity: use taxes to level wealth and income.

4. Intergenerational equity: birthrights for the young; security for the old.

5. Ethnic equity; gender equity.

6. Status quo equity: validate existing claims, regardless of their origin (whether as "earnings, findings or stealings").

Lemma I: contract theory of the state; benefits-received theory of taxation.

Lemma II: only an "old tax is a good tax." Only "win-win" changes are tolerable.

Lemma III: older uses of land deserve protection against new, higher uses.

Lemma IV: priority basis of property rights.

Lemma V: property as a moral good in itself, regardless of functional justification.

7. Median voter theory: "public choice"

8. Interregional equity

A. Domestic

Open access to better resources
Indirect open access via local taxes for public goods
Regional cross-subsidy
Horizontal fiscal balancing: equity among electoral districts
Subsidies to develop frontiers
Subsidies to sustain backwaters: "area redevelopment"

B. International
Common rights to oceans, polar regions, space, radio, airlanes, etc.
Duty to LDCs
Islamic solidarity and Arabian oil, etc.
Overlap of equity issues with imperialist and ethnic issues. The Crusade concept.

9. Pressure group equity: "a fair shake for the oil man," the surfer, the hunter, the farmer, the banker, ...

10. Consumerism as equity: Nader as folk-hero.

11. Middle class populism: "farm folks are good folks."

12. Merit as equity. Calvinism redux. Social dividends given only in form of education, or loans, requiring responsible response by grantee. _Noblesse oblige_.

13. Environmentalism: equity as preservation of desired natural conditions.

14. Equity in kind: rationing, military service, etc.

15. "Aesopian equity": reward the provident saver.

16. Anti-commercial equity: penalize fast turnover, trafficking, etc.

17. Contractual equity: enforce contracts; collect debts.

Details on Concepts of Equity

1. Functional equity

This refers to distribution among factors of production, regardless of who owns them -- even if some government owns them.

The prime factors are land, labor and capital. These are "prime" because:

a), some of each is necessary for all production;
b), they are not generally convertible into each other;

c), each has distinctive qualities not shared by the others;

d) the rewards of each tend to rise and fall together with others in the class, but not with others outside the class. Reproducible capital, especially, is a "pool," meaning each molecule loses its individuality with each turnover, so there is a common unit and a common rate of return. Labor is generally interchangeable, and completely as one generation succeeds another. Land is the least interchangeable within its class, never turning over or losing individual identity; but the structure of rents is subject to common influences, moving inversely with real interest rates and real wage rates.

The functions of factor payments are:

a), to educe and maintain and renew the factors (labor and capital only);

b), to induce the allocation of all three factors to the best uses.

Justice here means that those who give more should get more. "The work ethic," or "workmanship" is a virtue that Justice rewards. The saving ethic is also a virtue to reward. These justify returns to labor and capital, respectively. Justifying the rent of land is a sticking point, as land is not created by work or saving. Champions of functional equity have therefore had to choose among three options:

1, to ignore the point by silence, or equating land and capital;

2, to blend functionalism with 6, status quo equity; 7, median voter theory; 9, pressure group equity; 11, middle class populism; 13, environmentalism; 16, anti-commercial equity; and/or 17, contractual equity; or

3, to equate land rent with taxable surplus and let it be socialized by taxation.

There are two methods of establishing, identifying and measuring individual contributions.

a), The classical method determines wages and interest in the market, and treats land rent as a "residual";

b), The neoclassical method has every factor including land gets its MP, and distribution is exhaustive. (This should be covered in micro courses, but is often neglected.)

<u>Lemma I</u>: nonfunctional payments are unearned, therefore subject to socialization via taxation, followed by common distribution as "social dividends" (in cash or in merit goods), in which each citizen has an "entitlement," as a "common heritage." Socialization of unearned values, coupled with strict privatization of earned values, balances individual rights with common rights.

Some spokesmen for this view have been: John Locke, William

Bradford, Francois Quesnay, Pierre Samuel Du Pont I (not Pierre IV, our contemporary), Adam Smith, Tom Paine, Thomas Jefferson, Abraham Lincoln, John Stuart Mill, Alfred Russel Wallace, Henry George, Knut Wicksell, Leon Walras, Philip Wicksteed, Sun Yat-Sen, and others. In a limited way it has been practised by several nations and leaders at various times, including such unexpected parties as the Emir of Kuwait, (although he kept more than his share personally).

What is "unearned"?

a. Land rents (because land is not produced by capital formation process of saving);

b. Increments to land value (starting from zero).

Some tax provisions consonant with this ethic are these: earned income credit; property taxation, especially that based on land price; personal exemptions from income tax; corporate income tax; inheritance taxes; "capital levies"; exemption of direct labor services from sales taxes; severance and yield taxes on resources; etc.

Lemma II: Rising tide theory. This tells us to think only of maximizing total output, to accept or overlook unequal distribution in order to raise the tide which "lifts all boats." This is at opposite pole from socialist ethic which says "the problem is not production, but distribution."

A problem with both views (socialist and rising tide) is that some things are not produced, or produceable, but limited in quantity, so one person's abundance of non-produceable land is always at the expense of others' shortfall.

2. Free Market Equity

Here, equity is the absence of market power, either private or public. Inequity is control over price by private combination (monopoly, cartel, trade association, etc.) or public law.

Corporations are, by definition, combinations of individual capitals, with corresponding potential for using the combination in restraint of trade. That is why we have a corporation income tax, to offset this advantage. Historically, the corporation tax preceded the personal income tax by several years, and only in recent years fell below the personal income tax as a revenue source.

Standard-brand economists today often carelessly identify free markets with large corporations. We have gotten so used to corporations it is easy to forget each one is a combination by itself. They treat each corporation as an individual unit, and only regard combinations-of-corporations as "combinations" in the menacing sense (and often not even them, unless they are foreign and state-sponsored, like OPEC). Thus free market advocacy has been coopted by and identified with conservatively-biased people, including monopolists, even though competition and free markets are inherently radical and anti-monopolistic in what they do. This is a complete reversal of the original meanings, and a source of deep confusion.

During the Progressive, trust-busting era most people understood that busting trusts was to aid competitive business. Again, when Robert LaFollette ran for President in 1924, it was understood by many that he was anti-monopoly and therefore pro-enterprise. Fewer people, perhaps, understood that Herbert Hoover's program was to cartelize American industry and limit competition. Again during the 1938-41 reign of Thurman Arnold and Tommy Corcoran it was understood that anti-trust meant pro-enterprise.

Restrictions on factor mobility, or on entry into lucrative trades or markets, violate free market conditions and generate monopoly profits or rents in the protected field. Free market advocates censure these rents (variously called "monopoly" rents, or "transfer" rents). Their censure usually slights the equally non-functional background land rent on which monopoly rents are superimposed. "Libertarians" (modern philosophical anarchists) focus their censure on trade barriers erected by governments. They either accept, or deny the existence of, purely <u>private</u> barriers to free markets.

Free market equity points to five kinds of policies.

a) Removing state barriers to free mobility and exchange: tariffs, farm programs, licensing, much zoning, franchises, charter requirements, capital requirements, etc.

b) Making taxes either uniform or flat, to keep a "level playing field."

c) Favoring small firms over large, to promote competition and entry [not always consistent with (b)].

d) Regulating natural monopolies to make them charge prices no greater than average cost (and preferably equal to marginal cost).

e) Prosecuting combinations in restraint of trade.

The most obvious tax tool for favoring smaller firms would be to make the corporate income tax graduated, or progressive. Congress has never even considered doing so, except in token fashion, even during its most radical years in the 1930s. This says a lot about Congress.

Taxes on wealth, even if not progressive, tend to break up large concentrations of wealth. Such concentrations are an obvious source of economic and political power to dominate markets and interfere with factor mobility.

3. Egalitarian Equity

Here, "equity" is identified with "equality." Etymologically this makes sense: both words come from the Latin aequus. The etymology also tells us this identify has deep roots in history, for to the Romans aequus meant both equal and fair. In the Scriptures, "justice" generally refers to helping the poor (although John and Paul go off on another tack, and equate justice with having faith).

Egalitarianism sees the state as an extended family or tribe, with duties to all. This is called the "organic" view of the state. A problem has always been, how far does this family extend? Most prosperous nations attract immigrants, and exclude them from full equality, at least at first.

The slogan of egalitarianism is "From each according to ability; to each according to needs." The substance of the policy comes in defining the key words, ability and needs.

"Needs" can mean a safety net under the poor and disabled; or it can be dismissed as being subjective and/or paternalistic, and simply justify a social dividend for everyone.

"Ability" comes down to "ability to pay," and has different meanings at different levels of perception.

a) At the lowest level of perception, ability to pay means having money, i.e. being liquid. Taxes on gross sales and payrolls and property transfers and interest and dividends and severance have this rationale. No account is taken of the long or even short term costs of attaining current gross receipts.

Inflation is also a general tax on having money (or claims denominated in money).

b) At the next level, ability refers to cash income. This is gross receipts less expenses -- called "cash flow" -- less depreciation of fixed capital, and less selected personal expenses, some arbitrarily included or excluded. The personal income tax is of course the vehicle for implementing taxation according to this concept of ability. Generally our tax is based on the net income of property, and the gross income of labor. Although the tax thus treats property income preferentially, it does include increases in wealth -- but only when and if they are realized by sale.

c) At the next level, ability refers to holding wealth, regardless of liquidity and regardless of cash income. Taxes based on wealth are the property tax, the inheritance tax, benefit assessments, and capital levies. There are also special taxes on the revenues from wealth: corporate income tax, yield and severance taxes, property transfer taxes.

d) At the highest level of perception, ability includes unrealized increases of wealth (i.e. increased market prices for land and common stock held but not sold). Tax economists define income so as to include these (they are called "Haig-Simons" income). Congress has excluded them (although only by inaction). The property tax, we will see, taps them in part.

Mandatory military service is a special kind of tax imposed exclusively on healthy young males. It is based on putative fighting ability. It is not based on economic ability, and is in fact regressive (young males have much less wealth than older men and women). The regressivity is somewhat offset by veterans' benefits.

Egalitarian equity is also expressed in open access to public lands like streets, parks, beaches, hunting grounds, fisheries, etc. The unfortunate by-product is underprovision of these at the local level, to avoid overattracting outsiders.

4. Intergenerational equity

A. Equity for the young. The "birthright" concept is part of the organic view of the state, and is enshrined in tradition. ."... endowed by their Creator with certain unalienable rights" is one of our favorite slogans. "Unalienable" means no ancestor can have bargained them away, or lost them through conquest, or illness, or failing to get married. Your ancestor may even be an illegal alien: all you have to do is be born here.

The birthright concept is silent on the issue of when life begins. Rather it says whenever your "Right to life" does begin, in utero or ex utero, you have economic rights: public rights, that is, apart from inheriting private wealth, and often in conflict with that.

The Biblical birthright is a right to land. Every 50 years is a "Jubilee" when the game ends and a new one begins, "Ally Ally Oxen Free." The score is zip/zip and everyone has a new hand. The idea is to prevent inequalities from cumulating over generations. Moses lays it out quite clearly in Leviticus 25.

"French equity" is a species of equity-in-kind where each heir gets an equal share of the ancestral land. This is enshrined in the Code Napoleon, a code of laws which Napoleon implanted in lands other than France as well. It stands distinct from the English system of primogeniture and entail, under which the eldest boy gets it all, and cannot sell even if he would. The French system leads to division into small pieces, or morcellement. They went further and required that each heir get an equal share of the homestead-land, plowland, meadowland, pasture, and woodland. The result is called parcellement.

The American system combines the French and English. Most of us may be Anglos but it was the French, recall, who won the battle of Yorktown for us, and Jefferson was an ardent Francophile. We abolished English primogeniture and entail, and divided the land, but we divided it much less finely than the French. We let people amass as much as they pleased, but then asserted the birthright of others by subjecting the land to taxation. French equity is in-kind; American equity is in money, and achieves equity without imposing inefficiency.

In addition we gave 1/36 of all public lands to pay for starting up schools. (That's one section per township.)

Another idea of land as birthright is advanced today by conservationists and environmentalists. The idea is we must leave natural resources in good shape for future generations. Economists would amend this to allow some depletion, provided the resulting cash is used to create capital to leave future generations.

Open access to public lands, fish and game and prospecting opportunities, are also part of the land-as-birthright concept.

Maximum price controls imposed on certain land-based products and services also reflect an idea of birthright. Residential rents, and oil and gas, are two examples. Provision of public housing is another. The idea of homelessness as normal is very recent in U.S. history. (Cf. "gender equity," below.)

The right to a useful vocation used to be considered basic. In recent years we have substituted for it the right to various kinds of recreation. This right has been increasingly taken over by older folks, however, for the largest recreational subsidies go to golf courses.

B. Equity for the old. The old are exempt from the draft. Their shelter is increasingly free of property tax, and almost totally free of income tax: even realized gains are exempt up to $125,000, when they are 55 or older. They receive social security. Their golf is subsidized. Retirement homes are subsidized. They enjoy Medicare etc., and live longer than ever. They have run up huge public debts for the working generation to pay. There is no precedent for our evolving situation of elderly dependency, but the question of who shall pay, and how, will be on the front burner for a long time.

5. Ethnic and gender equity

Most ethnic groups as such receive no preferential tax treatment. Native Americans on reservations are the largest exception. Some natives have also received large land holdings, based on their ancestry. These benefits are viewed as expiating guilt for past invasions, although there is no clear relationship between present benefits and past suffering. These special benefits constitute an anomaly within the Federal system, constantly raising vexing questions of relative rights. Most Indians are very poor, but a few are extremely rich, like the Agua Caliente band of Cahuilla Indians who own and collect rents from half of Palm Springs.

Blacks' ancestors suffered the disqualifications of slavery, and later peonage and Jim Crow laws, during the period when most of the public domain was dispensed and privatized. As a result most blacks today begin life with little inherited wealth, a handicap that endures and cumulates over generations. Blacks' wage and salary incomes average somewhat lower than whites', but their holdings of real property average much lower. A U.S. Census Bureau study released January 10, 1991, reports the median wealth of black-headed households to be only 1/10 that of white-headed households.

After Emancipation the freedmen expected and sang about a "Year of Jubilee," and the "Radical Republican" bloc of reconstructionists attempted to legislate it, but it never came. Like all dispossessed people, blacks have been compensated historically by the use of property taxes to finance government, but this form of compensation has dwindled away over the years. Even before that, the well was poisoned by assessment discrimination against black owners of property. Especially after the success of Proposition 13 (1978), the tendency has been to substitute non-property taxes, most of which are fairly described as taxes on upward mobility.

Most Chicanos are in the same fix, for a different set of reasons, except that a few enjoy the inherited advantages of prior possession of land, and are extremely rich. They tend to keep a low profile. The word "Chicano" is generally reserved for Hispanic Americans without great inherited wealth. The presence of the very rich Hispanics may account for Chicanos' voting being more conservative than blacks'.

Blacks and Chicanos enjoy preferential hiring under affirmative action programs in some government employment. How effective these are is a moot question; but even if they are effective, they do nothing directly about the greater problem of unequal inherited wealth. Taxation is the only public policy bearing directly on that.

Ethnic equity is the one kind of equity where some effort is made to compensate for past wrongs, at least in theory. But the effort is very thin because property is exempt from it. Property, however acquired, enjoys greater legal safeguards than the right to work. Even these rights, however, have been partially overcome by "block-busting," and integration of public schools. The smallholders who paid most of the price for these changes were not those who could best afford it, however.

Foreign economic and military aid are deeply affected by ethnic ties of American citizens. Equity here would mean supporting my homeland as much as yours, but obviously that is not done, especially for German-Americans.

Undocumented foreign workers pay taxes in America, but generally receive less than equal protection of the laws, and less than equal benefits from government programs. It is perhaps inevitable that citizens receive preferential treatment, if citizenship is to have any meaning. While this is a matter of citizenship rather than ethnicity, it has a high ethnic content in practise. It also has a high political content, since right-wing immigrants of any ethnicity are more accepted for documentation than left-wing ones.

Laws against aliens' holding real property are common in many nations, but are mostly gone from the States. Restrictive deed covenants with ethnic discrimination are no longer enforceable in court. Aliens actually receive preferential tax treatment under various international tax treaties which exempt their capital gains from income tax. Some of these aliens, indeed, are American nationals operating from foreign tax havens.

Multinational corporations, including alien ones, generally escape paying full state income taxes, because of their special ability to transfer income to other jurisdictions with lower tax rates. They do this simply by recording imaginary prices when they transfer goods between jurisdictions.

Overassessment of real property held by poor people is common, and these poor people are often black. The apparent motives are both economic and ethnic; it is not always clear which weighs heavier. In the southeastern states until recently it was common to have segregated assessment records, for black and white property. It is widely believed that blacks were overassessed, and the existence of segregated assessment records creates a presumption of ethnic bias. In modern times, economic motives probably count for more; but either way the cost is high.

Ethnic diversity in America helps account for the reluctance of many to move to an organic concept of the state as an extended family or tribe. Homogeneous Japan, Sweden, or The Netherlands are more organic states. In heterogeneous America the contract theory of the state retains strong support, for better or worse.

As to gender equity, the traditional view is that males suffer the hazards of military duty, and if they survive they deserve a lot of breaks. It is also their moral and legal duty to support their wives and children, even after divorce. Women, especially housewives, are less mobile, and have less bargaining power in the work market, an economic force no law can overcome. These views have lost ground, but are by no means dead. Feminists would not deny there is a kind of equity in the old view; they simply prefer a different bargain.

The personal income tax favors the traditional housewife role, because the homework of housewives is not taxable. The so-called "marriage tax" is only a minor advantage that unmarried working couples may enjoy over married working couples. The primary force of personal income taxation and payroll taxation and sales taxation is to penalize working wives and posslqes.

Regardless, social forces have increased careerism among middle and upper class women (poor women always did have to work). The unintended economic consequence is a treadmill effect on housing prices. Yuppie and guppie and dink couples can bid more for housing, even as they need and use it less. This forces more wives into the work force in order to buy needed housing. But thus they just give the treadmill another turn.

Housing is the median American's best income-tax shelter, so much so that many Americans buy and keep housing more to shelter income than people. But this also induces buyers to bid up prices, so it gets harder and harder for young Americans, and others without superior credit, to get on the first rung of the housing ladder without sacrificing families. Thus the cards are stacked for ZPG (Zero Population Growth). Neo-Malthusians may applaud, this has been their goal. But massive immigration offsets it, so the net result is a displacement of old Americans by new ones from foreign lands where they are used to raising large families in close quarters.

Ethnic and gender issues are highly charged emotionally and have a great demonstrated capacity to move people to march, demonstrate, confront authorities, etc., and thus get some action. That is splendid and praiseworthy, but the same actions that attract the press and get results are also ones that substitute for and often drive out careful thought and foresight and analysis. The desired equity will be achieved at higher levels if integrated with demands for other kinds of equity of more general bearing.

6. The status quo as equity

This concept defines equity as the status quo, regardless of its origins. T.N. Carver divided sources of wealth into "earnings, findings and stealings," with only the earnings warranting full protection. The status quo position, in contrast, is that the essence of inequity is change. Taxation lowers the value of that which is taxed. Extreme status quo thinkers see such losses as takings of property in the legal sense, and demand prior compensation, just as if land were taken for a park or a right-of-way. But that would offset the revenues and defeat the purpose of taxation. Most allow some taxes are necessary, but "an old tax is a good tax" because a new tax comes as a surprise and imposes unexpected losses.

The view has no legal standing, although the courts are often regarded as defenders of the status quo, and in some ways are. The sovereign's right of taxation has little limit in legal theory. It was the voters, by passing Prop. 13, who put a cap on one form of taxation in the California Constitution.

Most of those who take the status quo view are less critical of government "giving"; and either silent on or accepting of private "findings" like the appreciation of land prices around growing cities. Usually it is the status quo of durable property like real estate that is defended; the traditional right of labor to receive untaxed wages and salaries has been abandoned over the last 45 years, without receiving much philosophical defense. The thinking seems to be that a new generation of workers does not inherit the rights of the old, but the rights of durable property endure with the property.

In modern times, de facto takings of land by means of zoning are common and accepted (although vigorously contested and often circumvented), so long as the takings are less than 100%. Status quo thinking still prevails, however, in the concept of a "grandfather clause." Any land use established before zoning is legally imposed may be continued indefinitely, so long as it is not interrupted. One must maintain a constant "history of use," or kiss grandfather goodbye.

Status quo thinking divides on the question of alienability. In View A, only the original grantee or licensee is protected, and must continue the traditional use in the traditional place. Selling a license would be censured as "trafficking," and viewed like money-changing in the Temple. Licenses to appropriate water in California are an example. Until recently, sale of a water right would violate its terms, and never happened. It still hardly happens.

Another example of View A is the provision that taxable real estate in California shall be reassessed only at time of sale. This we adopted as part of Prop. 13, 1978.

In View B, a main purpose of transferring resources to private control is to encourage market flexibility, with free and easy transfer, in order to foster allocation of resources to the most economical use: "highest and best" use is the common term. Most economists, obviously, endorse View B. Many carry it to the point of viewing alienation as strengthening property rights. Purchasers are viewed as "innocent" of flaws in title, and worthy of legal protection, not only for themselves but extending to other holders of the same class of property who are not themselves innocent purchasers.

In View C, private property is an end in itself. This is the pure equity position, requiring no functional rationale or historical justification. It is held as a religious conviction or presumption, a pure moral issue. In this it is no more arbitrary than egalitarianism. However the world's major religions are steeped with the egalitarian revelation.

Lemma I: "Benefits Received" theory of taxation. Taxes are to be paid only in return for benefits received, measurable and demonstrable. The common slogan for this, often used by Howard Jarvis, is "Property should pay only for services to property, not services to people." Jarvis construed services to property very narrowly. Others allow that many services to people are indirect services to property: e.g. good schools raise real estate values. Welfare payments, in this view, should be zero. Prisons should be supported by convict labor. Government should do nothing for those too poor to pay any taxes.

The State is here viewed not as organic, but as a contracting agency with private landholders whose standing antedates and is independent of the State itself. This is the Contract Theory of the State, as opposed to the Organic Theory which begins with observing that land titles originate with the sovereign and are held from the sovereign.

Taxes matched by equal or greater local benefits are called "beneficial," following Alfred Marshall; other taxes are called "onerous." Marshall coined these as objective terms, but they seem to reflect a point of view. Most national taxes, in this view, are onerous, and especially those used for welfare, and for what is called "horizontal fiscal balancing" (taxing rich regions to subsidize poor ones).

Lemma II: "An old tax is a good tax." The thinking is that there is a common _after_-tax rate of return to investors. They lower their bids for property subject to existing taxes, and invest less in industries or activities subject to such taxes, so that they get the same _after_-tax rate of return regardless of taxes. The saying is, they "buy clear of taxes." Thus, only surprise taxes make them pay more, and this is wrong.

This is also called the "theory of tax capitalization," which I will explain in class.

New taxes are never justified if they make anyone worse off, no matter how much good they may do for others. The thinking here is that it is wrong to compare the utility of different individuals, so we can never be sure the good we do for beneficiaries equals the harm we do the taxpayers. The only permissible new taxes and new programs are "win-win" cases, where every individual without exception receives a net gain.

Of course one might argue this backwards, we can never be sure that maintaining the _status quo_ does more good than harm, either. But in this thinking the burden of proof is always on those who would change the _status quo_; and it is virtually impossible to meet the burden.

Some carry this so far that no changes are permissible even if damaged parties are compensated according to objective appraisals of the damage. This is the way California's system of riparian water rights, for example, works (we have two overlapping systems, riparian and appropriative). Objective appraisals do not consider subjective feelings, is the reasoning.

In practise the main role for this theory is to oppose "Robin Hood" policies. It is identified with Vilfredo Pareto and James Buchanan, and is found in most economics texts under the heading of "Pareto optimality" or "Pareto efficiency" (Hyman, pp. 69-72). Logically, Buchanan et al. might well object to lowering old redistributive taxes, on the same grounds that they object to raising them, but I am not aware that they have done so.

A cynic might see this as a rationalization for concentration of wealth; a Marxist would see it as evidence that class bias dominates what passes for mainstream economic thinking. However one sees it, it is clear that a great deal of ingenuity goes into rationalizing property.

Lemma III: Older uses of land deserve protection against newer uses. This is the "grandfather clause" principle discussed above. In taxation this resolves itself into the proposition that land should be assessed on its current use, not its highest and best use. In California several land uses are assessed by use rather than market value: farmland (under the Williamson Act); forest land (TPZ Act); and golf courses.

In zoning it becomes the proposition that landholders who establish intensive uses that are later proscribed have established vested rights to continue them. In air quality management it has led to the idea of transferable "offset rights" to pollute, based on histories of past pollution. This is supported by something named the "Coase Theorem."

Lemma IV: Property rights are based on prior occupation and/or use. Priority of course establishes a status quo. Appropriative water rights in California and all western states are based on prior use. Oklahoma land titles go back to "sooners," meaning those who got there sooner. Mormon titles are based on prior settlement. "Squatter" titles were recognized throughout the west. "Adverse possession," "preemption," "residency," "beneficial use," etc. are common terms for the same idea. Throughout the Mexican cession land titles granted by the defeated power and its predecessor, which it had defeated, were validated based purely on priority.

The Indians are a special case where priority was not enough. Priority has to be coupled with sedentary culture, and general conformity with customs of the powerful state. Still, many Indians have received large landholdings based mainly on their historical priority. In Alaska, 100,000,000 acres has been allotted to the native corporations (Aleuts and Eskimos, as well as Indians proper).

A popular rationale for priority is the "lifeboat theorem" of Garrett Hardin of Sta. Barbara. It is a variation of Malthusianism. We are a lifeboat in an overpopulated, overbreeding world. We cannot save the others from drowning, they would only sink the lifeboat. It is our duty therefore to keep them out.

Lemma V: Property rights are a moral good in themselves, and require no rationale. This is discussed above.

7. Median voter theory: "public choice"

This is very much the vogue currently, and occupies Chaps. 5 & 6 of Hyman. The space it gets is out of proportion to its long-term importance, but reflects the weakness of texts to overweight current fashions.

8. Interregional equity

A. Domestic

i. Open access. Some of the most attractive features of some of the most desirable cities and regions are open to anyone: Central Park, Yosemite, California beaches, etc. Thus the benefits are not reserved to locals. The resulting overcrowding is called "the tragedy of the commons," and results in "the dissipation of rent," an economically wasteful outcome. (In crowded eastern cities, suburban beaches are reserved for city residents who are issued stickers or buttons to gain access.)

It could be worse. Studies of national parks have shown that actual usage declines with the square of travel distance from the park. (Such findings are called "gravity models," because the force of gravity similarly declines with the square of distance.) Thus the use of attractive resources is partially rationed by location, which is limited and for which one pays.

Thus open access is a workable strategy for equity, up to some point. As density increases, however, more and more open common resources have to be closed off and priced. Such "enclosures" have been going on for centuries, and as they do they seriously erode traditional equity, because some are fenced in and others fenced out. Taxation is needed to redress the balance.

ii. Indirect open access. The rents of private lands in rich cities are partially opened to general access when those lands are taxed, directly or indirectly, to provide superior public services which attract immigrants. Superior schools are an obvious example: they are even called "magnet" schools. (They used to be called "lighthouse" schools, when people were less sensitive to the magnet effect.)

Access to magnet schools is rationed indirectly by high local real estate prices: San Marino and Beverly Hills are not cheap to enter. This would be offset by immigrants living at high density in order to access the schools, but localities legislate against that by using zoning to limit density.

In California many school districts straddle city limits, and zoning is controlled by cities, not school districts. Thus Woodcrest, for example, floods the Riverside Schools but is not subject to Riverside zoning (or wasn't when first settled at high density). To the extent that immigrants do succeed in accessing the magnet schools without sharing fully in the cost, the national result is a geographic maldistribution of population. The local result is a reduced incentive to support superior schools. On the whole, therefore, this approach to equity has limited general merit. It does appear equitable to landholders and developers just outside the reach of city zoning, but inside school districts that tap city tax bases.

To restore equity without biasing locational choices, school financing is being transferred to higher levels of government.

iii. Regional cross-subsidy. This is a variation of "French equity" (equity-in-kind) which says that every settler, wherever he chooses to locate, deserves access to basic utilities on the same terms as those who are cheap and easy to serve. These basic utilities include transportation, postal service, deliveries, water, gas, electric power, telephone, police, fire protection, schools and busing, ambulance, hospitals, air quality protection, waste disposal and pickup, storm sewers, sanitary sewers, flood control, underground water protection, radio-TV-cable access, visiting nurse service, flat-rate service calls, mosquito abatement ... It's a long list, and grows as the number of services grows that are considered "basic."

"Regional equity-in-kind" also says everyone should pay the same insurance rates, regardless of hazards peculiar to his neighborhood; and borrow money on the same terms (no redlining), regardless of higher risks indigenous to his neighborhood. The last two are symbolic issues with more smoke than fire, and may obscure the major thrust of regional cross-subsidy in practice. The major thrust is to tap the rents of central cities to subsidize suburban and semi-rural growth.

This in turn raises peripheral rents. Indeed, it creates rents where there would otherwise be none at all. Overall it consumes more rent than it creates, and causes a net social loss. But in the process it raises gross activity in the affected region, and looks like a winner when one measures welfare in terms of gross regional product, rather than net. Many powerful groups do so. There is a huge market for economists who use "economic base multipliers" and "input-output analysis" techniques to forecast the gross regional product to be expected from various policies or causes, and help local booster groups plan how to maximize gross regional products. There is ongoing conflict, which you can hardly have missed, between groups for and against "growth." Many of the issues hinge on how you define growth.

iv. Subventions. A subvention is a subsidy from a higher to a lower level of government. These have become common (Hyman, Chap. 20). An equity concept has developed called "horizontal fiscal balancing," which means poor regions should get more than rich ones. Canada has carried this much farther than we have, such that some half the budgets of the poor "Maritime Provinces" of New Brunswick and Prince Edward Island come from Ottawa (I'm assuming, I hope correctly, you know Ottawa is the Capital of Canada; and also you understand Ottawa produces nothing itself, but transfers money from other parts of Canada).

Interregional equity in practice has little to do with interpersonal equity. A skeptic has defined it as a means of transferring wealth from poor people in rich regions to rich people in poor regions. New Brunswick is a good case: much of it is owned by a person listed among the 10 richest in the world. Poor West Virginia is another good case: almost all its rich coal reserves are held by Wall Street corporations. Interregional equity boils down to horse trading among Congressmen seeking "a fair shake for Boondock County."

v. Frontiers. There is a strong tradition of subsidizing frontiers, to nail down the territory for imperialistic reasons.

vi. Backwaters. There is another tradition of subsidizing declining regions, to preserve the status quo. Congress calls it "Area Redevelopment." Britain has carried it to absurd extremes, at high cost.

B. International.

i. Common heritage. The "high seas" are traditionally open to ships of all nations. The Law of the Sea is a subject in itself with many groups, especially the small inland nations, pushing for the ocean beds and other no-man's-lands to be declared in the U.N. to be a "common heritage" of all mankind. There is a great deal of constructive international cooperation in exploring remote areas. Traditional military and banking and private development interests view this with great skepticism and continue to project power and financial and tenure control in the old ways. The outcome is up for grabs; it is as exciting and unstructured an area as a person could get into.

The invisible resources of radio spectrum and airlane overflight rights also require international agreements. Their market value may exceed that of the more obvious resources.

ii. Duty to LDCs. LDC spokesmen encourage the idea that wealthier nations like the U.S.A. owe poorer nations aid. Sometimes this is because LDCs have lower incomes: that is an international application of (2), Egalitarian Equity. Sometimes it is because poorer nations have less land and worse land and resources per capita: this is (1), functional equity, viewed internationally.

The case is often quite weak. A nation like Guatemala, where 2% of the people hold most of the land, and foreign aid goes mostly to the same 2%, can hardly preach egalitarianism except to the very ignorant and gullible. A nation like Argentina, with an abundance of very rich land, can hardly preach equal rights to land.

In practise, therefore, the U.S. Government uses foreign aid for military-strategic reasons, appearing to go along with equity arguments as window-dressing. A common form of foreign aid is through bank loans which are defaulted, and the banks then bailed out by the hapless U.S. taxpayers. Perhaps we deserve it for going along with the charade; but the self-righteousness of overly dependent LDC spokespersons is unlimited, and quite amazing to hear.

iii. Islamic solidarity, etc. Some nations share common bonds of religion, ethnicity, language and traditions, and support each other. Egypt thus has some claim on Saudi oil revenues, for example. More than brotherhood is involved: a thinly peopled, fabulously wealthy nation like Saudi Arabia needs the Egyptian military manpower for security. But too much cynicism is as unrealistic as too little. Islam does preach sharing and mutual aid, and there is some history of it.

"Christendom," likewise, has at times been a viable concept for international sharing and mutual aid against the infidel: Moors, Saracens, Turks, Mongols, and assorted heathen. A Christian Filipino may be quicker to shoot a Moro Filipino than a Christian Caucasian. Judaism, too, has been a strong bond of mutual support.

The most common kind of international support is military. The U.S. has drained its resources for 40 years policing the world while its proteges saved and prospered under our umbrella. It's an interesting combination of charity and domination and cultural superiority and Crusading that seems to satisfy some yearning, or combination of yearnings that makes a viable political symbiosis, at least until the bills come due.

The long-term economic results are very costly, and ultimately unbearable. Many European nations have impoverished themselves sustaining empires which they finally abandoned: Portugal, Holland, Germany, Denmark, Sweden, Austria, France, Turkey, Poland, Lithuania, Spain and England make quite a list. Don't be surprised if we are next.

9. Pressure group equity

Washington and the state capitols are thick with lobbyists each pleading for his special interest. Each has his coalition of supporters, and coalitions trade votes. "A fair shake for the cattleman" carries more weight than "a fair shake for the 373rd district," if the cattleman's association has helped enough congressmen into office. The results are on every hand, and generally at odds with most other concepts of equity.

10. Consumerism as equity

Here the idea is to fight monopoly pricing, low quality, misrepresentation, concealment of dangers, adulteration, toxic residues, pollution, and a host of ancillary abuses. Consumerist causes run from informational (Consumer Reports) to paternalistic (mandatory buzzers for seatbelts). They include the consumer cooperative movement, which has had a few solid but limited successes, and is not too proud to enjoy and defend substantial tax privileges. Ralph Nader is the modern embodiment of the movement. Like earlier consumerists he allies with other kinds of reformers and branches out into other causes, including tax reform.

Public interest law seeks to serve consumers of legal service who are not able to pay market rates, and thus are often denied equal justice under law. The public health movement does the same for consumers of medical services, and also addresses health as a public good, which the market fails to. Billions of public dollars are now directed to this end.

Keynesian (demand-side) economics made consumption a macro-economic virtue, rather than profligacy, and dovetailed nicely with consumerism. Consumerists decry sales taxes (although these actually had their fastest growth during the Keynesian era). Consumerists generally favor raising wages in preference to interest, rent or profit, not so much on functional equity grounds as demand-side grounds: most wages are spent on consumption, much property income is saved.

Consumerism tracks with free market equity in opposing price floors, either private or governmental; but would tolerate or support price ceilings and rent controls. The consistent thread is supporting buyers over sellers. Part of the thought is that buyers are generally poorer than sellers, and less organized, and deserve a break through application of "countervailing power," which is seen as benign.

Consumerists are somewhat left of center and seldom if ever would support employers in beating down wages. But they are not very far left, and generally express middle-class views and interests. Their equity views overlap with many others, but have a distinctive Gestalt all their own.

11. Middle class populism

This is another distinctive Gestalt which is at once radical and conservative in defense of the perceived interests of small businessmen, farmers and homeowners. The farm movement is representative. "Farm folks are good folks" means what's good for farming is good for America, and farming means the kind of business I and my neighbors are in. The group is at once large enough to feel like a folk movement representing all Americans; and small enough to be exclusive in fact. It takes a little double-think, perhaps, but it works.

These populists are anti-monopoly, anti-banker, and anti-government in spirit, even though they often lobby through expensive government programs for themselves. They agitate to protect their property against monopoly on the right, and on the left against taxes, union labor and perhaps foreign competition. They are perhaps most susceptible to extreme swings from far left to far right, depending on their current prosperity.

Here, equity is identified with sustaining a perceived good society that upholds old folk virtues and verities: hearth and home, church, family business, small towns, conventional morality, prudence, common sense, saving, stability, dependability, personal honesty, etc. It's a little hard to pin down, but distinctive and recognizable.

12. Merit as equity.

This modifies (4), the birthright concept, by reserving the birthright to those who show merit; or meting rewards to degrees of merit. As UC students you understand how this works: your social dividend is not paid in cash but in class, and "you get out of it what you put into it." The grantee has to "learn to labor and to wait," as Longfellow put it. It also helps to be smart. The combination places you among "the elect," which used to mean you had been chosen for Heaven, but now means the world is your oyster.

Although we call this "Calvinism," and "the Protestant ethic," Catholic France called it "la carriere ouverte aux talents." It is carried much further in Japan than any Christian or Jewish nation. With the displacement of religion by science, the doctrine of the elect was reincarnated as social Darwinism, which has the elitism of Calvinism without the balancing sense of social responsibility or noblesse oblige.

After school, loans are preferred over grants because repaying a loan gives evidence of merit.

Competition, both in and after school, is seen as character development as well as revelation of the merit placing one among the elite or elect. Winners are expected not mainly to savor the fruits of victory, but to "serve": noblesse oblige. "From those to whom much is given, much is expected" said Catholic Jack Kennedy, graduate of Calvinist Harvard.

Somewhat related to this is the notion of giving special aid to "the cutting edge" of outstanding contributors to welfare.

Nobel Prizes are an extreme case. More generally subsidies to explorers, pioneers, researchers, inventors, composers, artists, writers, and other innovators reflect this ethic.

The hidden agenda in all this is the opportunity for those in charge of rewarding merit to control the recipients by defining merit in ways pleasing or advantageous to themselves.

13. Environmental equity.

Here, equity is seen as preservation of desired natural conditions. It has a lot in common with (6), status quo equity. An early application was the riparian doctrine of water rights, under which downstream riparian (riverbank) landholders have an absolute right to natural flows' continuing to reach their shores, "undiminished and unpolluted." An analogous doctrine, prevailing in England, is the doctrine of "ancient lights," which prevents anyone obstructing his neighbor's view.

The modern movement, although accused of elitism, puts more emphasis on common rights against individuals, rather than individuals against the commonalty. Everyone is seen as having rights to clean air and water and protection from toxins. The gene pool is seen as a common heritage which no one has a right either to extinguish or monopolize. The ozone layer belongs to everyone, as do great natural wonders like Grand Canyon down to small ones like the Stephens Kangaroo Rat and Snail Darter and Least Vireo. Groups like The Sierra Club have established their right to what lawyers call "standing," that is the right to sue in court on behalf of common rights. Before then, only landholders had standing to sue to protect their individual rights or privileges.

The question of original entitlement is important in determining values, contrary to the Coase Theorem. The Coase Theorem requires that your Willingness to Pay (WTP) someone else for environmental quality (assuming someone else owns it initially) is not much less than Willingness to Accept (WTA) money to give up an environmental easement or other claim on land (assuming you own it initially). The value of our National Parks is not what we would pay to acquire them, but what we would have to be paid to give them up, a much higher figure.

How much higher WTA may be than WTP may be felt keenly by putting one's self in the mocassins of Indians with Treaty Rights, say, to fish in certain ancestral waters with religious value. It may be that Chicago economists of the Coase School, with their distinctive beliefs and conditioning, would actually behave as the theory requires; it is certain that most other people do not.

Most environmentalists are Malthusians and ZPG or NPG believers. Most are critical, and rightly so, of mainstream economic thinking which is uninformed by any understanding of the limits of the Earth, which neglects and undervalues ecology and environment and conservation, and whose goal of ever-growing material consumption to them seems gross and shortsighted on a small planet.

Otherwise they are heterogeneous and range all over what pre-ecological thinkers would call the ideological spectrum. Some are anti-immigrationists and lifeboat theorists; others are one-worlders who see the whole earth linked through ecology. Some would reserve the wilderness for the few who are sensitive and educated enough to enjoy and respect it properly -- these are the ones who get labelled "elitist" -- others are intensely democratic and see themselves protecting everyone's common heritage, and public health.

14. Equity in kind

We have looked at one sort of Equity in Kind under heading of (8), Interregional Equity, (A), Domestic, (iii), Regional Cross-subsidy.

During wartime, if the war is severe, every able male is expected to serve, with money not taken in lieu of the warm body. And every consumer is rationed: put your money away until after the war, or buy war bonds. The market is simply dumped and the nation switches to a command economy. That was World War II. Resulting inefficiencies are accepted in the name of equity: when boys are drafted to kill and die, the good life at home does not sit well, as we saw during the Vietnam undeclared war. Equity will rear its head and must be served.

15. "Aesopian" Equity

I had to coin this name from Aesop's Fable of The Grasshopper and the Ant, for lack of a folk name. Folklore is generally unkind to the saver, and economists who have tried to explain interest as a "reward for abstinence" have been silenced by intimidating ridicule. (Yes, economists who pride themselves on being "scientific" are not above settling issues by braying and trashing.) Folklore is hard on the miser, the skinflint, the tightwad, Midas, Scrooge, Shylock, et al.

Yet capital is productive, and is only created by those who consume less than their incomes, and only maintained by those who consume no more than their incomes. (1), Functional Equity, calls for a reward to savers in order to get capital created and conserved. Marxist and again Keynesian thinking has said people save even at zero interest, but these positions are easily refuted and there is a functional case for interest. But what about equity?

Folklore notwithstanding, capitalists are doing very well in fact. The most powerful dynamic of our times is to rehabilitate saving as a virtue. In Washington this means that tax changes are being pushed to shift taxes off property income and onto consumption; also onto wages and salaries. Corrupt and improvident savings institutions will be bailed out by general taxpayers, at very high cost, to avoid losses to depositors. The people engineering these changes are not just greedy, they generally believe it is equitable to reward those who accumulate capital, the "ants" of Aesop.

They have the power. All they are lacking is a coherent, articulated philosophy of equity. "A fair shake for the ants" is not very salable. "Justice for bankers" would not get far.

Early economists, following John Locke, solved this problem by saying capital is produced by labor, and the right to own capital follows from the right of the laborer to his product. The trouble with that is, capital is not owned by the labor that produces it. Labor as such gets paid and consumes as much as it creates. Capital is created by saving. Rewarding saving is justifiable, too, when money is saved from earned income. However, people save from findings and stealings as well as from earnings. A major source of capital financing the English industrial revolution of the 18th century was gained in the slave trade and accumulated in Liverpool, along with money gained from land speculation and seizure. So long, therefore, as findings and especially stealings are allowed as private income, title to capital is somewhat clouded.

Defenders of property generally duck that problem. Indeed the tendency is to use the virtue of saving as an indirect way to defend findings and stealings, on the functional grounds that rents and unearned increments are likely to be saved (which is probably not true, but is widely believed). This is probably why there is no coherent, popular philosophy defending interest and returns to capital generally as forms of earned income.

What is needed is a philosophy of equity that clearly distinguishes capital formation from acquisition of existing assets; and returns to capital, the product of saving, from returns to land which was here before we got here, and will be here after we go.

16. Anti-commercial equity

There is some feeling that slow gains are more legitimate than fast ones. This shows up in tax provisions that defer taxes until gains are realized by sale for cash; and require long holding periods to qualify for lower tax rates.

This is generally a throwback to values of a pre-commercial society and is in strong conflict with (1), functional equity, especially the concept of "Haig-Simons" income described there.

17. Contractual equity

Here equity is viewed as honoring contracts and paying debts, as matters of personal honor and responsibility. Within reasonable limits such equity is basic to any workable society, but there are gray areas where it gets interesting. Bankruptcy is one, generally regarded as a preferable alternative to debt-slavery or peonage, common in the southeastern states after the Civil War, and still common in some countries. The idea of bankruptcy as escape from bondage goes back at least to Moses (Leviticus 25 and 26) and is not an irreligious notion.

There is a conflict with the birthright concept (4) when people come into the world liable for debts contracted by others. Private debts in excess of assets are generally extinguished at death, but public debts are something else. Debts of many LDCs were contracted by corrupt officials who made off with the proceeds for high living in Miami, leaving the debts to others. Loan officers often got cut in on the deals. How liable are the poor peasants who stayed behind to pay these debts? How liable are you, as a future U.S. taxpayer, to bail out the banks? How liable are the depositors? Someone is going to pay, and your generation will get to make a lot of those choices.

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Seventeen ideas of justice in distribution is a lot. But that's the way it is: I hope you will have learned at least there is no one simple idea of equity in the world.

But don't go away confused. Fortunately there is a lot of overlap, and you can piece together your own combination which incorporates a good deal of many ideas of equity. I hope you make the same choices I do, but you probably won't, and that is your right. Just look for internal consistency in your choices. Some fences are too high to straddle and you'll just make yourself vulnerable from both sides, not to mention the fence.

As we move on through the nuts and bolts of public finance you'll find judgments constantly being made in terms of someone's idea of what is fair, just and equitable. You should now have a better feel for various prevailing concepts, and a better basis for framing your own without having to reinvent the wheel. But if you can come up with a better idea, go for it.