

# Three Theories of Rent

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[This is the second and final instalment of the article, the first having appeared in the May—June, 1941 issue. We take this occasion to correct two typographical errors in that part of the article heretofore published: on page 95, 6th line from top of second column, the word "normal" should read "moral"; on page 96, 28th line from top of second column, the word "ascertain" should read "ascribe." Immediately following this concluding instalment will be found an article entitled "In Defense of Ricardo," a comment on the views of Mr. McNally.—ED.]

## The Realists

THE realists are neither moralists nor psychologists. Their method is purely scientific. They insist upon a strictly literal explanation of economic life as *it is today*. In discussing the market, they have in mind only one kind—namely, that which operates today. They regard it as the area in which men bid for the goods and services that other men have to sell. The mere presence of goods and services does not give them value. Human labor alone does not create value. There must be a demand for them. But the mere bidding on the part of buyers is not enough. To have value, the goods and services must be *actually sold*. Before sale, they can have only a potential or speculative value. Every business consists of a buying and production department and an administrative and selling department. Some business concerns of course do not make things themselves but buy them ready-made from other establishments, and their only production activities, if any, consist in getting them ready for sale. Although the owners of businesses supervise the production and buying, their chief personal functions are those of administration and selling. Goods and services may be produced, but they cannot reach the hands of consumers and have value until they are sold. They are sold for money or credit by means of which other goods and services are obtained, either immediately or later, in exchange for those that have been sold. In the market, buyers are free to refuse to pay the price demanded by sellers, and, on the other hand, sellers are free to refuse the price offered by buyers. Neither the buyers nor the sellers coerce or compel each other. Unless this freedom prevails, there is no market and thus no value.

Now just as private services must be bought if people want to obtain them, so public services must be bought if people want to receive them. To receive the latter, one must occupy a certain portion of land, for these services are only delivered to sites or locations and are sold to the occupants by landowners. The payment is called rent. Rent or the value of land, therefore, is based on public services and on nothing else. The landowners do not sell or rent land as such but only the public facilities that attach

to land. If these facilities were obtained direct from the government, they would not be services but *privileges* or *benefits*. To constitute services they must be obtained by purchase through the democratic process of the market. The government officials cannot sell the public facilities, for they are not in the market. Why they cannot possibly be in the market I shall explain later.

The value of the public services is determined by the bargaining that takes place in the market between the landowners and the occupants of the sites. We observe that the landowner and the user of the site enter into a free contract, neither coercing or threatening the other. The tenant is free to refuse to pay the rent demanded, for not only does the landowner not coerce him, but the landowner has no monopoly of public services. The tenant can obtain them at other sites. And by the same token, the landowner is free to refuse the rent offered by the tenant. There is more than one tenant. This is democracy at its best. And so we see that rent is not an arbitrary payment like a tax but is fixed by the competition of the market. The tenant pays only what he believes the services are worth to him.

The public servants comprise the production department of the public service business, while the landowners comprise the administrative and selling department. The former receive stipulated salaries and wages, but unlike the employees of a private business, they fix their own compensations and pay themselves out of the wealth they seize from the people through taxation. They do not receive them from the owners of the public capital by any exchange of services. The landowners, on the other hand, receive their compensation in the market by virtue of their service in selling the public services to site-users. This compensation constitutes the profits of the public service business which remain after all the costs, consisting of the wages of the public employees and the interest on the borrowed capital plus all other costs of depreciation and obsolescence, have been met. The net income or net rent left in the hands of the landowners when capitalized at the current rate of interest gives the capital value of land. This capital value of land is nothing else but the value of the *public capital*.

To the extent of merchandising the public services to site-users, the landowners are the owners or administrators of the public capital. Unlike the owners of private capital, they fail to supervise the employees of the production department. The result is irresponsible government and bureaucracy, for these employees are responsible today, not to the owners of the public capital, but to the electorate, or to be more precise, to the pressure-groups to whom they



grant privileges and subsidies in order to maintain themselves in office. These privileges and subsidies call for taxes in addition to those deemed necessary to provide compensation for the public employees. All these taxes, including those used to compensate the public employees, reduce by that amount the value of the public services to site-users and less rent is paid. But the burden on the site-user is not only the amount of the taxes he pays but the loss caused by the indirect cost of taxation—that is, by the methods used to collect taxes and the restrictions and regulations imposed on his business directly or indirectly by the manner in which the tax funds are spent. Thus the site-user is still further impoverished, and the amount of rent he pays is even more reduced. He does not pay twice for public services, once in rent and again in taxes, as the neo-Ricardians claim. Taxes are a charge against rent. The landowners today do not pay the wages of the public employees and the costs incidental to the maintenance and the borrowing of the public capital directly. These are paid out of the taxes collected from site-users. Not all the taxes, however, are used to finance the public services. Some of the funds are wasted, and a large part of them goes to finance *disservices* such as subsidies and various ventures for the regulation of and, consequently, interference with private enterprise. But the landowners do pay the public expenses *indirectly* when their rent is reduced by the taxes levied on their tenants. If all taxes were abolished, landowners could pay the public expenses directly, because rent would be increased by at least the amount of those taxes. In fact, they would have to pay them and also to see that the funds were spent as effectively as possible, for otherwise there would be no public services and consequently no rent. And it is reasonable to assume that it would be to their advantage not only to do this but also to supervise the public employees and to extend their administrative functions in connection with the public capital, for the abolition of taxes together with their concomitant indirect costs arising out of the restrictive and punitive methods of collecting them and the waste and inefficiency and the devastation of private enterprise involved in the spending of them, would enable site-users to pay more rent and thus to increase the landowners' profits. The realists, however, are careful enough to point out that landowners are no more aware of their real functions and the true nature of rent than are other people.

In order to see more clearly why the site-user does not pay twice for public services, let us turn our attention to private enterprise for an illustration. If a furniture establishment, for instance, were to conduct its affairs as the public service business is conducted, it would soon go into bankruptcy. If the owner failed to supervise and pay the employees and allowed them to compensate themselves by seizing the wealth of his customers, his income would fall

off. His customers, being in reduced circumstances as a result of the depredations of the employees, would not and could not possibly pay twice for the furniture. If a bedroom suite cost \$1,000 to make and to sell and the employees seized \$500 from each customer for their compensation, the customer would pay only \$500 to the owner for the suite. He would pay the difference between the total cost of the suite and the amount seized from him by the employees. In other words, what he would pay would be equivalent to the value of only the administrative and selling services of the owner himself. The same thing is true of public services. The rent the site-user pays today represents not the total cost of the public services (for part of them is financed by taxes—the part that I term the production department) but only the value of the landowner's services fixed by the market plus the amount of taxes that are now levied on the value of land and the wages of any private employees he may have. It is doubtful whether the owner of the furniture factory would receive as much as \$500 for the bedroom suite, for the manner in which the employees would seize the customer's wealth would impoverish the customer by more than the actual amount seized. If these seizures continued, the owner's income would steadily decline until he was forced out of business.

I wish to refer now to the statement that I previously made that government officials cannot sell the public facilities because they are *not in the market*. Only the owners of capital, whether public or private, from the use of which services flow, can sell those services. Government officials do not own the public capital, not even as representatives of the electorate. The masses of the people are consumers of the public services and they cannot also be owners of the things they buy. That would be like a lawyer acting as his own client or a storekeeper acting as his own customer. It might be said that they are owners in the collective sense and consumers in the individual sense; but then there is something else to consider. The owners of capital receive the income from it, but the masses of the people do not receive any income from the public capital. Furthermore, the citizens of a country cannot exercise proper supervision over the public servants, because there is no unity among them. They have many different interests, and each one seeks his own welfare, not the welfare of all. Government, therefore, is responsible only to the strongest pressure-groups, and the particular interests of each conflict with those of the others. The owners of a private business may at times disagree on policies, but they are all united for their common good by a common interest—their income. The citizens receive no income from the public capital and, therefore, have no unity of purpose. And being divided against one another, their only *direct* interest in government lies in the favors that are doled out to them. Their *indirect* interest concerns itself with the public services, but these



they buy in the market direct from landowners as occupants of sites. The public servants have no contact with the market. They could only be brought into the market and made responsible through the medium of landowners if all taxes were abolished and they received their compensation direct from landowners out of the increased rent that would result.

### Recapitulation

The rent we have been discussing is ground rent as distinguished from the rent that is paid for the use of a building or a machine. We have seen that rent is not paid for land as such nor for the natural advantages attaching to land. Rent is paid for those advantages of location that cannot be dissipated or equalized by exchange—namely, the public services, such as public highways, sewerage systems, police and fire protection, etc. It is determined by the competition of the market and is a *voluntary* payment to the landowner. It cannot be paid direct to public officials, for then it would be a tax. Taxes are always paid *under compulsion*. Those who advocate paying rent direct to public officials or who advocate taxing the value of land (which would require public assessments) are in effect demanding that we scrap part of the exchange system—that part which concerns itself with public services—and that we place ourselves *to that extent* under the domination of the state. They are dangerously close to the Marxist who demands that the *entire* exchange system be scrapped and that we place ourselves *entirely* under the domination of the state.

The realists, on the other hand, favor extending the exchange system or, in other words, the democratic way of life, so as to bring the public servants within its scope and make them responsible individuals. They contend that private *property* in land as distinguished from mere private *possession* must be maintained, as private property in land is the bulwark that protects private enterprise from the encroachments of bureaucracy. Destroy private property in land, they say, and the trend toward state socialism would be accelerated.

Some people honestly fear private property in land because they believe that it leads to the holding of land out of use. They view the problem of poverty and unemployment as a land question. This view is invalid because there is no scarcity of land in the aggregate. There is a scarcity of certain types of land or locations but so is there a scarcity of certain kinds of skilled labor. Furthermore, to say that land is held out of use is to set themselves up as arbiters of what rent the landowner must accept. This attitude leads them to demand that land be taxed into use. This is the attitude of the fascist who has little or no understanding of the basic principles of the exchange system. We cannot force the production of wealth. Production is

a voluntary process. Forcing land into use is only one step removed from forcing employers to pay minimum wages or forcing industry to charge prices fixed by the state. It lessens rather than increases the production of wealth. Landowners as a class are anxious to receive an income from their land, and they can only receive it if they rent their land to those who are able and willing to use it. Some landowners of course have very poor business sense, and their land lies idle because they demand too high a rent. This does not force men to go without land, for they merely take some other location. Nor does it compel them necessarily to go to poorer locations, for the owners of the poorest locations sometimes demand so high a rent that producers move on to better locations. If we are to maintain the democratic process of the market, landowners must be accorded the same freedom to refuse the rent offered as site-users enjoy to refuse to pay the rent that is asked. Otherwise there can be no rent. Rent is established by the bargaining process, and there must be freedom on both sides.

We cannot *force* land into use, but we can *increase the demand* for land by abolishing all the taxes and restraints that are depressing industry. When industry is depressed, it uses less land, rent falls, and landowners are inclined in some cases to wait until the demand revives rather than rent their land at too low a figure. Whether land is ever actually held out of use is a matter for the psychologist to determine. Not concerning himself with psychology, all the economist knows is that land is *driven out* of use by taxes and bureaucratic interference with private enterprise. Private property in land today is gradually being destroyed, and land is rapidly passing from private hands into the clutches of the state as a result of the heavy taxes that bear on industry and on land itself. We can scarcely imagine the heights to which civilization could rise, the stimulus to invention and productive effort, the flowering of the arts and the increased mental and physical vitality that would result, were industry freed of bureaucratic restrictions and society purged of political corruption and inefficiency. And it must be definitely stated here that the resultant advantages would not be absorbed by rent, as the Ricardians claim, for as I previously pointed out, rent is not fixed by the "margin." No one would bid for any location if all of the advantages were absorbed by rent.

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A great deal more can be written on this subject, and I realize that many questions may arise in the reader's mind that I have not specifically answered. However, I believe that the thoughtful reader will find that I have anticipated some of them at least, if only by rather broad strokes. My chief purpose has been to stimulate thought on this very important subject.