

# Money and Taxes

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## Introduction

Most money transactions now are electronic, not cash. The proposal in this essay is modest: to increase that to all electronic and do away with cash. The proposal enables a drastic simplification to taxes that has interesting consequences for the financial industry and for all of us.

## Money

In this proposal, each person carries an electronic device for money transfer; perhaps it is handheld, perhaps it is like a wristwatch. I will call this device a “mun”. It could be a device specially for that one purpose, or it could be a “mun app” on a smartphone or computer. Ideally, a mun should have biometric technology that recognizes its user, and gives access to its user's account(s), and not to any other accounts. Alternatively, we can use password protection, as we do at present with credit and debit cards.

To make a transaction, a person must be holding a mun, and must give the mun the receiver's identity and the amount. To make this easy, a mun can store the identities of frequent recipients. And by touching two muns together, the recipient can give the sender its identity. On request, a mun shows the current amount in its user's account(s), and a list of past transactions to and from other accounts.

## Accounting

An account is just an electronic memory location. For each currency (US\$, €, £, ...), a single government agency keeps the accounts. There are no attributes or characteristics like “savings”, “chequing”, “investment”, and so on. It is not interest bearing, there are no service charges, and the amount in the account cannot be negative. A transaction transfers an amount from one account to another. For efficient implementation, accounts may physically be located regionally, and an account migrates automatically to a new region when transactions from that account become predominantly from the new region. But that is an implementation detail beneath the concern of people using their accounts.

All accounts, and the record of transactions, are kept by a government agency. Any person or organization, whether resident in the currency zone or not, can have as many accounts as desired. A mun is a communication device privileged to access accounts. The correspondence between muns and accounts is not necessarily one-to-one. One can arrange for a single mun to access more than one account, and for a single account to be accessed by more than one mun. Also, a mun can make a single account appear to be as many accounts as its owner wishes, named for whatever purposes the account owner wishes.

## Taxes

Each transaction is taxed. When person A pays person B an amount  $d$  dollars,  $d$  dollars are subtracted from A's account,  $d \times (1 - t/100)$  dollars are added to B's account, and  $d \times t/100$  dollars are added to the government's tax account, where  $t$  is the tax as a percent. This is the only tax, replacing income tax, sales tax, property tax, and all other taxes.

It is possible to choose  $t$  so that the government receives no less and no more tax money than at present. It might be reasonable to choose  $t$  so that the government receives less money than at present because the entire tax department disappears. Perhaps annually, or perhaps whenever needed, the government must choose  $t$ . Experience will tell us the appropriate rate, but we might imagine something like 5% for reasons to be explained in the next section. When A pays B one dollar, A loses one dollar, B gains 95 cents, and the government gets 5 cents.

As with all transactions, when an employer pays a salary to an employee, the transaction tax is subtracted. Since this tax is much less than current income tax, it is possible for the employer to pay less and the employee to receive more than at present.

The current tax system includes a myriad of loopholes, preferential treatment, tax holidays, and tax exemptions. For example, some religious organizations (those lucky enough to be classed as official religion) pay no taxes. Some wealthy individuals and organizations use questionable donations and shelters to avoid their share of taxes. All tax loopholes and exemptions are gifts from the general population to the loophole users. The proposal is to sweep away the patchwork of tax loopholes and exemptions. If the government decides that the general population should give a gift to a person or organization, it can do so. But it should not do so by means of the tax system, or any other indirect mechanism. There is no reason why the amount of the gift should be tied to the tax a person or organization pays; it could be more or less. Who should get gifts, and how much they should get, should be a conscious decision based on merit, not an accident of the tax rate.

## Legal Tender

There is currently an enormous illegal underground economy consisting of services performed for cash that is not reported as income. If all these transactions are taxed, there is an enormous increase in the tax base, resulting in a low tax rate. To this end, we propose that the only money and the only monetary transactions recognized as legal by the courts are the government administered accounts and the transactions between them, which are taxed.

Why won't the underground economy continue, or even increase, in order to avoid the tax? There are two limitations: inconvenience and lack of trust. Nothing will stop two people from avoiding the tax by exchanging goods or services directly with each other, except that it is difficult to find someone else who wants what you have and has what you want of equal value. To be practical, an underground economy needs to allow indirect exchanges of various values among a larger group (a local exchange trading system). For that, a system of accounting, or a form of currency (which is just a distributed system of accounting), becomes necessary. The most convenient system of accounting is the one provided by the government accounts. Still, it might seem worth some inconvenience to avoid taxes, so the group might employ an accountant (that is exactly what a company does, and its internal accounting is an untaxed economy). Of course, the accountant must be paid, and trusted. Or perhaps a new, group currency is printed or minted; the group then takes upon itself the problems of credit, money supply, theft, and counterfeit. Or perhaps an existing foreign currency is used.

To illustrate the problem, consider this scenario: Person A does some work for person B, and person B pays person A in the underground currency. Person A accepts the payment and makes use of it. Then, with the encouragement of the legal system, Person A sues person B for lack of payment. Legally, foreign cash is just paper and metal. The only proof of payment accepted by the court is an entry in the transaction list of a government account. Person B is forced, by law, to pay person A again, this time in legal tender. That's why person B won't pay in the underground currency in the first place.

The current underground economy does not have these problems because it uses the existing legal tender untaxed. The proposal in this essay makes it impossible to use the legal

tender untaxed. For a transaction to enjoy legal recognition and protection by some country's legal system, it must be made in the currency of that country, paying that country's transaction tax. The inconvenience and lack of trust inherent in the use of an untaxed tender make paying taxes the better option, especially at the low rate that results when everyone pays taxes.

## Foreign Currency

People and goods travel, so it must be possible to convert money from one currency to another. The foreign currency is not legal tender in the land of the local currency, and as discussed in the previous section, transactions in the foreign currency do not have legal recognition and protection locally. But we need foreign currency to make transactions where the foreign currency is the legal tender, so we need to be able to convert money.

Suppose there are two unconnected automated transaction systems, one for each currency. Suppose person A has an account AA in currency A\$, and person Z has an account ZZ in currency Z\$. These people want to exchange some money at the currency conversion rate. Person A opens a new account AZ in currency Z\$, and person Z opens a new account ZA in currency A\$. Person A now sends money in currency A\$ from account AA to person Z's account ZA, and person Z sends the converted amount in currency Z\$ from account ZZ to person A's account AZ. They each now have some of the other's currency.

Suppose we want to make it more convenient to convert money by connecting the two automated transaction systems. When money is sent from an account in one currency, converting it automatically, to an account in the other currency, what is the tax rate: the sender's rate, the receiver's rate, or the average of the two? To whom does the tax go: the sender's government, the receiver's government, or half to each? These problems are solved simply by deciding.

But there is another problem. With the proposal of this essay, we would all keep all our money in the currency that has the lowest transaction tax rate. The government that has the lowest tax rate would get all the taxes, and all other governments would get none. So we need to eliminate the competition between currencies. To do so, we don't need co-operation between governments. One solution, perhaps drastic, is that the automated transaction system allows only those transactions that send money to receivers whose tax rate is equal to or higher than the sender's rate. Another, less drastic, solution is to charge double the tax for a transaction to a foreign account.

At present, a large amount of the world's wealth currently resides in "offshore" tax-free havens (Jersey, Cayman, Switzerland, ...) to avoid taxes at home. This problem is eliminated by having unconnected transaction systems, by having connected transaction systems with the restriction that money cannot flow from a higher to a lower tax rate, and by having connected transaction systems that charge double tax on money flowing out.

At present, money traders use rapid currency conversions to take advantage of changing rates. The wealth they gain comes from the devaluation of a currency, and therefore from all holders of the currency. It is theft, but unrecognized as theft because the victims are so numerous and each person's loss is small. In the proposal of this essay, there would be no gain because each transaction is taxed.

Elimination of off-shore tax havens, elimination of the untaxed underground economy, and taxation of currently untaxed financial industry transactions will allow the tax rate to be low. My 5% estimate may be too high.

## Allowance

The preceding sections propose replacing the current patchwork of taxes with a single transaction tax. Similarly, we could replace the current patchwork of payments from governments to people (social security, unemployment insurance, welfare, tax rebates, ...) with a single allowance. Who gets the allowance, and the amount of the allowance, are government decisions. Considering the savings to the economy won by the transaction tax, the amount could possibly be enough to cover all basic needs, paid to each citizen. The automation and uniformity of the allowance make it possible to pay the allowance daily. This frequency eliminates the start-of-month excess and end-of-month shortage that afflict people who have trouble budgeting. A citizen receiving a daily allowance can set their own preferences to make it appear that the allowance is divided into several accounts, such as the rent account, and the electric account, and so on, so that monthly expenses are covered, if that helps them budget.

## Winners and Losers

Financial institutions lose their role as the safekeepers of money, and the facilitators of transactions for daily living. But people still want to lend (invest) money for interest, and people still need to borrow money. Financial institutions can continue to play the important role of connecting lenders and borrowers. To keep the taxation involved to a minimum, money would not go from the lender to the financial institution, and from there to the borrower. Instead, the financial institution will tell the lender and borrower about each other, and the lender will send money to the borrower directly. In effect, the financial institution becomes a match-maker, matching a lender's characteristics to a borrower's needs, assessing and reporting on each to the other, and charging a fee for the service. This arrangement has the wonderfully salutary benefit that lenders will know to whom they are lending, and borrowers will know from whom they are borrowing.

At present, a lender may buy mutual funds that are characterized as “green”, for example. The prospectus for the fund probably lists financial institutions as the first nine destinations for the fund money, and the fund manager will defend the choice by saying that these financial institutions are both “green” and profitable. But these institutions are not destinations for investment; they are just way stations. They will invest the money as they see fit, and they are not bound by the original investor's desire to be “green”. In effect, they “launder” the fund constraints. Perhaps the tenth destination listed is a real destination. It may be “green” according to the fund manager, say “clean” coal, or nuclear power, but not “green” according to the investor. Knowing where your money goes places the responsibility for ethical investment on you, not masked and laundered by layers of financial intermediaries. Likewise for ethical borrowing.

Banks will no longer be able to create money when they make loans. If the government has a reason to create money, it can do so by adding money to its own account(s). When it does so, the money held in all other accounts is thereby devalued; the government gains some, and the people collectively lose the same value. But at least the government is their government. At present, when a bank creates money as banks do every day, the money held by everyone else is devalued; the bank gains, and everyone else loses.

The transaction tax makes rapid money movement unprofitable. “Investments” that last for hours or days, quick property flips, daily money trading, and any quick speculation will all disappear. To be profitable, an investment must last long enough to accrue interest greater than the one-time transaction tax. A well-run company will be able to count on retaining investment long enough to plan and prosper. Investors will have to take much more care, investment will

become much more stable, and the economy will be much healthier. This is achieved without legislated regulation, without policing, and without prosecution.

Some people produce real products (food, manufacturing, building, ...). Some people provide real services (education, medical care, transportation, entertainment, ...). Some people just “make money”, which means “take money” for no real production or service. A large part of the financial sector produces no real goods and provides no real services. The service they claim to provide is to advise the rest of us, and to help us, to join them in taking money for no real production or service. To join in, we just need to give them some money. It is large scale gambling, and the house always wins. The financial sector has brilliantly convinced us that the more money they drain from the economy (their profit), the healthier is the economy.

Eliminating the part of the financial industry that is unproductive causes unemployment to rise. That is the perfect opportunity to reduce the standard work week from five to four days. At one stroke, we reduce unemployment to near zero, and improve people's lives.

## Crime

The purpose of biometrics or a password is to make sure that only the owner of an account can see what's in the account, and pay money from it. It is still possible for a thief to defraud you, or to hold a gun to your head and force you to pay them money. But then you have a record of the transaction, including the account where the money went, from which the thief can be caught. Any crime involving payment of money leaves a record of the payment. Police who obtain the proper warrants can see the transaction record, and that aids crime detection. Criminals will have to find some other form of payment, and that will make their business much more difficult.

At present, most monetary transactions are made by computer, and many of them are made automatically on a prearranged schedule. The use of computers for transactions makes theft far too easy. Private and company and bank computers are corruptible by viruses, by reprogramming, or just by the accidental use of insecure communications. According to the proposal in this essay, accounts are kept and managed by government computers kept in high security. A mun need not be a general purpose processor that can be reprogrammed or corrupted by a virus. A mun's program can be compiled to silicon, making it a non-reprogrammable circuit.

In this proposal, a company's payroll computer cannot, by itself, make money transfers. It makes payments through a mun held by the right person. The need to have the right person present greatly reduces the opportunities for theft. And again, if anyone finds a way to make an unauthorized payment, there is a record of it saying where the money went.

At present, to make a transaction, the sender gives their identity (a credit card number or account number) to the receiver, allowing the receiver to extract money from the sender. It also allows thieves who fraudulently obtain the senders identity to extract money from the sender. In the proposal of this essay, the receiver gives their identity to the sender, allowing the sender to send money to the receiver. There is no need for secrecy; a receiver could publish their identity, allowing anyone to send them money. Identity theft would be pointless.

## Privacy

Many people will be concerned about a government agency that keeps track of every transaction they make. Certainly people who make illegal transactions and tax-evading transactions will be concerned, but we should not be swayed by them. Currently, private companies and financial institutions do track and record transactions for the odious purpose of target advertising; this may account for some of the concern. But a government agency does not have any interest in target advertising, so we should be less concerned about a government agency having our

transaction history than about a bank or other private institution having it. You do want a transaction history kept by someone, in order to protect yourself against theft and fraud, unless you are a thief or fraud.

At present, the tax department employs people to verify tax return statements, and to audit people and companies it considers questionable. Under the proposal, there will be no verifiers or auditors, and that should result in better privacy.

A single government agency is easier to monitor for any breach of privacy than a myriad of private institutions. If there are any remaining privacy concerns, they must be weighed against the enormous benefits of convenience, security, simplicity, and economy of the proposal in this essay.

## **from Here to There**

The proposal of this essay could be implemented in stages. In the first stage, the government accounts are introduced as an alternative to all other forms of currency, co-existing with them. This stage should last a year, long enough for everyone to convert all their liquid assets to their government accounts. Then it is declared the only legal currency. This stage should last a year, during which statistics are gathered, from which the appropriate tax and allowance rates can be calculated. And finally the tax and allowance are added, replacing all other taxes and benefits.

Most of the financial industry takes money from the rest of the economy without producing any real goods or services. It does so by constantly moving money, taking a fee with every movement, and creating money from nothing. The proposal of this essay would make that unprofitable, and the rest of society would be that much richer. But at present, the financial industry is large and rich, and it won't like losing its business. So we can expect it to oppose the proposals of this essay. They will not admit that their loss is everyone else's gain; they will convince our legislators and most of us that their loss is everyone's loss. I doubt that our legislators have the intelligence and courage needed to oppose the financial industry.

Here's what will probably happen. Programmers will create new accounting services that bypass banks, are more convenient than banks, and charge less than banks. The old banks will lose business even without the proposal made in this essay. The new services will then be our new banks; they will make quick speculation and trades easier, and the economy less stable. They will make the underground economy and offshore tax avoidance easier. They will increase the opportunities for fraud and default. That is my prediction.

## **Summary**

I have proposed a device and an accounting means to replace existing money. I have also proposed a tax to replace all existing taxes. I think the proposals are good ones in the sense that we would be better off with them than we are at present. But I have little hope that any government has the wisdom and courage to implement them.

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