

Hibernate and Circulate

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I have been arguing that the correct response to a pandemic is to invoke a hibernate-and-circulate strategy. "Hibernation" requires the closure of nonessential business and services where there is a risk of spreading the infection. "Circulation" entails replacing the resultant missing revenue by taxing those from whom this revenue used to emanate when paying for goods and services no longer available. Hibernation must last as long as is medically necessary and the circulation element must be sustainable through this period.

This strategy should be adopted irrespective of the taxation system in operation and should be moulded to the latter's form. Hence, although the Asset Based Taxation proposals have no place for taxes on income and profit, these are precisely the taxes I would use to raise circulation taxes: not because they are right but because they are there.

Rationale

The economic hit has been attributed to the pandemic. This simple view of the world is widely accepted by nearly everybody. But it is not accurate. The flaw is this attribution of cause when made without further qualification: it simply does not make sense.

Pandemics make people ill and kill many. In economic terms the temporary or permanent loss of productive workers and active consumers reduces the tax take while higher medical costs are incurred. If no action is taken, the human toll will be enormous and the economic toll will follow it. If action is taken to control the spread, fewer workers and active consumers are affected and the increase in medical costs can be limited.

What actually causes the economic hit is not the pandemic, but the mitigation. Closing nonessential businesses, imposing social distancing are all sensible mitigations both from an economic and medical perspective. But the mitigation tactics come at a cost.

Businesses cannot function without sufficient customers. They rely on these customers to provide them the income their business requires to operate. The rules of a market economy say that if they cannot generate enough then their product is not attractive enough to represent a good use of labour and must close. However, if legislation makes this impossible to achieve legislators have broadly three options:-

- 1). Say: "Sorry, that's life!" and let the businesses fail
- 2). Throw businesses financial lifelines
- 3). Fix the bit they broke

In the UK, the tactic has been a mix of 1 and 2. Government has intervened with grants and financial support and the furlough scheme has meant that incomes are supported without the requirement to work.

But there's still a significant proportion of option 1 in the Government's response. The Chancellor has declared, for instance, that he can't help everyone (BBC News, 09/07/20). Well, of course, he can, he's the Chancellor and empowered to do that. His utterance suggests that he believes the scale of the problem to be beyond his capacity to fully counter, i.e. he does believe "that's life" to some degree. In other words, the rules of the market economy are immutable and all he can do is provide support within those constraints.

Option 3 has not been considered because the concept has not really been framed. Because there has not been the recognition that it's the mitigation that's causing the economic problem there's been no thought to mitigate the mitigation, so to speak. Like a medic who has to crack some ribs to resuscitate a patient, the action is necessary and proportionate. But the ribs remain cracked and require fixing.

This analogy needs adapting a bit, however, as the collateral damage in our case is more like to an artery than a rib.

Quantity and coverage

Many of us in contemporary first-world countries are fortunate in that we are able to pursue activities that are not wholly related to daily subsistence. We all of us have to contribute, mostly through paid employment, to the common requirement to provide for subsistence: food networks, water, energy and accommodation. We further have the capacity to provide other goods and services over and above these. We probably didn't think about it too much before the pandemic, but the latter make up the nonessential goods and services, the former the essential ones.

The problem, in a nutshell, is that the way we are structured we can't just close down the nonessential part of the economy such that everyone limits themselves to essentials. But it is important to note that this is:

- a) Something we'd like to be able to do short-term, and
- b) Logically coherent

It is simply the rules of the economy that we are playing to that makes this impossible. It's impossible because the means by which we ensure everyone contributes is by making everyone pay money for essential goods and services, basically food, utilities, rent and mortgage payments. If our work happens to be in the nonessential sector, a lockdown means that we can only pay for these if we have savings or we have our incomes supplemented.

Because money isn't circulating, some people are short of it and this leads to the impression that there's an overall shortage of money. The government, likewise, is losing its revenues and cannot balance its budget without borrowing. Despite this, it knows simply letting all nonessential business fail and triggering unemployment on an unprecedented scale is not something that can be contemplated. So it feels it needs to borrow more to provide the necessary support.

This heightens the impression of there being lack of money in people's pockets, in businesses and at the Treasury, but actually there's nothing of the sort. The quantum of money will not have changed

that radically; it's just not circulating through the whole economy as it was, the coverage impacted and the velocity reduced.

Nonessential business is by definition paid for from disposable income, disposable meaning here that which is left over after the essential goods and services have been paid for. If the money was there pre-lockdown to do this, it's there afterwards as well. Sure, some of this money came from overseas, but the UK's balance of payments deficit means we were paying more away overseas than we were receiving, so any reduction in foreign trade should potentially improve the situation (though it will depend on the proportions of essential to non-essential goods and services being sourced from overseas). Further study could tell us how much of an impact this would have, but it doesn't look likely to alter our conclusion that mitigation primarily causes problems with money reaching the right places rather than an actual drain on the quantity of money.

The lockdown blocks an artery in the financial system. What the Government is currently doing is pumping blood into the remainder of the system rather than trying to bypass the blockage. Lockdown causes a circulation problem, but we're addressing it in terms of quantity.

Is this a problem?

So long as the government is willing and able to pursue its strategy for as long as is medically necessary, there's no problem with an injection of quantity as a means of rectifying the loss of coverage. But the UK chancellor is still intent on ceasing the furlough scheme at the end of October despite there already being signs of a resurgence of Covid-19 cases meaning that further easing of restrictions looks unlikely. If nothing changes there is only one way one can see this going: a large number of businesses failing and mass unemployment.

The government could stop all this by extending and expanding the scope and sophistication of the furlough scheme while funding the operation from taxation.

Doesn't taxation depress the economy?

Many progressives have argued against raising taxes arguing that it will depress economic activity and thus slow the recovery. Even the excellent Ann Pettifor seems to take this view, citing measures the UK government took after the Spanish flu pandemic: "Taxes were raised, government spending was cut, interest rates rose and the strengthened pound boosted debt servicing costs. Soon the British economy was in free fall" (Pettifor A., 2020). I contend that raising taxation as part of a circulation strategy that funds the furlough scheme will have a very different effect from doing so when government spending is to be cut.

Covering fixed costs

Businesses should receive funding from government that covers their entire fixed costs i.e. principally salaries, rents, rates and essential maintenance activities. This would start at 100% for

those businesses whose entire revenue streams have been blocked by the lockdown. Where the blocking is less than 100% (e.g. activity is allowed but has been restricted), claims can be made for the percentage by which maximum trading capacity has been reduced.

Businesses should self-certify, and a government service should be set up to capture the certification and provide evidence checking. It is reasonable for government to charge processing fees for participating businesses.

Funding should only go to those businesses that are directly impaired by government rules and guidance from gaining revenue. For example, should a business suffer a loss of income that is the result of a drop of public appetite for the service in the light of Covid-19, they would not per se be eligible, though government could extend loans to such businesses if it chose.

The duration of the support is this tied in with the duration of the constraints. There is no arbitrary cut-off date before the removal of restrictions.

Scope and sophistication

Extending the scope of the furlough scheme means putting an end to caps, haircuts and exclusions as these all frustrate the aim of disturbing as little of the circulation of money in the economy as possible. So let's end the UK's 20% salary haircut, the £2,500 per month cap and the exclusion of benefits for the self-employed above £50,000. By introducing an option to being assessed on previous employment, people who have recently moved jobs should not fall through the cracks.

Benefits should be frozen as the businesses fixed costs at the time of the initial lockdown. Employers making use of the furlough scheme should pay an additional rate of corporation tax on profits that is equivalent to the percentage of allowable benefits they claimed. In other words, an employer claiming 80% of its entitled funding and also making profits would pay the current rate of corporation tax on the profit plus 80% of the untaxed portion. Additional Corporation Tax would be capped at the value of furlough payments received.

Income and Corporation taxes would temporarily be raised to cover as much of the remaining costs as is practical whilst trying to ensure that the rises put as few people as possible into financial difficulty. The policy can be deemed successful if the burden is spread more fairly than now. The additional tax rates would be periodically reviewed and reduced as the lockdown is eased. Income taxes would, in effect, be rates payable for the purposes of PAYE with the final annual rate only determined at the end of the year.

Drawing dividends instead of salary

Workers who routinely pay themselves dividends instead of salary should be given the option having their last three years earnings re-designated as salary and pay any additional tax and national insurance applicable. These salaries could then be used to enable a furlough payment.

The practice of drawing dividends instead of salary should be abolished by denying certain limited companies the right to issue dividends. This would be fairer and simpler than the IR35 legislation. Dividends are a reward for lending savings to help capitalise a business. Some of these small limited companies have no share capital to speak of and few investors: it should not be difficult to arrive at a set of criteria for determining which businesses should be allowed to issues.

Using furloughed workers

Any government bankrolling employees while they are not working is entitled to draw on that labour to help them achieve whatever additional activity is necessary. There will be a temporary anomaly in that some of these new “workers” will be being paid different rates of pay for the same work. Once lockdown ceases, should these new jobs still be required, workers will have the option of staying on at the newly determined rate for the job or returning to their old work.

Future applications

If the above was successful, it would demonstrate that an economy is able to function with a considerably reduced level of economic activity over the long term. The economy would be balanced and essential services maintained. It would be a blueprint for how an economy could function with reduced economic activity.

If we are to be serious about addressing climate change, reducing the ecological footprint of our nonessential activity must be a priority - and that will include the volume of that activity. We cannot just go on saying that activity is essential because it provides incomes and livelihoods. The success of hibernate and circulate would show that the premise of that argument is false: it would demonstrate that livelihoods can be just as well protected with or without the activity.

A farsighted government could use these tactics outside the pandemic to help transition to a truly sustainable economy. This pandemic is our dress rehearsal for this: now is not the time to fluff the lines.

August 2020

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