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The Tax Trap

A long line of critical fiscal theorists has pointed to the limits of financing a politics of emancipation through levies on a regressive economy. We need to heed their warnings today.

Daniel Wortel-London • Winter 2021 A supervisor at Green City Growers Cooperative in Cleveland packages lettuce with employees. (Duane Prokop/Getty Images for takePart.org)

Read Aasha Desai's response to this article, "The MMT Trap," here, and Daniel Wortel-London's reply here.

"The State cannot cease to be a class State so long as its public finances remain class-bound at every level," declared Rudolf Goldscheid, an Austrian novelist, economist, and socialist, in his 1925 essay "A Sociological Approach to Problems of Public Finance." For Goldscheid, this binding took the form of the state's fiscal dependence on taxes drawn from the incomes and profits of the wealthy. While liberals and social democrats waxed rhapsodic over the social programs that could be funded via progressive taxation, Goldscheid cautioned that this arrangement provided their opponents with the fiscal leverage needed to veto those very policies.

Goldscheid's critique of what he called the "Tax State" has had a recent revival. In 2018, Stephanie Kelton, an economist and prominent advocate of Modern Monetary Theory (MMT), pointed out that although progressives may want to "break up the banks" and "shrink the size of the financial sector," they also want to finance social programs through taxing that very sector. This, she said, was a contradiction: it would leave those programs "completely dependent" upon "the very thing that you loathe."

That progressive taxation can serve as a barrier to progressive transformation can seem counterintuitive in an era when tax rates on the wealthy are already criminally low and tax evasion criminally high. Nonetheless, the work of Kelton, Goldscheid, and a long line of critical fiscal theorists exposes the limits of financing a politics of emancipation through levies on a regressive economy. With few exceptions, we cannot expect speculative and extractive firms to willingly fund reforms that will lead to a green and equitable economy—in other words, to dig their own graves. Nor can we expect taxing the profits of those sectors to make up for the broader social, environmental, and economic destruction they cause. Above all, we cannot allow our political capacity to be constrained by fiscal dependence upon our political opponents.

Only by democratizing public finances can democratic policies be firmly established and defended. But how can this be done? For traditional socialists like Goldscheid this meant displacing the for-profit sector and gradually moving profitable enterprises in a more public or cooperative direction, thereby allowing citizens to appropriate surplus value directly. Kelton and other supporters of MMT, by contrast, argue that the U.S. Treasury already has monopoly control over the creation and issue of U.S. dollars: we have only to realize and seize that power in order to finance the future we want.

These seemingly divergent critiques can be brought together for progressive ends in the United States. We can follow Goldscheid and his successors by developing democratically owned forms of public wealth creation where progressives are currently strong, particularly at the local level. The revenues generated by public and cooperative enterprises can then begin to displace the FIRE (finance, insurance, and real estate) and tech sectors as the fiscal foundation of progressive administrations, while simultaneously generating new constituencies for progressive politics. The expanded political and economic capacity generated through these enterprises can place progressives in a better position to push for the adoption of MMT principles at the national level, thereby fully opening up the fiscal horizon for the policies our communities, country, and planet need.

The Rise and Fall of the Tax State

Goldscheid's skepticism toward the "Tax State" was not shared by his contemporary and conational Joseph Schumpeter, who wrote an appreciative rebuttal of the socialist's ideas in 1918. "The hour that is belongs to private enterprise," Schumpeter argued, "and with private enterprise the hour also belongs to the tax state." Yet he paid homage to Goldscheid's broader point: taxation is not merely the "price we pay for civilization," but is specifically the price we pay for capitalist civilization.

In the feudal era, Schumpeter noted, European nobility had relied upon rents rather than taxes for revenue, drawn from the peasants whose land they owned. Between the fourteenth and eighteenth centuries, however, the endless wars conducted by this nobility (and the states that superseded them) required a more dynamic and profitable source of financing. Liberal political economists such as Adam Smith had a solution: if economic growth took place most rapidly and efficiently in the competitive private sector, it was in the interest of governing officials to contract out their revenue-producing property and confine their financing strictly to taxes drawn from flourishing market activity. Capitalist expansion and power was thus predicated on dispossessing and delegitimizing profitable state enterprises, just as peasants had been disposed of their commons and artisans of their guild monopolies during the era.

As a general rule, capitalists have been willing to furnish public revenues to the extent that such revenues are ultimately returned to them either by direct subsidies or by spending that promotes the accumulation and protection of property, like building infrastructure or financing police forces. When taxes are used to fund less evidently beneficial services—especially social goods directed to the working classes—capitalists have been far more reluctant to pony up. Still, there have been moments when changing ideologies within and power relations without the for-profit sector have facilitated more progressive uses of their profits. This occurred most notably during the mid-twentieth century, when many decommodified welfare services coexisted with a highly profitable private sector throughout much of the Global North. Between the pressures of a more densely organized union workforce operating under conditions of full employment, businesses whose commanding heights remained relatively geographically bound, and paradigms of economic growth at least somewhat receptive to demand-side rather than supply-side models, the tax state was able to furnish both guns and butter to a greater extent than ever before. (Matters were far more fraught on the local level in the United States, where white fears over public spending on behalf of racial others was a perennial source of political conflict.)

The 1970s marked the beginning of the end of the progressive tax state. A secular slowdown in economic growth took place across the Western world, at the very moment when emboldened workers were demanding increased social services. In response, a new generation of Marxist-inflected critical theorists, including James O'Connor, Claus Offe, Roger Friedland, and Frances Fox Piven, resurrected the kind of radical fiscal analysis pioneered by Goldscheid. Whereas conservatives blamed liberal social programs and business regulations for the crises in public finance, these theorists believed that it was the sluggish and unwilling corporate sector that was hastening fiscal crises and unduly restricting public coffers—and that the public needed to assert greater control over this sector in order to save both state and private finances from collapsing.

This is not what happened. Faced with a growing disjuncture between revenues and expenditures, many states chose instead to buy time by incurring debt from the financial sector. (For MMT proponents, the real story was not the borrowing but the issuing of more Treasury bills in response to deficit spending.) The borrowing came at a price: creditors demanded that economic decision-making be vested in undemocratic and unaccountable institutions, from local economic development corporations to central bankers to the IMF, and that the taxes used to service public-sector budgets and loans remain both regressive and minimal. In this way, what Goldscheid said of the Tax State became true of its Debt State successor: "The State became the instrument of the ruling classes by the fiscal organization which they imposed upon it."

The Power to Destroy

The visibility of private wealth in the midst of public squalor makes taxing the rich a seemingly commonsense method of paying for social services. The flaws in our current tax system are so glaring that their redress can serve several strategic goals for the left, and there is no doubt that the increased tax revenues such mobilizations can claim are sorely needed by citizens who rely on the public sector for goods and services.

This does not excuse us, however, from the duty to remain clear-eyed about how such well-intentioned campaigns to tax the wealthy can reproduce rather than challenge their power. We know too many examples of how, when progressives capture a city hall, state house, or even a national government, the public sector's reliance upon resource-rich actors for revenue or loans gives economic elites veto power over the democratic majority. As Frances Fox Piven stated in a co-written essay from 1977, "As long as state financing is dependent upon taxation (or public debt to private financial intermediaries), its autonomy is limited by the necessity to avoid policies that might impinge upon capital accumulation." As far as progressive policies are concerned, the old saying about the power to tax involving the power to destroy should be reversed: the power to *be* taxed is often, in the hands of the wealthy, the power to destroy.

Of course, history is rife with examples in which unions, social movements, and other vehicles of countervailing power have been able to compel the wealthy to pay for public goods that don't directly benefit them. Moreover, as the historian Adam Tooze recently discussed, the power of "bond market vigilantes" to enforce austerity appears to be obsolete in the wake of the deficit spending prompted by COVID-19 across the world. Yet we can't put the cart before the horse: the progressivity of a tax state depends largely on the balance of power outside it, and until the left substantially increases its power, we cannot expect even expanded public finances to be used for our purposes for any substantial length of time.

On a deeper level, however, we should question whether capturing the profits of powerful corporations and wealthy individuals can make up for the economic and political damage wrought by their operations. Economists are increasingly aware that the subsidies demanded and externalities generated by traditional models of "trickle-down" economic development—sprawling office parks, speculative luxury housing, glitzy stadiums, all catering to potential investors rather than current residents—undermine rather than stabilize local finances, even as their users and occupants displace the very marginalized communities progressives seek to serve. On the state and national levels, fiscal reliance on extractive and "too big to fail" sectors predicated on the cannibalization of middle- and working-class enterprises and jobs is both economically unsustainable and politically destructive for the left. For progressives to be fiscally dependent upon the same economic developments whose existence displaces their constituency, whose owners contest their policy agenda, and whose operations consistently undermine both private and public finances is profoundly self-defeating.

Still, for thousands of struggling working-class communities dealing with simultaneous crises of public financing and economic decline in every part of the country, the prospect of corporate-centric growth—no matter how hazy its benefits or harmful its consequences—is preferable to unemployment, regressive taxation, private bankruptcy, and public default. If progressives are unable to speak to these fears, their criticisms of traditional methods of economic development and public funding will be ignored, and justifiably so.

Fortunately, there are ways of financing the public sector that can strengthen local economies, expand the ranks of the left, and finance the policies we all need.

Popular Control Over Economic Growth

“A Propertyless State,” Goldscheid argued, “may be politically conquered by the workers for a time, but it cannot be economically held in the long run.” His solution was for the public to claim direct ownership over profitable enterprises—in everything from land and transit to energy and finance—and thus eliminate the “power of the purse” held by the private sector. Popular control over economic growth, free from the specter of tax or capital strikes, was a necessary if not sufficient condition for popular control over who that growth should benefit.

Today an increasing number of communities are pursuing local economic alternative development strategies (LEADS, in the terminology of the political scientist David Imbroscio) lodged in neighborhood businesses, nonprofits, and cooperative or publicly owned enterprises. Whereas many progressives rightly value co-ops and publicly owned businesses for the democratic virtues of their operations or the affordability of their services, it is key to remember that they also, tacitly or explicitly, contain possibilities for displacing corporate-centric frameworks of public finance and trickle-down models of economic growth—and it is on this point that their greatest potential lies.

State-owned financial institutions such as the Wisconsin State Life Insurance Fund and the Bank of North Dakota have operated profitably for more than a century, and proposals for similar enterprises are in the works in other states. Publicly owned power utilities currently generate more than $50 billion in annual revenue in the United States alone, while providing more tax and service contributions to the communities they serve on average than their investor-owned alternatives. State and local governments are increasingly turning to direct ownership in other sectors, among them real estate, telecommunications, insurance, retail, and equity investment.

The growing cooperative movement has a similar record of success. As of 2018 there are 465 worker co-ops in the United States employing 6,454 workers and generating $505 million in estimated revenue. More than 100 million Americans are members of profitable consumer cooperatives, covering sectors as diverse as banking, electricity, housing, food, and utilities. Altogether, there are currently 29,000 co-ops in the United States representing 130 million member-owners generating $650 billion per year in revenue. In Jackson, Mississippi, an entire network of worker-owned cooperatives is being developed as a means of overcoming racial injustice and the city’s economic challenges. Other examples, such as community development corporations, land trusts, and companies with employee stock ownership programs, show that entrepreneurialism and economic efficiency are not the monopoly of the for-profit model.

LEADS are rooted in the local public sector or civil society rather than run by unaccountable elites, which means there is less opportunity for these enterprises to use the threat of job or taxpayer flight to combat progressive policies. In addition, the superior services and economic efficiency provided by LEADS can enable progressive administrations to win support from a wider constituency—struggling small businesses, under- and unemployed workers, small taxpayers interested in reducing regressive levies, and anyone else shortchanged by extractive and corporate-centric patterns of growth. Developing these enterprises can also deepen the values of solidarity and mutualism that are essential for building an egalitarian polity and are left underdeveloped by trickle-down public financing. Finally, by providing actually existing alternatives to dominant (and ineffective) paradigms of political economy while building up our civic, political, and economic capacity, LEADS can enable progressives to win victories at higher tiers of political and ideological conflict.

Because the American public sector is already spending generously on economic development, moreover, the fiscal means and policy rationale for promoting LEADS are well-established and within our hands. In 2018, for example, New York State dispensed $9.9 billion in economic development subsidies—just a fraction of what a 2018 Brookings report estimated to be $45-90 billion a year of state and local subsidies. The majority of this aid went to the usual corporate suspects. What if some of it were redirected to development agencies that actually accomplish what they promise? What if local and state governments provided cooperatives with the same kind of technical assistance, zoning allowances, procurement preferences, tax incentives, and other benefits they currently give away to for-profit firms and wasteful mega-developments like New York City's Hudson Yards?

As critics of state capitalism have long charged, however, claiming public or even cooperative ownership over economic enterprises does nothing to eradicate the dangers of hierarchy or exploitation within them. Nor, as long as these enterprises must remain profitable, does changing ownership eliminate the compromises and tensions that attend making those profits. What democratic ownership does is widen the scope of who gets to navigate these tensions, while holding owners to a greater standard of responsibility for their choices.

What if, however, there were a way for communities to raise revenue that wasn't dependent on profitable public enterprises, taxes, or loans drawn from the private sector, or even the functioning of an economy at all?

Money as a Public Utility

For MMT advocates, national governments are masters of their own fiscal destiny by virtue of their monopoly over currency creation. The money through which taxes are paid originates not in the private sector but from credit lines first extended by central banks, which can be expanded or contracted as the state sees fit. From this perspective, debating whether we can "afford" expansive social programs is misguided or disingenuous. The money is there. All that limits us are physical resources, inflation, and our imagination.

Seeing money as a centralized public utility, rather than a private and finite resource, clears the path for one of the most venerable of progressive demands: a job guarantee. By subsidizing and creating jobs around green energy and transit, we can begin to shift our economy off its current earth-destroying path. By serving as a generous employer of last resort, the government can also bolster the wage floor, shop conditions, and bargaining power of every worker.

In addition to freeing workers from the tyranny of their bosses, MMT can free the government from the tyranny of private investors and large taxpayers. Cash-strapped municipalities would no longer need to justify gentrification or mega-developments in the name of increased property taxes, or corporate handouts and subsidies in the name of increasing sales tax revenue. The public sector wouldn't be forced to bail out financial firms, only to suffer the indignity of borrowing from those very firms at extortionate rates in order to make ends meet. No longer, in short, would the corporate for-profit sector set the tone and pace of our politics. Nor would progressives need to engage in the difficulties and compromises of establishing public enterprises or cooperatives on a profitable basis.

While MMT might expand the fiscal capacity of the government, however, only politics will determine what that money will be used for. If a political weakness of the tax state lies in its dependence on those who furnish the revenue, and a weakness of LEADS lies in their commitment to profitability, then a weakness of the modern monetary state lies in its very strength: the concentration of money-making power within the national government.

A growing number of MMT advocates are attempting to think through the challenges of decentralizing the means of monetary production through local currencies, providing sovereign monetary power to local governments, or giving credit-extending powers to public universities. Nonetheless, for the most part the U.S. Treasury remains prioritized as the entity that can "mint the coin" of progressive dreams. Unfortunately, the Treasury is a national institution in a country whose national institutions—the Electoral College, the Senate, a first-past-the-post voting system—are structurally biased against progressive infiltration.

Even if progressives should win over the national government, federal aid will find its way to the wrong hands if delivered to unreconstructed local regimes. This took place during the New Deal, when robust national spending was often diverted or directed into the pockets of white power brokers at the local level. It also took place in the 1960s, when local political machines were able to isolate, suppress, and co-opt experiments in community action funded by the Great Society at the national level. And it can still happen: even if local and state governments were to receive additional stimulus aid under a Biden administration, such aid alone would do nothing to halt the wasteful forms of economic development they currently practice.

MMT makes a convincing case that austerity is—and always has been—a bogeyman. What remains to be seen is whether a broader acceptance of MMT principles will threaten or be appropriated by the masters of our current political economy.

A New Economy

Critical fiscal theory along the lines pioneered by Goldscheid reveals the profound limitations of the liberal tax state. The more we encourage progressive taxation as a means of financing the public sector, the more we risk defeating our own purposes. And yet without progressive taxation, we foist regressive burdens upon working-class citizens. MMT, on the other hand, provides progressives with a post-revenue approach to public spending—but without sufficient political capacity on the left, such an approach can wind up in the wrong hands, benefitting the wrong people. What is to be done?

In the short run, progressives must continue to fight for fair taxation, but we should simultaneously use some of that revenue to place our public finances on new footing. By providing resources to working-class communities in a way that the corporate for-profit sector is both unwilling and unable to deliver—and with more concern for social equity and environmental sustainability than shareholder-dominated concerns ever could—LEADS can secure and expand the fiscal and political capacity of left administrations. This will provide progressives with better grounds for fighting for and implementing MMT practices on a broader scale, much as local political coalitions around publicly promoted economic development provided the groundwork for Keynesian breaks in fiscal orthodoxy on the national level during the 1930s and ’40s. Whereas the Keynesian growth machine helped set the stage for our current extractive economy, however, MMT can be used to transition our economy to one built on sustainable, equitable lines.

We cannot afford to wait. Over the coming years, we will see an increasing number of governments chafe against what remains of the Washington Consensus via populist curbs on the free market, corporatist governing arrangements, and expansionary monetary policies. Just as with Keynesian growth strategies, though, the political valences of these developments are open-ended. If xenophobic authoritarians and right-wing populists capture the benefits of challenging neoliberalism and public austerity, we are all in for dark times. If the left is to have the political capacity to take advantage of neoliberalism’s deepening crisis, we must begin restoring the economic vibrancy of our communities and local governments where we are already strong *now* and build upward. It is not enough to demand the goods; we have to start delivering them.

We need a new economy—one that is socially productive, democratic in operation, and equitable in outcome. We don’t need to rely upon taxing the wealthy to establish it. To seize the possibilities of collective ownership and MMT, and to place our public finances on a new and stronger foundation, is to open up our political horizon beyond the false dilemmas imposed by the current purse holders of the economy. This will only, however, make starker an older and greater dilemma: between unlimited individual desire and the limited resources of the planet. If money and its masters were no object, would we be capable of separating our needs from wants to avoid bankrupting our environment? Would we be capable of developing a common framework by which we could adjudicate and justify separate claims to a shared earth? Only by placing our public finances on cooperative lines can we reach the point when these questions can be answered truthfully—and affirmatively.

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