

'SLIMMING DOWN GOVERNMENT'

THE FIRST CHRIS R. TAME MEMORIAL LECTURE,
HELD AT THE NATIONAL LIBERAL CLUB, LONDON,
ON THE 18TH MARCH 2008

Professor David Myddelton



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Professor David Myddelton is Emeritus Professor of Finance and Accounting at Cranfield University, Chairman of Board of Trustees of the Institute of Economic Affairs and Chairman of the National Council of the Society for Individual Freedom. In the late 1960s he was involved in the Young Libertarians along with the Libertarian Alliance's founder Dr. Chris R. Tame.

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Libertarian Alliance

For Life, Liberty, and Property

Suite 35
2 Lansdowne Row
Mayfair
London
W1J 6HL

Telephone: 0870 242 1712
Email: admin@libertarian.co.uk
Website: www.libertarian.co.uk

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Introduction

First of all I should like to say what an honour it is to be asked to give the first Chris Tame Memorial Lecture. It does make one feel somewhat ancient, to be giving a memorial lecture named after someone younger than oneself! But it's worth remembering that many of the liberties we value have a history far longer than a single human lifetime.

An Historical View of the Size of Government

I'm going to start by taking an overall view of the size of the British government at three different times. First, in the late Victorian period, say 1880. One could regard that as the height of *laissez-faire*, which I define simply as 'government non-intervention'. It probably doesn't much matter whether it was a formal policy or simply the practice and general attitude of the governing classes at that time.

Second, 1965, clearly post-Second World War, yet fifteen years pre-Thatcher. That may seem like history to some of you, but I remember it well! It was at this time that Robert Carnaghan and I founded a group called the Young Libertarians, which Chris Tame was associated with. I resigned five years later, not because I ceased to be libertarian but because I ceased to be young!

And finally 2008, which, oddly enough, I find quite hard to evaluate. It's a bit of a struggle for my generation to keep up with all the changes there've been; and I find it hard to tell what remains of the England we thought we were trying to defend when we were young.

Measuring the 'size' of government isn't easy; but

one approach is to look at government spending as a proportion of national income. In the long run, this is similar to taxes as a proportion of national income.

In 1880 it was 7½%—well under one tenth. In 1965 it was just under 50%—one half—and it's about the same today. Peacock and Wiseman wrote a book explaining how the huge increase in government spending during the two World Wars was never afterwards much reduced.

One big difference between 1880 and 1965 is the growth of the 'welfare state'—government spending on schooling, health services, retirement pensions and other social security.

In very rough terms, in 1880, the government spent about 4% of the national income on military defence together with interest on the national debt that had mostly been incurred to finance earlier wars. It spent about 3½% on law and order and everything else (making a total of 7½%); and virtually nothing on the 'welfare state' as we know it today.

By 1965, the government spent about 13% of the national income on military defence and debt interest; as much as 18% on law and order, housing, the losses of the nationalised industries, and all sorts of industrial subsidies; and 19% of the national income on the welfare state.

But today, although the total is still about 50%, there's quite a difference compared with what the government spent our money on in 1965. Today the government spends about 7% of the national income on defence and debt interest, 10% on law and order and everything else, and no less than 33% of the national income on the welfare state.

You could express the key difference between

the scope of the British government in 1965 and the position today in two words: Margaret Thatcher. After 1979 she reduced the damage from government activity in several respects. Over a period of eighteen years between 1979 and 1997 taxes fell from about 45% to about 37% of national income; but in the last eleven years they've gone back up again to 45%.

The Thatcher government privatised nearly all the nationalised industries (state monopolies), including the airlines, coal, electricity, gas, rail, steel and telecommunications; it improved the laws governing trade unions; and it reduced the top rate of income tax first to 60% and then to 40%. These changes have not since been reversed. Previously the top rate had been 83% on earned income and no less than 98% on investment income.

Their attitude was different too. When Geoffrey Howe had just become Chancellor of the Exchequer in 1979 he was asked what the government was going to do about some problem. And he replied: 'It's nothing to do with us!' I remember it because it so flummoxed the interviewer. He'd obviously set aside five minutes or more for this topic, and had trouble believing there was *anything* a British government would think wasn't its business!

One of the first things the Thatcher government did in 1979 was to abolish foreign exchange controls, which I, and others, had been proposing for the previous ten years. The only demonstration I ever went on was a march I led round the Bank of England in 1970 to protest against exchange controls. There were only half a dozen of us—such a pathetically small number that it got quite a bit of publicity! And when the government abolished exchange controls, nearly ten years later, it was the only time I've ever written to congratulate a British prime minister on a matter of policy!

Top rates of income tax over 90% and exchange controls were supposed to be *temporary* measures during the war-time emergency. Yet they both lasted for *forty* years, from 1939 to 1979, with the support of all three political parties. So we mustn't kid ourselves that once repressive laws are

introduced they're likely to be easy to get rid of.

High taxes tend to dampen incentives, involve a heavy burden of complexity, and waste the time of some of the cleverest people in the country. And of course they transfer money from the voluntary sector to the compulsory sector. They are fiendishly complicated. One of my favourite quotes is from Lord Justice Diplock in the three-man Court of Appeal. He said: 'It would be a poor compliment to the draftsman of Section 28 of the *Finance Act 1960* if this court were to be unanimous as to its meaning!'

I know the Inland Revenue (as I continue to call it) regards me as a bit of a nutter. That's because on the front of my income tax return each year I write a message in red ink: "Please forgive me if I've made any mistakes in completing this form. I've been studying the British tax system for more than forty years; but I'm afraid I haven't quite got the hang of it yet!"

Government in General

Let me now say something about 'government' in general. Dicey, writing about the advent of collectivism towards the end of the Victorian era, advocated *laissez-faire*. 'The beneficial effect of State intervention, especially in the form of legislation, is direct, immediate, and, so to speak, visible, whilst its evil effects are gradual and indirect, and lie out of sight... Hence the majority of mankind looks with undue favour on government intervention. This natural bias can be counteracted only by the existence ... of a presumption in favour of individual liberty—that is, of *laissez faire*.'

His point was illustrated last week by an absurd 'Budget competition' for schools. *The Times* published the winning entry, which contained nine promises to spend government money on various good causes, but *not a single word* about where the money was to come from. If the government didn't confiscate our money in taxes, we ourselves would have more to spend on what we value, not on what politicians think will buy votes. The technical name for that is 'opportunity cost'—and because it's hypothetical, it's very easy to overlook.

I agree with Arthur Seldon, one of the founders of the Institute of Economic Affairs, that we should take more risks of *under-government*! I don't want the government to 'encourage' business: all I want it to do is 'get out of the way'. In particular I'd like governments to be subject to the kind of Hippocratic Oath that doctors take: "above all, do no harm!" If only politicians would observe that simple instruction, it would cut out a great deal of damaging interference.

Probably 90% of legislation nowadays is attempting to put right evils introduced by prior legislation. I've lost count of how many *Criminal Justice Acts* have been passed in the last ten years. And we mustn't forget that democratic governments don't usually aim to 'do good' (whatever they think that means), but merely to *look as if* they're doing good!

Of course government also impinges on us all in economic and other ways that are hard to measure. For example, price controls don't show up in taxes or government spending, yet they're probably the most effective way to destroy free markets. Hayek said prices in the economy fulfil the same sort of function as signposts on roads: they give you informative signals, but they don't *command* you which road to take. In *Beyond the Fringe* there was a sketch where English people changed the directions of all the signposts to confuse the Germans if they invaded. But then, of course, they themselves couldn't tell how to get home!

And regulations seem to be growing all the time. In 1990 there were some 300 pages of accounting regulations: now there are about 3,000! Where will this kind of nonsense stop? The direct cost of regulations to the *government* may be fairly small; but the costs to businesses and individuals may be much higher; and the indirect effects higher still.

I want here to say a word about inflation, which I prefer to call currency debasement. As an accountant I've been much concerned with it over more than fifty years. Money is so important in a modern economy that governments which insist on a state monopoly and then badly mismanage the currency can do an enormous amount of

damage.

As you can imagine, the statistics going back hundreds of years aren't all that accurate; but as far as we can tell, the level of prices in general—that is, the purchasing power of the pound sterling—was about the same on the Restoration of Charles II in 1660 as it was on the outbreak of the First World War in 1914. In other words, apart from a significant blip around the time of the Napoleonic Wars, there was virtually *no* inflation for 250 years, a quarter of a millennium.

It was in 1913 that Keynes, in his first book, wrote: 'A preference for a gold currency is no longer more than a relic of a time when governments were less trustworthy in these matters than they now are ...' But governments are *not* trustworthy! One of the best bits of advice in the *Book of Common Prayer* says: 'Put not your trust in princes.'

The modern period has been very different. In sixty years since 1947, when the modern Retail Prices Index started, prices have multiplied nearly thirty times at an average inflation rate of just under 6% a year. In other words, over that period the pound's lost about 96½% of its purchasing power. That's completely unprecedented in sterling's thousand-year history. And a reminder of the incompetence, or worse, of a state monopoly in currency.

The word 'government' comes from *gubernetes*, the Greek for 'steersman'. I was born and grew up in Henley-on-Thames, famous for its Regatta. So from an early age I was familiar with the idea of a rowing eight, that is eight oarsmen steered by a cox. With tax now taking about 45% of the national income, the analogy that springs to my mind is that of a boat with *four* coxes and only five oarsmen! That's what the current level of 'over-government' means to me. Of course a rowing man might protest: if you had five oarsmen, with three on one side of the boat and two on the other, that would mean the boat going round in circles—to which I'd reply: yes, that sounds like modern British governments all right!

The public sector nowadays provides four differ-

ent kinds of things:

- Public goods, such as ‘defence’ or ‘regulation’.
- Welfare services, such as ‘health’ or ‘schooling’ provided more or less ‘free’.
- Services from nationalised industries such as the Post Office or London Transport, which charge prices, but which survive even if they make losses year after year.
- ‘Transfer payments’, that is cash payments to individuals. As a result there’s a huge amount of ‘churning’: people paying taxes in order to receive social security benefits—after the administration has deducted an enormous ‘service charge’!

Decisions about ‘what sort of services?’ and ‘how much of them?’ are essentially political. In the public sector, profit is absent, both as an *incentive*, and as a *measure of effectiveness*. Instead you tend to have ‘targets’ as proxies for ultimate objectives. But it’s politicians, not customers, who decide what to target. An article in the *Financial Times* recently was headlined: ‘Time for Darling to enforce more efficiency’; but the fact is governments don’t have the right incentives to be efficient. Their *incentives* make them irresponsible.

The Welfare State

I started arguing the welfare state should be abolished more than forty years ago now. In those days, people thought I was wicked. Now they don’t think that, they just think it’s impracticable. So we’re making progress!

Total government spending takes about 45% of the national income; of which two-thirds is on the welfare state, and one-third on everything else: interest on the national debt, defence, law and order, tax collection, and so on. So government spending on the welfare state takes about 30% of the national income.

It would be nice to think you could simply cut out waste in government spending to save money; but there are problems with that:

- First, it’s not always easy to identify ‘waste’.
- Second, even if you can, cutting it out isn’t

easy given the political objections.

- And finally, even if you do manage to cut out waste, in the government system it’s almost bound to creep back in again.

If you want to reduce taxes (as I do!), to reduce the extent of government coercion, you’ve got to find some way of permanently cutting out a big chunk of government spending. And the obvious way is to denationalise much of the welfare state, where most of the spending is. I believe we’d have far *more* welfare if we had far *less* state!

There *were* schools in this country before the government interfered. By providing free education the state crowded out fee-paying schools. The Newcastle Commission found that more than 95% of all children were receiving schooling in 1861; and a few years later W.E. Forster said: ‘We must take care not to destroy the existing system.’ But that’s largely what the state did, knowingly; and it’s what the new *Charities Act* is about to do, again deliberately, with the remaining independent schools.

There had been hospitals for centuries, mostly founded as charitable institutions. In London alone, for example, five new general hospitals were created between 1720 and 1750: Westminster, St. George’s, the London Hospital, the Middlesex Infirmary and Guy’s—to add to Barts and St. Thomas’s which already existed. But in 1948 the National Health Service simply nationalised them. It was the greatest expropriation by the state since Henry VIII’s dissolution of the monasteries in the 16th century.

After 1905 the Liberal government introduced state pensions, led by Lloyd George and Winston Churchill. Despite the total cost, it’s clear the current state pension is totally inadequate. There’s an interesting chart in the *First Report* of the Turner Commission on Pensions. It summarised a survey asking people “who they trusted not to let them down on pensions”. 67% said they trusted *employers*, while 27% didn’t—a net score of plus 40%. A net plus 14% trusted *pension providers*. And *government*? Their net score was minus 66%!

Keynes said government should only provide

those things which nobody provides if the state doesn't. I don't count welfare services, such as education, health and pensions, as public goods proper, since in principle one could charge for them. They're what Arthur Seldon called 'public goods improper'!

The present welfare state system is socially divisive, because only the very well-off can afford to opt out of state provision by paying *twice*—once for their own welfare services and then again in taxes for their compulsory contribution to the state system. The way to go is to get the benefits of the market—competition, innovation, incentives, enterprise—for everybody. For the many not just the few!

As a start, a voucher system, rather like they have in Sweden in education, would allow consumers to 'top up' their vouchers and choose private provision from competing producers. It would mean the government using tax money to *finance* health and education but not actually *providing* the services. That would surely increase the total *amount* spent on education and health, and would also be likely to improve the *quality* of spending. It would give *customers* a genuine *choice*, and it would provide *competition* for *producers*. These are two of the key aspects of a market; and two of the things that state monopolies don't allow.

And state monopolies are *risky*. They're now changing how they teach people to read back to the traditional way, after imposing a much worse system on generations of children in state schools. But how costly that wrong central decision years ago has been! In contrast, competition tends to spread best practice, and allows trial and error. Government spending focuses on *inputs*, while the market lives and dies by *outputs*.

A voucher system wouldn't *reduce* government spending, so it wouldn't yet enable you to cut taxes. The next step would be to withdraw most, if not all, of the vouchers and cut taxes significantly. My philosophy is that most people can be expected to pay for themselves over their lifetime. After all, what's the alternative? That some people have a right not to pay their own way, but to live at everyone else's expense? I find

that very hard to justify.

And free societies have three mechanisms to help:

- 1) Intra-family transfers. Your parents provided for you while you were a child, and then you'll do the same for your children when you become a parent.
- 2) The capital markets. Most people borrow to buy a house when they're young and poor, then repay the mortgage loan when they're older and richer.
- 3) Charity. People who are down on their luck may need financial help. As a rule, the first port of call will be their family. But if necessary a civilised society will provide either money or benefits in kind from 'external' sources. A key question is whether this should be voluntary charity or what I call coercive charity, financed out of taxes.

I prefer *voluntary* charity, for three reasons:

- 1) It's likely to be more effective.
- 2) It allows taxes to come down.
- 3) It avoids having half the population (in some areas) on the state payroll.

But even I accept that, in the extreme, some coercive redistribution via taxes may still be necessary. But this would be a last resort, and in total on a very modest scale.

In principle it's better to give money and let the recipients themselves choose how to spend it. The poor may need freedom in this respect even more than people who're better off. When you're spending your own money, you tend to be more careful and—very important—you *learn* from your mistakes. In contrast, the welfare state's an *irresponsible* society because it separates in people's minds the concept of getting *benefits* from the concept of *paying* for them. Moreover it keeps people in a permanent state of dependence.

How would private provision work in detail, in education and health and pensions? *I don't know*. Free markets and competition aren't predictable: Hayek called competition 'a discovery procedure'. I appreciate that those who started the welfare state, and many of those who continue to

support it, have good intentions. They're not 'do-gooders'—but they're often 'mean-wellers'! But we supporters of *laissez-faire mean well too!*

What about the argument that, as Douglas Jay said: "The gentleman in Whitehall really does know better what is good for people than the people know themselves." We need to recall how that quotation began: "Housewives as a whole cannot be trusted to buy all the right things, where nutrition and health are concerned. This is really no more than an extension of the principle according to which the housewife herself would not trust a child of four to select the week's purchases." *A child of four!* If that were true—then government could simply publish its 'superior' information—and let individuals choose.

The logic of that paternalistic attitude is: why allow people who can't even look after themselves to vote on who should govern them? As Herbert Spencer remarked: "The ultimate result of shielding man from the effects of folly is to fill the world with fools."

In the market system people make millions of separate choices every day between competing suppliers. In contrast, government monopolies often allow little or no choice. In the political system you get one vote every four or five years between so-called 'rivals' whose policies often seem very hard to distinguish. Those of us who've been following the arguments over the new *European Treaty* know that governments don't always *keep* the promises they make in their election manifestos. Unlike commercial contracts in the market system, political promises aren't enforceable at law.

What really matters is what *kind* of government we've got, not how you choose which party is to form the government. The essential is to *limit* the government's powers. Government is coercive whereas the free market is voluntary. People normally expect to be better off as a result of voluntary exchanges: otherwise why would they enter into them? The Greek word *catalassein*, which means 'to exchange', also means 'to turn from enemy into friend'—an interesting illustration of the fact that the *market is peaceful*, it's ag-

gressive *governments* that so often seem to make war.

The Nanny State

I believe modern Western governments are deliberately using fear of terrorism as an excuse to increase the power of the State. In July 2005, 52 people were murdered in London, in four related terrorist attacks. But it's absurd to talk about a 'war' on terror. In the Second World War, Britain lost 380,000 military personnel and 70,000 civilians. Deaths from that war amounted on average to *more than 200 people every day* for nearly six years—more than *four times* as many as died on that single day of terrorism in London.

If fifty people died from some natural disaster, or from a bad train crash, a normal robust society could easily survive it. What makes terrorist atrocities so awful is the *malice* behind them. But let's keep a sense of proportion and not throw away civil liberties that have taken generations to build up. And let's remember, as I mentioned earlier, that it can be very hard to uproot emergency legislation once it's been enacted.

The recent proposal to imprison suspected terrorists for as much as 90 days without trial, without even any charge, may yet resurface. In my opinion even 28 days incarceration is far too long for a free society. And if that remains on the Statute Book I dare say it'll be used for all sorts of other offences before long. It shouldn't be necessary to point out that in this country people accused by the state are innocent until proved guilty.

One of the great virtues of jury trials is that juries can deliver so-called 'perverse' verdicts if they think a government prosecution is unfair. That's why when you could be hanged for stealing a sheep, not many people were convicted of it. It's a sinister development that the government is thinking of abolishing jury trials, or at least restricting, their scope.

Quite apart from all the taxes and the regulations, modern governments seem to think everything is their business. They're operating a Nanny State. The government's attitude so often seems to be: 'Go and see what little Johnny is

doing and tell him he mustn't! There are CCTV cameras all over the place. It almost makes one wonder if Orwell's *1984* vision of state snooping in every home is so far off the mark.

Whenever I see my GP I always say something like: 'Thank you very much for your advice: I'll think carefully whether to take it or not.' I'm *teasing* her because we both know she doesn't think she's giving me advice: she thinks she's giving me instructions! Am I eating five pieces of fruit every day? Am I drinking more than however many units of alcohol I'm allowed a day? (Whatever a 'unit' is—I've never managed to work it out!) Am I getting too fat? (Or 'obese'—not a word I normally use!) I haven't yet noticed the obesity police on the streets, but it can't be long.

In my view it's the government that's obese. Grossly overweight. It was reasonably slim in 1880, taking less than 10% of the national income in taxes. I regard that as government's natural size. Now it's become greedy, elbowing everyone else out of the way in its determination to get its snout in the trough.

Moreover a view which Macaulay criticised in 1830 has since become all-pervading, the idea 'that a government approaches nearer and nearer to perfection, in proportion as it interferes more and more with the habits and notions of individuals'. In my block of flats, there's a sign saying 'No smoking in this building'—a gross infringement of individual freedom. What else would they like to forbid but don't yet quite have the nerve for?

A free society is tolerant. We may not approve of everything other people do or say or think; but that needn't mean we want to forbid them from doing it. In this country, as a general rule, everything is permitted that is not specifically forbidden. When I was at prep school we had an abbreviation: 'MYOB'—Mind Your Own Business. Of course now I'm grown-up, I'm far too polite to use such a phrase—but my goodness I think it every day where the government's concerned!

The Institute of Economic Affairs has just pub-

lished a book discussing government prohibitions on various things like alcohol, drugs, gambling, advertising, boxing, firearms, pornography and prostitution. Its conclusion is that government prohibitions usually do more harm than good, quite apart from restricting individual freedom.

Conclusion

My conclusion is that the extent of government in this country has grown enormously in the last 125 years or so; from about 7½% to about 45% of the economy. And there's no sign of any significant reduction any time soon. The Opposition is so 'responsible'—or so desperate for power!—that it won't promise any tax cuts, even from present levels.

If we want to reduce the heavy burden of taxation, which distorts the market, penalises enterprise and reduces freedom, there have to be significant cuts in government spending. And the main reductions must be on the welfare state, which now accounts for two thirds of government spending. To do that, we need the political will, which there's little sign of.

Even apart from taxes, government interference—and over-regulation and snooping and bossing us all about—infects nearly every area of everyday life. So if I'm asked whether we'd be better off with less government, with a slimmer government, instead of the grotesquely overweight monstrosity we've got at the moment. I can only answer yes. Of course we would!