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America’s Constitution of Unhappiness
By Fred Harrison

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12.1 Beyond the Land of the Free

THE dream lives on to this day as folklore. America is the land of the free. It was, once, for those who sought refuge from the aristocracies of Europe which had dispossessed them. The New World was a continental-wide bolthole to freedom. But once the land was liberated from its original occupants, staked out and the title deeds were assigned, something eerie happened. When the land ran out in the 1890s, the land of plenty turned into a hell of poverty.

Today, across the land, we find a depth of human tragedy not to be found in the worst of inner city slums in Europe. Even as the empire waves the flag of democracy under the noses of the populations of other cultures, the internal colonisation of the citizens of America proceeds unabated.

That is not how Americans interpret the crises that afflict their communities. Real estate is revered rather than held culpable as the root cause of their problems. But how, then, can they account for the fissures that split this metropolitan civilisation? Given the sacred character ascribed to the laws of their land, the fault had to be displaced onto the psychology of the individual. Racism was, and necessarily remains, a favourite explanation, and the statistics lend credence to this interpretation. A *New York Times* analysis highlighted the evidence that exposes the marginalisation of Afro-Americans.

- The proportion of black men (aged 22-30) without jobs had climbed relentlessly. In 2000, 65% of black male high school dropouts in their 20s were jobless unable to find work, not seeking it or incarcerated. By 2004, the share had grown to 72% compared with 34% of white and 19% of Hispanic dropouts.

- In 1995, 16% of black men in their 20s who did not attend college were in prison; by 2004, 21% were incarcerated. By their mid-30s, 6 in 10 black men who had dropped out of school had spent time in prison.[i]

Was America reviving racial segregation in schools? That was the view of one commentator.[ii] Fears of racism are understandable in states located at the US margins – like Louisiana and Mississippi – but do those fears distract people from the causal roots that nourish discrimination? They do, in the view of a social activist who combined academic economics with concern for people addicted to narcotics – and who is also a landlord. Dr Polly Cleveland was a close observer of the real estate market from the inside, as co-owner two rental apartment buildings in New York. In her view, the problem of deprivation is more complex than the psychology of whites *versus* blacks.

> Increasing racism? Or maybe a consequence of growing inequality of wealth and income *driven by a system of taxes, subsidies and regulation that directs resources to the top*? The system varies from state to state; it's no coincidence that the black poverty trap of New Orleans lies in Louisiana, which vies with Mississippi for most unequal state.
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> *Growing inequality drives growing housing segregation by wealth and class, followed by growing psychological segregation*. It reduces empathy between classes. It makes it easier for officials to withdraw services from poorer neighbourhoods, and easier for employers to hire their own kind. It leaves the cities' young black men isolated and bitter. To fight racism, we must also challenge the rigged system that has now pushed wealth inequality back up to levels last seen in 1929.[iii]

The poverty-stricken condition of some southern states is in part self-inflicted. Tax laws that impoverish, driving people into the zone below the economic margin, are wilfully adopted by local and state governments. That proposition was tested by economist Mason Gaffney and former newspaper proprietor Richard Noyes. Louisiana, for example, featured near the bottom of all US states in terms of *per capita* income. A people-friendly regime of state and local taxes would raise revenue from the property tax, preferably by exempting buildings and directing the charges at land. Louisiana was sixth from the bottom in the league that ranked states by the ratio of property tax to all taxes.[iv] In other words, its revenue-raising policies were *designed* to impoverish its people. Low productivity employees are penalised for working while the owners of land are rewarded for accumulating assets whose value increases in line with taxpayers' investment in infrastructure.

This vicious funding-and-finance cycle drives the wedge ever deeper between those who rent their homes and those who own them. The impact as transmitted through the housing market was analysed by two economists at the Federal Reserve Bank of Philadelphia. They wanted to know how welfare would be affected as a result of a 10% increase in the price of houses. Families that rent their homes suffered a 4% drop in welfare, compared with a 5% increase for owners who had paid off their mortgages (see Graph 12:1).

As employees' wages were taxed and invested in highways and other public amenities, the financial status of renters deteriorated while the asset-rich became increasingly prosperous. For the owners of real estate enjoyed two streams of income: the money they earned if they worked, and the money they could borrow from banks when they offered their houses as collateral. The re-financing of homes was a buoyant source of tax-free revenue. Over the life of the mortgage, about 45% of households re-financed their properties.[v]

Two graphs have been deleted here to shrink the size of the file.

Source: Wenli Li and Rui Yao, *Your House Just Doubled in Value?* Federal Reserve Bank of Philadelphia *Business Review* Q1 (2006).

Home owners increase their consumption by monetising their windfall gains. They can live beyond their means. How much more they can consume depends on where they happen to be on the family life-cycle and the size of their mortgages. Graph 12:2 exposes the void between the renting community and property owners. The additional consumption by young owners is about 5 to 6 cents for every additional dollar in the price of their homes. This jumps to 8 cents for elderly owners. Similar effects have been identified for the UK, where the effect (11 cents) is largest for old homeowners, with zero effect for renters.[vi]

As the value of residential assets increases over time, a contrary trend is observed among renting families. Campbell and Cocco, referring to the UK, found that "Over the life-cycle, individuals who remain as renters typically have stagnating or declining incomes, while individuals with rising incomes tend to become homeowners".[vii] If public policy was not heavily to blame for the plight of renting families, we might accept a crude Darwinian interpretation of the differences of lifestyles. In fact, renters spend their lives locked in that unidentified battle with the state and its tax-take.

Thus is discrimination at its most elemental level built into the treatment of citizens. But unlike the racial segregation laws that disgraced the Deep South up to the time when they were outlawed in the 1960s, the discrimination sponsored by the Tax State's economics of real estate is not decoded for the public. An economic class structure divides the people, and yet they unite in celebrating the laws that segregate them. The facts are laid out in the official statistics, and yet no-one interprets them in terms that can lead to calls for a renewal of the campaign for civil liberties.

Social scientists tend to avoid questioning the fundamental principles on which the US constitution is based, but nature is brutal in its indifference to doctrinal sensibilities. Nothing was going to stop Hurricane Katrina from exposing the underbelly of American society.

12.2 Where's the Levy on the Levee?

NEW ORLEANS, one of the jewels in America's urban civilisation, was not a sustainable city. This thought troubled Mason Gaffney as his jetliner cruised over Louisiana one day in 1965. The city built below sea level was vulnerable, but not because of the thermal threats that lurked menacingly out in the Gulf of Mexico. Nor was the city's fate a matter of technology. Concrete walls shored up the sides of the levees that drained the land on which the city was built, but more sophisticated technologies were available for purchase elsewhere in the world. The litmus test for sustainability lay with the way New Orleans and the state and federal governments raised revenue to fund infrastructure.

Gaffney, at the time a professor of economics at the University of Wisconsin, was responding to an invitation from a civic group to advise them on urban economics. He would lay the truth on the line. To secure their lovely city's future, so that Mardi Gras and all that jazz would continue to lure the tourists, New Orleans would need to reshape the property tax. Gaffney mailed ahead of him the literature which he had published in the academic journals, and in the cordial precincts of a downtown hotel he explained how the city could fund the reinforcement of the levees. People who occupied the land should be charged rent for the benefits they enjoyed; with compensating reductions in the taxes levied on their earnings. By this means, the levees would be self-funding, and there would be no state-sponsored obstacles to the employment of the population, white or black.

By locking out the water, the land acquired immense value. The city stood at a confluence of world trade and, combined with the cultural diversity of its population, it was a highlight of the tourist circuit. The more valuable the land, the more money there would be to upgrade the levees in line with the technologies which, in Europe, had kept the North Sea from breaching London's defences, prevented the inundation of Holland and had bought a new lease of life to Venice.

The civic leaders listened to Gaffney with respect, entertained him royally at the home of one of their bankers – and despatched him on his way with no intention of taking his advice. Forty years later, Gaffney watched the result on his TV.

Katrina landed on the levees on August 29, 2005. By the time the hurricane had moved on, more than 1,300 people were dead. Bodies floated in the streets, homes levelled by the onrush of water from the Gulf as the concrete defences buckled and exposed to the rest of the world the real story behind the tax system: a shocking depth of poverty.

The President was in his bunker on his ranch in Texas. By satellite TV, George W. Bush had been warned that the levees might not stand up to the pressure. They didn't. As the residential areas were flooded, the people of the ghetto – the residents who could not afford to flee - paid the price. Poverty immobilised them in one of the transport hubs of the richest nation on earth.

It need not have happened. But someone would have had to pay if the levees were to be upgraded. True, the defences would have paid for themselves: barriers that excluded the Gulf raised the rents people are willing to pay to live in New Orleans. But America believed in privatising those rents and taxing people into poverty. So there was no impregnable wall between the people and Katrina.

But after the deluge, what then? Here was the chance of a fresh start. Surely, now, the political leaders – from the Mayor all the way up to the President – would champion the core principles of a sustainable community? Here was the opportunity for democratic governance and the social sciences to prove themselves. Would the correct tools be used to re-create a balanced city? The US Government had access to the wisdom of the best brains, and they do not come sharper than Thomas Schelling's. His concern for the welfare of America is indicated by the terms of his professorship at the University of Maryland: foreign affairs, national security, nuclear strategy and arms control. In 2005 he was awarded the Nobel Prize for Economics, "having enhanced our understanding of conflict and cooperation through game-theory analysis".

Schelling's understanding of the rules of the game has helped to shape public policy since 1945. So when reporter Peter Gosellin from the *Los Angeles Times* asked him how New Orleans could be rebuilt, his words would resonate in Washington, DC. He is quoted as stating:

> There is no market solution to New Orleans. It is essentially a problem of coordinating expectations…But achieving this coordination in the circumstances of New Orleans seems

> impossible…There are classes of problems that free markets simply do not deal with well. If ever there was an example, the rebuilding of New Orleans is it.[viii]

Mason Gaffney, at home in the midst of a hilltop avocado orchard overlooking Riverside, read that diagnosis with horror. Now a professor at the University of California, he recalled his clash of words with Schelling in 1969. It happened at a seminar at the Brookings Institution in Washington. Gaffney was a research associate at Resources for the Future, a think-tank whose offices were in the same building as Brookings. He had been invited to present his analysis of the relationship between taxation, the land market and public policy. Schelling objected to his critique. Gaffney had stressed that the property market operated most effectively when the public's services were defrayed out of the rent of land. The switch to that policy, Schelling warned, would *break the social contract, destabilize people's expectations and shatter the confidence of investors*.[ix]

Katrina – not Gaffney's tax agenda - had shattered New Orleans. Might it have been a different story if that city had adopted Gaffney's funding strategy 40 years earlier?

But Schelling was not just hostile to the tax plan that would reduce the silent civil conflict that was continuously rupturing the fabric of people's lives – a conflict resolving strategy absent from his influential *The Strategy of Conflict* (1960) and *Arms and Influence* (1966); he was also selling short the ability of the free market to work with the grain of people's needs in the rebuilding of New Orleans.

The burden of Gaffney's presentation to some of the leading social scientists in America was that the market *did* enable people to provide for their needs, *if* the tax obstacles were removed. The land market, for example, responds to all the influences that constitute an urban environment, including investment in a flood-control facility like the New Orleans levees.[x] Without this reform, warned Gaffney, the economy, urban communities and the environment are all seriously compromised.

Gaffney's diagnosis went to the heart of the US Constitution. He warned that the tax authorities might be flouting the constitution. The 16th Amendment authorised taxation of "income from whatever source derived", but the tax rules provided owners with covert loopholes through which to exempt their rents. One of the most lucrative loopholes was the way land could be manipulated for depreciation purposes – as if it were a building that rotted with age. That trick was repeated time and again, for the same plot of land.

Gaffney was emphatic: "Nothing less than a thoroughgoing shake-up of the tax treatment of land income will avail. And this is exactly the time when such a project, hitherto a pipe dream, may be seriously entertained".[xi] The consequences of not having this policy in place could be observed in everyone's neighbourhood. For when rent was privatised, people who obstructed the market were rewarded.

> [T]he income imputable to land is largely exempt from income taxes. This helps explain why landowners in high [tax] brackets hold out for higher prices than can be met by low-income workers whose wages are fully taxable. It helps explain the paradox of high and rising land prices in the face of a vast surplus of vacant and under-utilized land, and the twin paradox that islands of hyper-intensive, high-density land use, appropriate to high land values, arise in oceans of empty space with which they have little complementary linkage. It helps explain why the land market is not nearly as responsive to consumer demands as a market has to be to be functional in a complex modern economy.[xii]

Schelling was not convinced. By his negative response to the plan he implicitly contributed to the perpetuation of the culture of inefficiency and injustice. Would this happen if scholars had to audit their doctrines, to inform the people of the wealth, welfare – and quality-of-life options – which they *could* enjoy if they adopted optimum policies such as the one advocated by Gaffney?

An estimate of the scale of the potential gains has now been calculated by Nicolaus Tideman. He began his teaching career at Harvard, served as a Senior Staff Economist at the President's Council of Economic Advisors in Washington, DC, and became Professor of Economics at Virginia Polytechnic Institute and State University. If the US government was sufficiently concerned about the well-being of its citizens to optimize the public's revenue raising policies, average earnings per worker after taxes would have been about $4,000 higher in 2005. Within 10 years, after-tax earnings per worker would be higher by an average of $7,000. And by consistently applying public charges to the rent of land, by 2025 - in an open economy, trading with China without fear - American workers would be earning an additional $10,000 per year after taxes, compared with their prospects under the current tax regime.[xiii]

We can infer what a difference this would make to the people of New Orleans. By swapping the constraint-on-trade doctrine for the freedom-to-produce philosophy, they could rely on their personal and community initiatives to rebuild their city, working in partnership with government and its agencies. If Katrina left the land worthless on the day she struck, that value would be restored on the day that people cleared the derelict buildings and began to reconstruct their homes.

After Katrina, all that the survivors needed was a plan that created the right combination of incentives to undertake the renewal work. The primary innovation was a land levy for the levee. The government's unique function is to provide the legal framework for ensuring that the value added to the land was recycled back into the public's services rather than allowed to leak through the colander of the current tax regime. People would hand over those land-rents if they knew that this was the best defence against Katrina's sister, who is waiting in the Gulf ready to strike. The Mayor of New Orleans could offer his citizens the off-the-peg plan for a sustainable city by drawing on the scholarly papers available on www.masongaffney.org.

Box 12:1 The State as Enemy of the People

WHEN its revenue is at risk, the state becomes an instrument of tyranny. That contention is consistent with the evidence that was documented in US Congressional Hearings chaired by William V. Roth, Jr.

The taxmen of the Internal Revenue Service (IRS) were rewarded with cash for their assault on the innocent and "to feed the insatiable demands of Washington for revenue and more efficiency". People were driven to commit suicide to escape the abuse of state power. With an 83% compliance rate in the payment of taxes - the lowest in recent history – emergency measures were taken against dodgers. Fear was used as a tool by the IRS, for "Fear leads to submission. Frightened Americans will more readily pay their taxes".

The Roth hearings showed that the "bribery, embezzlement, influence peddling, and rampant conflict of interest" which had been documented by Congress in the 1950s had continued unrestrained by the rule of law up to the end of the century. The lack of accountability within the IRS "facilitated the abuse of power and denial of due process for taxpayers".

> Many innocent taxpayers, denied due process and living lives on the edge of financial ruin, were forced and even bullied into paying more taxes than they owed, and the perpetrators of this abuse were being promoted, given cash awards, and allowed to carry on within a federal agency that is shrouded in more secrecy than the CIA.[2]

Errors were concealed through the use of intimidation that would have earned the admiration of Don Corleone. Senator Roth documented abuses such as "wrongful enforcement procedures, unaccountable managers with near-absolute power to ravage employees, an informal policy of *omerta* that results in threats and retaliation against those courageous enough to come forward".[3]

William V. Roth Jr. & William H. Nixon, *The Power to Destroy*, New York: Atlantic Monthly Press, 1999, p.120.
[2] *Ibid.*, p.9. [3] *Ibid.*, p.120

But that is not what happened. The speculators moved into New Orleans as the water was driven back. Taxpayers would fund the renewal of the levees and raise the value of adjacent sites, a process described by Gaffney for the benefit of his Washington audience:

"The extraordinarily favourable tax treatment encourages speculators to buy and hold land, and retards their releasing it to developers and builders, whose income is fully taxable at ordinary rates".[xiv] After Katrina, the biggest losers in New Orleans would be victimised a second time: excluded from their homes by the land speculators.

There are worse things than the wrath of nature. Katrina was unforgiving, but the state's abuse of power is unforgivable. Evidence of how it manipulates taxation to terrorise people was documented in the US Senate by William V. Roth, Jr., a Republican who represented Delaware and who, at the time, was chairman of the Senate Finance Committee (see Box 12:1). Here, in black and white, was an account of the perpetual civil war waged by the state against citizens. Witnesses testified to the abuse of power which challenged the official doctrines on which the Anglo-American model of society rested.

12.3 The Anglo-American Model Challenged

TERRORISTS like Osama Bin Laden cast their critiques of the West in terms of strident cultural preferences and the blasphemous invocation of God to justify mass murder. The Anglo-American response was advocacy of the formal trappings of democracy. There was no meeting of minds in this Clash of Cultures, so the mutual hostility of the fundamentalisms trapped the innocents in a process of violence.

The challenge to the Anglo-American model, however, is not confined to Muslim extremists. Within the West, the nations of the Enlightenment disagree over the direction that social evolution should take. This is an impasse that cannot be tolerated indefinitely, now, thanks to the intervention of China and India in the global market. For without a rescue plan, the cumulative weight of deprivation among the peoples on the peripheries of the West will drag everyone else down with them. Europe and North America have two choices. They either support the marginal regions with policies that would enable them to fund their way into the future out of the rents which they generate. Or they cut adrift the peripheral regions, which in Europe includes vast areas along the Mediterranean coastline, so that the core cities, those with the highest productivity, can operate as adjuncts to the new centre of industrial gravity in the East.

Few people would choose the second option. And yet, the first choice brings with it the anxieties associated with change. But the history of Europe and America over the past 500 years has been a continuous medley of social experiments. The great reforms included radical changes to perceptions of moral standards and the way in which these required amendments to property rights. Americans would empathise with such an agenda, for they celebrate the association of their civil war with the notion of "the land of the free" for African and well as European Americans (see Box 12.2).

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In the labour market, the abo ion of taxes that destroyed jobs would transform life at the margin and consolidate the valu of the New World, based on the independence of the individual in the face of the adve ties of nature. We can test this claim by comparing resource-poor countries – those that are traditionally assumed to be marginal locations - with resource-rich territories. Intuitively, we would expect resource-rich populations to enjoy higher standards of living. That deduction does not follow from the facts, and the reason is of profound significance.

Table 12.1
GDP *per capita* (2004)

	GDP/*per capita*: $	Government Consumption of GDP: %
Norway	39,259	22
Japan	39,941	17.6
UK	26,391	21.3
USA	36,067	15.4

Source: Marc A. Miles, Kim R. Holmes and Mary Anastasia O'Grady, *2006 Index of Economic Freedom*, Washington DC: The Heritage Foundation, 2006.

In the 19th century, during the transition to urban commercial society, the peoples of Norway and Japan managed to retain their rural land rights. This exercised a major influence over the way their societies evolved during the industrialisation of the 20th century. The cultural differences between them were considerable, but they had one thing in common. Their home territories were very poor in the natural resources that were readily available in the UK and USA. But Norway and Japan preserved traditional values based on the ethics of social solidarity. So although they did not possess precious metals and fertile plains, the economic independence enjoyed by people on their family farms and small coastal and rural businesses enabled them to develop a quality of life that came to exceed those in Britain and

America. The data on GDP *per capita* (an admittedly insufficient representation of a society's welfare) are shown in Table 12.1.

This comparison alerts us to the reality that the suffering caused by the dispossession of birthrights in land was not a pre-condition for the emergence of the capitalist economy. How the two resource-poor countries worked their way into the top of the income league by honouring people's rights to land will be the subject of a separate study.[xv] The relevance of the comparison for our present problem is this: the restoration of social solidarity is imperative if the Anglo-American model is to adapt to the challenges of the 21st century. The aged and infirm, for example, are vulnerable, with the gains of the last 50 years under threat. Substantial changes in the pension arrangements are unavoidable. The Tax State's solution is to require low-income people to work until they drop dead. Similar challenges are arising in the health sector. Long-term spending in the UK is predicted to increase from 7.2% of national income to 12.7% by 2050. If people want access to the medical care made possible by scientists in their laboratories, they cannot rely on these being delivered by the Tax State.

In the United States, the private pension crisis faced by employers is resulting in the jettisoning of employees' pension plans. Private enterprise is covertly shifting responsibility onto taxpayers. What it distastefully calls Big Government is now being treated by Big Business as the escape route from the pension obligations which it assumed after the Second World War. So what looks like a low rate of tax-take in the US today will escalate to levels closer to other countries under the pressure of populist politics. This will erode the competitiveness of America, adding further stresses to an already over-burdened economy which is suffering from record levels of national debt.

The Tax State is rapidly losing its financial viability. Because economic growth is now hostage to consumption funded by debt, in Britain, in 2005 families pushed their debts to £1,158bn. This was over £30bn more than the value of total economic output. The nation reached the point where it was no longer paying its way.

A similar escalation of indebtedness has surfaced in the US. But the national debt, for which the US is dependent on creditors like China, India and Japan, has to be seen in its historical context. We have to go back to the early 1960s to track the trends in wages and salaries.

For households in the bottom half of the income distribution, wages (in inflation-adjusted dollars) have been flat or declining. For those in the top half, and particularly the top 10%, income has escalated into the stratosphere. This is the financial context for investigating the sociological implications of indebtedness.

Stagnant wages have made it increasingly difficult to acquire homes. As the price of real estate escalated, those at the bottom of the income league have been locked deeper into mortgage debt. That debt increased by more than 190% for people in the lowest 20% of incomes, compared with 40% for families in the top 10% income band (between 1989 and 2001). Then there is the difference in the kinds of debt being incurred. Credit card debt is a fraction of the total held by homeowners compared with those who rent their homes. By 2005, total household spending exceeded after-tax income for the first time since the Great Depression. Americans were dis-saving, eating into the seed corn (to use one of their favourite agricultural analogies).

The financial pain, however, was cushioned for one class of indebted household: the owners of real estate. With property prices rising rapidly, owners were able to borrow to spend. But this has increased the fragility of family finances. For over the 25 years to 2005, despite rising prices, the percentage of the value of homes that families own has plummeted (from 67% in 1979 to 56% in 2004).[xvi] The extraction of equity bequeaths a multi-dimensional crisis. First, families are getting deeper into debt and exposed to the day of reckoning when China pulls the financial plug and interest rates rise. But, secondly, the upward drive in property prices is transferring much of the debt to the next generation of American working families.

Economic growth continued apace, but the rewards were not distributed in a way that left the nation happy. In the 1960s, something started to go seriously wrong. The nation's state of happiness did not improve alongside the aggregate increase in material prosperity. Why? Was this not offensive to the constitution of America?

12.4 Happiness: a Constitutional Right?

THE NATURAL right to possess property was affirmed by John Locke (1632-1704). His version of the social contract contained the memorable restatement of the right to *life, liberty and estate*. The word *estate* was the old English term for land. Locke argued that we all enjoyed the natural right to possess land, which was freely provided by nature. He explained in *Second Treatise on Civil Government* (1690) that government was obliged to secure the practical means by which this could be delivered.

Locke's treatise was an embarrassment to the feudal rent-appropriators. How could the noblemen of the kingdom justify the accumulation of vast estates by dispossessing others of their natural birthright? The patricians of the New World solved that conundrum. Even though they claimed to base their Declaration of Independence on the doctrines of the English philosopher, they dropped one of Locke's natural rights. They swapped the right to land for the right to pursue happiness. Everyone in the "land of the free" enjoyed the right to "life, liberty and the pursuit of happiness". Little thought was given to how this right to happiness could be squared with the mal-distribution of land to a privileged minority.

The spirit of Locke's thesis was written into the constitutions of some of the states, including California's. But a right is meaningless if it cannot be enforced. How can a marginalised person in the United States seek to enforce his or her right to the pursuit of happiness in a Supreme Court? It is not in the gift of the legal system to ensure a person's happiness, or to determine the means by which that happiness can be pursued in each case. About 37m people are classified as poor in America, the blacks in the urban ghettos and the whites in the suburban trailer parks. It is reasonable to assume that many of them are involuntarily unhappy, but even if they could prove this, a court could not apply sanctions against others to ensure restitution.

Unhappiness on a socially significant scale is ingrained into the rich nations of the West. The scale of discontent is evident in our neighbourhoods. An obvious case is the stress associated with people's working lives. Family lifestyles are sacrificed as they work longer hours to make ends meet. This means less sleep than is needed, leading to physical and psychological deprivation.[xvii] Forced to commute long distances to work – by the need to move to locations where house prices are affordable - people skip meals (see Box 12:3). And so, even while medical science has learnt how to extend lives, the quality of life atrophies.

Does the proposal for tax reform address the problem of happiness? Discontent is heavily determined by the financial distance between the rich and the poor. In societies where the gap is relatively narrow, empirical research shows that the populations are relatively content. Happiness is not a function of the absolute level of prosperity. The United States, as the richest nation on earth, is also one of the unhappiest. The evidence was documented by Richard Layard.

Graph 12:3 tracks the growth of income in the US since 1945 and the index of happiness as reported in the General Social Survey. In general terms, there has been no increase in happiness since 1960. This confirms the common sense view affirmed by surveys which conclude that "there appears to be little income-induced increase in life satisfaction once one's family income rises above the median income".[xviii] But while happiness levelled off in the United States, it has risen in Europe where income *per capita* is significantly lower. How do we account for the disparity, and what can be done about it?

Graph 12:3

Income and Happiness in the US

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Source: Richard Layard, *Happiness*, London: Allen Lane, 2005, p.30

Layard is an influential academic whose work on unemployment and inequality helped to shape the Blair government's policies. His prominence as a policy advisor earned him a peerage. Startlingly, Layard concludes that we should impose *higher* taxes on people to persuade them to work less. And the data, if taken at face value, appears to support his shocking recommendation. In Table 12:2 we compare four countries where the hours spent at work vary by a considerable margin.

Table 12:2

Selected Quality-of-Life Indicators				
	Hours worked in the Year (Full-time workers, 2002)[1]	GDP *per capita*[2]	Top income tax rate: %	Home ownership rates: %
USA	2,000	36,067	35	70
UK	1,990	26,391	40	71
France	1,660	22,723	48.1	55
Germany	1,650	23,002	44.3	40[3]/43

Sources:
[1]Richard Layard, *Happiness*, London: Allen Lane, 2005, p. 50.
[2]Tax rates and GDP derived from Marc A. Miles, Kim R. Holmes and Mary Anastasia O'Grady, *2006 Index of Economic Freedom*, Washington, DC: The Heritage Foundation, 2006.
[3] Owner-occupied housing for the Federal Republic in 1988.

Americans work 350 hours more, on average, than German workers. During the year, Germans enjoy 43 days of leisure more than Americans. British workers invest up to 42 days more in work than their continental partners. These extra days are reflected in the higher GDP *per capita*. And yet…French and German workers enjoy their vacations and the quality of their lifestyles in general. They *expect* high quality public services. And from their vocal opposition and street protests against Anglo-American "neo-liberal reforms", it is clear that they are reluctant to swap their social model for one that is underpinned by tediously long working hours.

We cannot be dogmatic in deciphering the meaning behind the statistics. Some generalisations are defensible, however. It does appear that continental Europeans do want more of their services delivered through the public sector, compared with Americans. And the Europeans are less discontent with taxation than their English-speaking cousins. But is it the higher tax rates in Europe that encourages workers to seek an escape from work through leisure? That is the logic of Layard's analysis.

> Taxes are clearly performing some useful function, beyond that of raising money to pay for public expenditure: they are holding us back from an even more fevered way of life.[xix]

His recommendation – that we increase happiness by increasing taxes on incomes – is counter-intuitive. People would say that the reverse is consistent with common sense: if they were not taxed so heavily, they could afford to buy the things they need without having to work so hard. But in Layard's view, workers in Britain and America – who are subject to lower tax rates - suffer from "addiction" to work. And since we deal with addictive expenditures – such as tobacco – by taxing them, the way to adjust the life/work balance is to reduce living standards by raising taxes on those who go to work!

To justify his prescriptions, Layard is obliged to challenge the traditional treatment of taxes as injurious. He does acknowledge that "£1 collected in tax actually hurts more than the simple loss of £1 – the difference being called the 'excess burden' of the tax. This makes taxes harder to justify".[xx] But he transforms the negative qualities of taxation. For by defining work as an addiction, a tax that deters people from going to work is transformed into something good, and the losses associated with taxation become acceptable.

Our competing thesis is consistent with reality. We have to factor in the impact of the real estate market. The reason why people are coerced into working harder is not just because of tax rates, but because of the distortions caused by the character of the taxes used by government. One impact is the unaffordability of houses, which forces (for example) mothers to work when they might prefer to devote their lives to nurturing their children. The result emerges in social surveys, such as the one which reported on the effects of the long hours worked by UK employees compared with their fellow citizens in the EU. With people in the UK having the longest working hours in Europe, more than one third of British men rely on alcohol to relieve the stress from over-working. Notably, men who found it most difficult to switch off from work had careers in property, with 52% saying it was hard to stop thinking about the job. Overall, more than 25% of men suffer from exhaustion through stress. According to Cary Cooper, Professor of Organisational Psychology and Health at Lancaster University: "Employees are more autocratically managed and are intrinsically more insecure. These changing patterns of work seem to be having a negative effect on men's health".[xxi]

But if raising the tax rate is at odds with reality, a solution to discontent is not to be found in merely lowering the rate of taxes. For lower taxes tend to be offset by a rise in land prices. Land prices are higher in the relatively low-tax Anglo-American countries compared with those in Germany, where people work the fewest hours and a larger percentage of the population lives in rented accommodation. German workers are not pressured by the burden of mortgages, which sit heavily on the shoulders of British and American employees. It is the two taken together – tax rates and land prices – that have to be weighed in the balance.

Culture plays a major role in the propensity of people to buy or rent their homes. In America, ownership has achieved the status of a cult-like quality, as one *Financial Times* correspondent saw it.[xxii] Security of possession (such as is provided by leases) rather than freehold tenure was sufficient for the majority of German families. This is reflected in their attitude towards home-owners, who are labelled as *spiessig*, or petit bourgeois.

From the conflicting sentiments over ownership rights spring financial costs that affect psychological health in America, where, in many residential areas, the premium for owning a house is a cost 40% higher than renting the home, according to research by the HSBC bank.[xxiii] Is that extra burden worth it? What is not in doubt is that Americans have to devote more hours to earning money, and devote more time to commuting, to cover the extra costs of owning the freehold to their homes.

By combining the tax and tenure effects we arrive at a rounded assessment of the conditions that determine material prosperity and personal contentment. Superior results are achieved when we diminish the taxes that distort people's freedoms. As for the provision of public services, the best results are achieved when the payments are symmetrically tailored to the services that each of us wants to access from the locations where we want to live or work.

This agenda does not receive attention by governments. Instead, advisors like Lord Layard propose strategies that aggravate society's problems. Raising the tax rate, for example, does not help people to fund their mortgages out of post-tax incomes. Nor does it resolve the problems that flow from the propensity of high income earners to "shelter" their wealth from taxation through investment in real estate, which consequently widens the gap between rich and poor. To the relatively poor, the robust equation is: Taxes = Unhappiness.

Is this reasoning beyond the comprehension of people like Lord Layard (who is an economist, not a psychologist)? Couldn't Layard have drawn on "public economics", a sub-discipline of his specialty, to deepen his understanding of the way in which taxation damages people's efforts to achieve happiness? In fact, Layard had studied public economics, and he concluded that it needed to be radically reformed because it "fails to explain the recent history of human welfare and it ignores some of the key findings of modern psychology".[xxiv] As evidence, he cited the book by Nobel Prize economist Joseph Stiglitz and his co-author Anthony Atkinson. This was a puzzling piece of evidence in favour of his tax-raising agenda. Can we unravel that puzzle?

In an article published in an academic journal in 1977, Stiglitz explained that it was possible to fund public goods out of land in place of those taxes that damaged economic incentives. And in the volume to which Layard referred, Stiglitz and Atkinson affirmed this tax theorem in which "rents equal public goods expenditure. This has been dubbed the 'Henry George' theorem, since not only is the land tax non-distortionary, but also it is the 'single tax' required to finance the public good".[xxv]

Stiglitz, who has served as Chairman of the President's Council of Economic Advisors and as Chief Economist at the World Bank, took the trouble to affirm the truth of an economic law that has a tradition which links Locke in the 17th century, Adam Smith in the 18th century, J.S. Mill in the 19th century and Alfred Marshall in the 20th century. Could this be why Stiglitz was selected as Layard's target (if only unconsciously)? Stiglitz provided the algebraic proof that confirmed the public policy virtues of rent and he exposed as injurious the taxes favoured by the economic fraternity. Those findings were at variance with Layard's eccentric psychology: "[W]e now know that people would work too hard if taxes were zero".[xxvi] Therefore, "much of the addiction to general spending, like the addiction to smoking, is not foreseen. If we are willing to tax addictive substances, we should also be willing to tax other forms of addiction" - like work.[xxvii]

Layard's prescription brings to mind a fiscal policy employed by British colonial administrators in Africa. A hut tax was introduced to force men to leave their families and seek work – for cash wages – down the mines. Men had to be driven out of the countryside, where they were free to choose the balance between work and leisure that met their personal needs. These Africans were deemed to be idle, and had to be *made* to work: hence the imposition of the tax on their homes. The colonial tax philosophy was an abuse of people's human rights, and so is Layard's proposal to supposedly deter people from working.

If the Anglo-American model of society is to be redeemed, we need to apply greater rigour in our economic analysis. Governments and their agents may not like the results, but that is not a problem for the people.

References

i Erik Ekholm, “Plight Deepens for Black Men, Studies Warn,” *New York Times, March 20,* 2006. The US had the highest percentage of its population in prison in the world.

ii Jonathan Kozol (author of *The Shame of the Nation: The Restoration of Apartheid Schooling in America*, New York: Crown, 2005) claims: “It’s not simply that segregation has returned with a vengeance to public education; it’s worse than it’s been at any time since 1968.” (Interview in Extra! March/April 2006, <http://www.fair.org/>www.fair.org).

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iv Mason Gaffney and Richard Noyes, “The income-stimulating incentives of the property tax”, in Fred Harrison, *The Losses of Nations*, London: Othila Press, 1998, p. 211. Table 8:IV.

v John Y. Campbell and João F. Cocco, “Household risk management and optimal mortgage choice”, Harvard University and London Business School Working Paper. April 2003, p. 23

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vii *Ibid*, p. 21.

viii Peter Gosselin, “On Their Own in Battered New Orleans”, *Los Angeles Times*, December 4, 2005.

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xxv Anthony B. Atkinson and Joseph E. Stiglitz, *Lectures on Public Economics*, London: McGraw-Hill, 1980, p. 525.

xxvi Layard, “Happiness and Public Policy”, p. C27.

xxvii *Ibid*., p. C29.