SOUTH
AFRICAN
CONSTITUTIONAL
PROPERTY
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FOUNDATION

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Submission on the Draft Rate and Monetary Amounts and Amendment of Revenue Laws Bill

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The SA Constitution anticipates radical economic disruption.

Summary of the case for challenging the state's fiscal policies:

We propose a new section in the budget for land-use charges, the nation's land rents. These are to gradually replace income taxes and vat.

Most taxes and other sources of public revenue undermine the economic productivity of an economy. Three types of public revenue do not: prices for public services that are no more than the marginal costs of those services, charges for harms such as pollution and congestion, and public collection of land use-charges, the land rents.

In today's submission, we focus on the public collection of the rental value of land, those revenues which presently accrue to owners without any effort on their part. They come from nature's endowment, population increase and state spending on infrastructure, services and governance, including the protection of titles.

Public collection of the rental value of land does not undermine economic efficiency because when properly administered, the amount of tax that is collected is independent of any action that might be taken by the owner of the land. This means that the owner has no tax incentive for reduced productivity. Like leaving idle.

We therefore propose an additional line in the budget for land-use charges, with other taxes reduced by the amount rent that is collected.

We suggest that rents be phased in over four years, replacing first 25%, then 50%, then 75%, then 100% of income taxes and vat. Government revenues therefore remain stable.

The government should be considered to have an obligation to reduce the income tax and other harmful taxes whenever it can, since the Constitution requires that the taxing power not be used in economically destructive ways. Section 228 of the Constitution specifies that the taxing powers of the provinces:

> "May not be exercised in a way that materially and unreasonably prejudices national economic policies, economic activities across provincial boundaries, or the national mobility of goods, services, capital or labour."

In interpreting these words, one ought to take account of the economic fact that when a tax is economically harmful, it is harmful from the very first rand. Furthermore, the harm from a harmful tax is roughly proportional to the square of the tax rate, so that the harm starts out small and grows insidiously and disproportionately, as the tax rate increases.

Since land rents are not harmful, it is reasonable to conclude that while such sources of revenue are available, any economically harmful tax

> “materially and unreasonably prejudices national economic policies, economic activities across provincial boundaries, or the national mobility of goods, services, capital or labour”.

The harms from harmful taxes are the increased costs of goods and services, the reduction in incentive to save, the increased incentive to invest abroad rather than domestically Annexure B, the reduced incentive to identify entrepreneurial opportunities that create jobs, the costs of collection and the reduced incentive to work productively with the opportunities that come one’s way.

These “dead-weight losses” from taxation in South Africa are estimated to cost R1 trillion rand annually; a 1:1 ratio in lost GDP.

That is an average of ±R67Kpa for each family unit.

Public collection of the rent of land has the further economic advantage that it takes the profit out of land speculation, so that those who have land will be motivated to use it efficiently.

Yet another important advantage of avoiding taxes on productive activity and instead using the rent of land as a primary source of public revenue is that the selling price of land will fall, so that access to land will improve for all of our fellow citizens who are struggling economically. This is brought about where land rents form a part of state revenue as Annexure A.

In fact, in Section 25.5, the Constitution demands that:

> “The state must take reasonable legislative and other measures, within its available resources, to foster conditions which enable citizens to gain access to land on an equitable basis.”

The foundation of access to land on an equitable basis is therefore the public collection of the rent of land.

Equitable access to land would be further improved if all citizens received a basic income from which they might pay the rent on a basic share of land, and if land use control were conducted by charging people for the harm of harmful land uses (including the disuse of land) rather than by zoning land for specific use categories.

HOW DID THIS ALL COME ABOUT?

Constitutionalism is the new legal order in South Africa. It is the synthesis of the pre-1994 socialism and capitalism and requires that the taxing power not be used in economically destructive ways.

So what happened? Those who were appointed to advise the state on what fiscal system abolishes the jobless, landless and low growth South Africa conditions were not qualified to do so.

These advisers included the Katz Tax Commissioners, the Freemarket Foundation and their fellows in academia and the media, as well as the National Development Plan (NDP). More recently the Davis Tax Committee (DTC) added to the confusion:

The 1994 Katz Tax Commission's Interim Guideline of Principles included the famously injudicious para 1.5.4(h);

Balance between taxes:

> "Both equity and the enhancement of economic growth require a considered balance between direct and indirect taxes, and between taxes based on income, transactions, resource use and consumption, and also require a balanced presence in the system of taxes on capital or wealth.
>
> "The Commission recognises that economic stability cannot be promoted through attempts to shift the tax burden predominantly onto any single dimension of economic activity."

The first mistake is the choice of a "balance" between man-made and natural sources of revenue (between taxes based on income, transactions, resource use and consumption; that is work, land and shopping) when they have diametrically opposed consequences.

This is shown by the fact that the state can appropriate 100% of all land rents without the supply of land shrinking by one centimeter. That is why the capture of land rents is deemed inelastic for no supply constraints occur.

On the other hand personal taxes on (elastic) income, capital and shopping reduces supply. This is established by the Laffer curves which shows that supply will reduce at 1% tax and expire at tax rates above 25%.

Katz related mistake was to suggest that a single land tax cannot bring about economic stability and GDP growth. This is better described by Leon Louw the Freemarket Foundation's CEO:

> "With tax policy, however, government is left a free hand. The legitimacy and sense of taxing one activity, not taxing another, and subsidising a third is hardly questioned. Yet it is only common sense that you get less of what you tax and more of what you subsidise."

Which aligns with Katz second paragraph above.

As for the NDP there is again no distinction between "good" inelastic taxes on natural assets like land and the spectrum and "bad" elastic taxes on work and wealth.

More alarming is that the DTC used the 2011 UK Mirrlees Report as a virtual blue-print for its 2016 Macro-Economic Analysis, citing it seventeen times. But the DTC failed to even mention the advantages of land rents which Mirrlees sets down in his chapter 16, Taxes on Land and Property. Sir James Mirrlees was awarded a 1996 Nobel Memorial Prize in Economic Science.

Finally, unlike South Africa, the UK had no written constitution to guide the Mirrlees report. Yet the DTC has the nerve to assert that the South African tax system must flout the Constitution. This is shown in para 6.3 of the DTC Principles of a Good Tax System, August 2016: -

> "The tax system must not be used to offset pathologies in other parts of the system (e.g. in respect of property rights or labour market challenges). If other elements of public policy are unclear or problematic, these should be dealt with at source and not compensated for by the tax system."

This is a malevolent finding, especially from Judge Davis who teaches constitutional and tax law at UCT. For the pathologies that the DTC asserts in the property market are that half the population wants high and increasing land prices and the landless want them to be low and affordable. In the labour market too, rampant unemployment inevitably arises whenever the state taxes work and wealth not land rents.

That is because, by default, personal taxes subsidise land prices. ABSA reports that average urban land (like in Southfield) has risen seventeen times since 1994 to R750 000. That windfall arises without owners leaving their stoep. And that is why it is understood that landowners do not pay taxes but simply advance funds to SARS and wait for land price rises for reimbursement. This flagrant unfairness contradicts sec 9 of the Constitution.

Further, without affordable access to land some thirty percent of the bill of rights are diluted, if not choked. These include the right to life, dignity, freedom from slavery and forced labour, freedom of occupation, housing, security of persons, clean environments, health care, food, water and education. The DTC recommendations are therefore unconstitutional.

Economic growth in a post income tax era means literally growing, rearing and making more things on unused land when disuse is illegal everywhere in the world.

Open-air factory floors of one hectare can then annually bear 20 piglets from one sow or 840 rabbits from a doe. If each of the 27m hectares of unused arable land in South Africa had one sow, then pig slaughterings could have increased by nearly two hundred times from 2.7million (2011) to 540 million (2017). And rearing pigs can be done on remote, cheap land.

Access to land is worth some R126Kpa to every indigent and illiterate pig farmer.

THE ULTIMATE ECONOMIC DISRUPTION A BLUE PRINT

The ultimate economic disruption is a Constitutional imperative. By insisting that citizens have access to land it finally ends the century's old divisive proletarian condition.

That means ending the dependency of millions on a wage or salary or on social grants for their very livelihood.

The constitution outlaw's the involuntary reliance on others. A common-sense reading is that, for equity to prevail, all able-bodied citizens must have access to sufficient land and natural resources to enable them to earn, let us say, a minimum of ±R10 500pm, depending on location. That is three times the state's new minimum wage proposal.

This measures up to the Henry George and Genesis axiom that "In nature there is no room for poverty."

In practice, and starting with an arable plot of 900sqm, it requires that a family spends an average 2 hours a day growing food for themselves and a cash-crop, (enough for another family), for sale to state institutions such as hospitals, schools, departmental offices and state-owned enterprises such as Eskom and Transnet. The produce must be collected twice a week and paid for at the gate.

One can quite accurately imagine what work families will need to do to save or earn the R10 500pm. On a 900sqm plot a family of four will save ±R3500pm in supermarket costs on 450sqm and earn ±R1750pm in cash crops on the other half. If they have two children the current social grants of ±R750pm will remain. There will also be ±R2 500pm savings in transport costs and in leaving back-yard rents in the corrugated iron suburbs. This all adds up to ±R8500pm.

The remaining six hours a day is spent building houses in gangs of nine. A reasonable 40sqm, three-bedroomed house, will be habitable within three months so that all the nine houses can be completed in 25 months. Materials will cost ±R240 000.

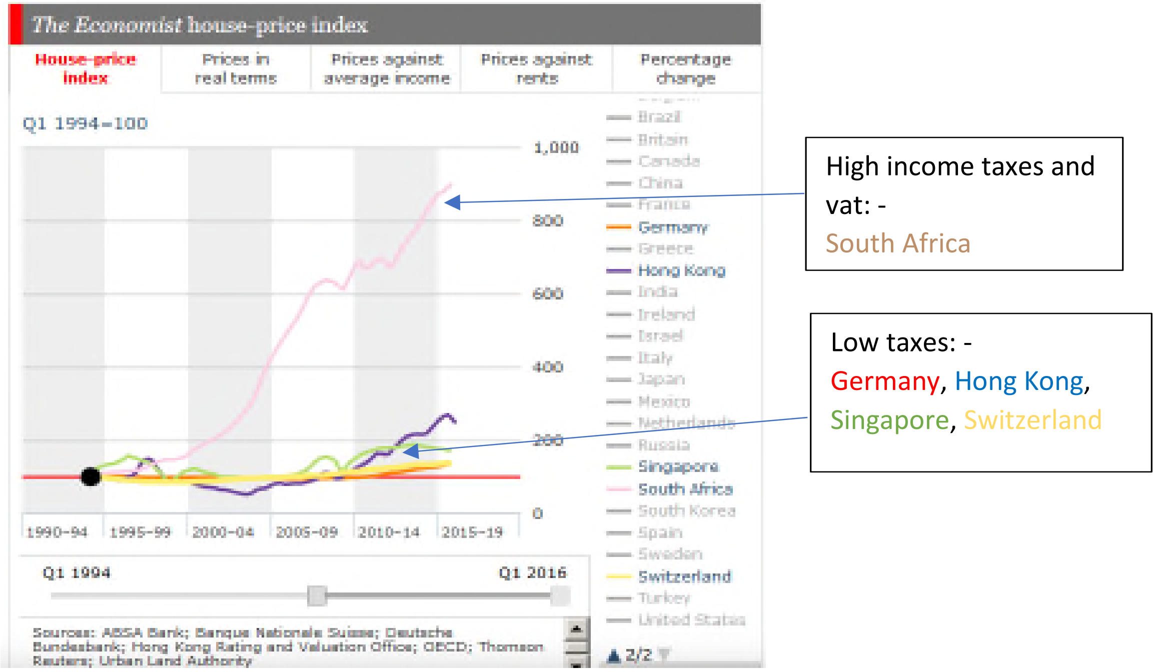
This does not rely on a state subsidy. A conventional terminating bond for that amount will be raised and paid off over 20 years at ±R2500pm.

This is a glimpse of the formula that ends the proletarian and landless condition by permitting people to confidently walk away from unwanted wage or salary contracts and rely instead on themselves and nature.

It raises many questions but it gives everyone a secure base to live off the land in frugal luxury, much like in Victorian times in UK.

Annexure A

House-price indexes as a proxy for land prices. South Africa vs Germany, Hong Kong Singapore and Switzerland



According to ABSA average urban land prices have risen 17 times to R750K since 1994

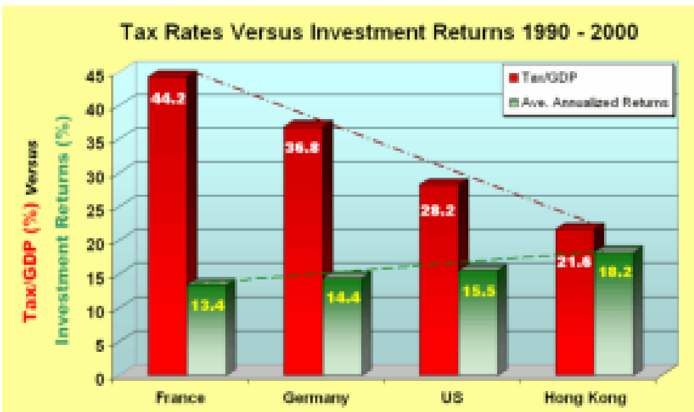
Annexure B

How International Tax Rates Impact Your Investments

Figure 2 compares the relationships between tax rates of four nations as a percentage of GDP and the average annual return in those nations' stock market indexes over the 11-year period from 1990 to 2000.

Indexes used were the French CAC-40, German SE XTRA DAX, U.S. Dow Jones Industrial Average (DJIA) and Hong Kong Hang Seng Index. These are 'buy-and-hold' annual rates of returns from 1990 through 2000 versus average percentage of taxes as percent of GDP. Market data provided by http://www.pring.com/ and http://www.metastock.com.

Figure 2



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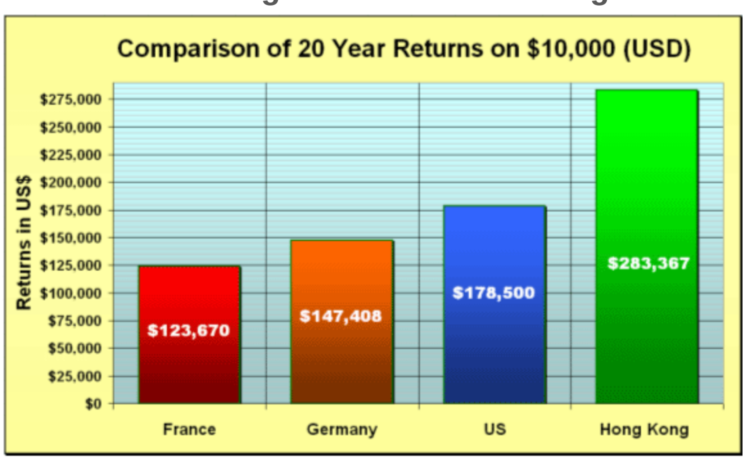
It appears there was an almost linear relationship between tax burden and index returns (see dashed dark red and green lines). If the rates of return in figure 2 continued for 20 years starting in 2004, the international investor would earn the returns represented in figure 3 if he or she were to invest $10,000 in each of the four national indexes.

Figure 3: Differences in 20-year returns for a $10,000 investment in the four national indexes assuming rates of returns in figure 2.



Differences in index performances between nations were found to be significant. Over a 20-year period, an investment in Hong Kong's Hang Seng Index, for example, would have returned more than double the same investment in France's CAC-40 and nearly double an investment in Germany's SEXTRA DAX Index.