

BOOMS WITHOUT BUBBLES

Selling Land Tax to Land Owners

by Gavin Putland

Land owners should support a high rate of land tax to finance the infrastructure that increases the value of their land.

The infrastructure would be built, not because politicians can be trusted to spend any additional revenue on infrastructure, but because the additional revenue *depends* on the infrastructure: each infrastructure project would *pay for itself* (and more) through the increases in land values that it causes, provided that the project satisfies the condition

$$g > 1 + it$$

where t is the marginal LVT rate, i is the discounting rate, and g is the ratio of the total taxable uplift in land values to the cost of the project, the word "taxable" allowing for any thresholds and exemptions. If the LVT rate (t) increases, the required value of g decreases, so the self-funding criterion is easier to satisfy, so more projects go ahead, causing more increases in land values.

If you are a land owner, your tax bill does not increase unless the market value of your land increases, and the market value of your land does not increase unless, in the judgment of the market, you are better off in spite of the tax. So you can't lose because of higher tax bills.

This argument applies to a conventional LVT computed on the capitalized value of the land, with or without a threshold. It does not apply to a Mill tax or a full site rent system, both of which attempt to prevent any increase in capitalized values. So as long as we are content to advocate high rates and fewer exemptions for LVT, we should be able to count the landed class not as our greatest enemy, but as our most important ally.

The first strategic goal in the geoist project must therefore be the implementation of the strongest possible LVT. I say this for at least four reasons.



First, it may be that we cannot achieve anything without the support or tolerance of the landed class, and that the necessary degree of support or tolerance will not be forthcoming for any geoist policy beyond a strengthened LVT for funding infrastructure. In other words, it may be that the LVT-for-infrastructure policy is as far as we can go, in which case, if we reject that option, we consign ourselves to oblivion.

Second, for a given LVT rate, the fraction of ground rents taken in tax is inversely related to the prevailing interest rate and approaches 100 percent as the real interest rate approaches zero; and the disinflationary effect of the initial change in the tax mix would allow a loosening of monetary policy, perhaps causing real interest

rates to fall. (Why only "perhaps"? Because the LVT-for-infrastructure policy would make land a better investment, and the return to land is a benchmark for interest rates.) So it may be that a seemingly moderate LVT rate would collect enough of the rental value of land to defray the whole cost of government.

Third, even if it is desirable and politically possible to move beyond LVT to a Mill tax or full site rent system, it may be necessary to demonstrate the benefits of the least radical option (LVT) first, so that more radical options can be promoted as "more of the same".

Fourth, putting aside all "it may be" arguments, it is clear that a strengthened LVT would be a step in the right direction.

Nevertheless, an alliance between geoists and land owners would be a novelty for both sides, and its maintenance would require sensitivity and tact -- especially from the side taking the initiative. Accordingly, I now attempt an issue-by-issue survey of geoist rhetoric and how it can be modified so as not to alienate powerful friends. I do this with some trepidation, because the idea of an alliance with property owners is almost as new to me as it is to most of my readers, and my thinking on the subject continues to evolve. But the attempt must be made. If I only manage to start a debate, it's a debate that we had to have.

MORAL FOUNDATIONS

The LVT-for-infrastructure model not only accepts private property in

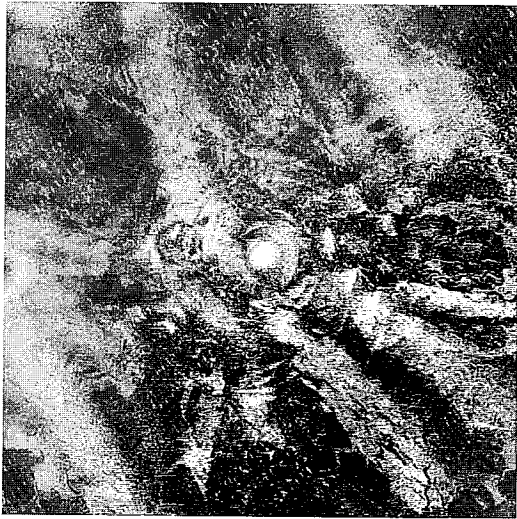
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land and the private appropriation of unearned increments in land values, but even offers more unearned increments as a political carrot. Fortunately, however, it is possible to defend the geoist project on purely economic grounds, without

taking any controversial moral stand. So:

DON'T attack private property in land, capitalization of land values, or private appropriation of increases in land values on moral-philosophical grounds.

DO point out that because neither land nor its value is created by the owner, taxes on land values cannot deter production and therefore cannot cause inflation or deadweight. If someone questions the morality of "confiscating" part of the unearned increment, respond that it is



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surely better to confiscate unearned windfalls than to confiscate the fruits of labour.

Of course, some of what purports to be moral opposition to land taxation is actually driven by pecuniary interests, and will therefore not be heard from land owners who understand that they would benefit from our policies. Therefore, in statements intended for non-specialist consumption:

DON'T anticipate objections such as the "poor widow", or the assertion that property taxes should pay only for services to property, or the claim that land cannot be separately valued.

DO answer such objections if others raise them, and direct the answers at land owners and their associations, who of course have an incentive to

defend the LVT-for-infrastructure policy against such objections.

LAND SPECULATION

Here we seem to face a contradiction. On one hand, we know that land speculation prices productive land users out of the market; on the other, promising capital gains due to infrastructure looks like pandering to the speculative motive. But if the LVT-for-infrastructure policy is a step in the right direction, it must reduce speculation and its ill effects; and if the same policy increases land values, it must be possible to put a pro-land-owner spin on that reduction of speculation. A possible approach is as follows:

DON'T define speculation simply as the pursuit of capital gains.

DO define speculation as putting faith in the greater fool and failing to associate capital gains with growth in real or imputed income, which in turn is caused by, among other things, improving infrastructure.

DON'T characterize speculators as bidding up land prices to the detriment of potential owner-occupiers.

DO characterize speculators as failing to make the most productive use of land on which capital gains are sought, thus restricting the availability of land to productive users, and increasing the cost of access for those users but reducing the overall returns to land.

DON'T characterize land tax as discouraging people from acquiring land that they don't intend to use productively.

DO characterize land tax as requiring people to make productive use of whatever land they acquire, so that they earn income in proportion to the capitalized value of the land.

In other words, define the problem negatively and the solution positively, not the other way around.

SPRAWL

Causes of sprawl include:

(a) The need to leapfrog over vacant land held by speculators;

(b) Opposition to infill development for fear of devaluation of surrounding land.

Point (a) is addressed under the preceding heading. The standard geoist answer to (b) is that any form of land value taxation gives at least partial compensation to those whose property is devalued by planning decisions, and that it's a bit hard to compensate the losers if you don't also tax the winners, albeit only of part of their winnings. This answer is already aimed squarely at property owners and does not need to be modified for the LVT-for-infrastructure approach, except to admit that LVT, by itself, gives only partial compensation.

OWNER-OCCUPIERS

Investors will want to bring owner-occupied principal residences into the tax net in order to maximize the taxable increase in land values for each project, thus maximizing the number of infrastructure projects that pay for themselves, and/or minimizing the LVT rate required to make a given project self-funding. To retain the support of investors, who are the more powerful faction, we must propose to bring owner-occupiers into the net somehow, and must sell that policy to owner-occupiers. Fortunately this can be done without difficulty or dishonesty:

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DON'T completely deny that owner-occupiers gain from increases in land values.

DO make a distinction between speculative bubbles and the benefits of infrastructure, pointing out that

speculative increases in land values do not reflect increases in amenity and are offset by higher prices of alternative sites in other areas, whereas increases due to infrastructure are accompanied by increases in amenity and are confined to localities serviced by the infrastructure, so that the owners can either enjoy the increased amenity or sell and move at a profit.



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Note: The above distinction is spelt out for the first time in our submission to the Queensland electricity review (<http://grputland.com/subs/pavedsd.htm>). In earlier writings I have denied that home owner-occupiers benefit from property bubbles, but the restrictive context may not have been obvious.

COMPLIANCE COSTS

No taxpayer -- not even a parasitic land speculator -- likes compliance costs. So:

DON'T forget property investors when complaining about compliance costs.

DO point out that it is more convenient for a small-time property investor to pay a land tax bill than to keep records of rental income, interest, depreciation of buildings and fittings, other rental deductions, capital gains, capital expenditure, stamp duty, etc.

RATING SYSTEMS

Concerning the argument about capital-improved-value (CIV) vs. site-value (SV) rating:

DON'T trumpet the conventional geoist line about CIV giving a lower rate to developers and speculators at the expense of home owners. (But equally well, don't complain if developers and speculators trumpet the same line in view of the following.)

DO explain that because new infrastructure adds to land values but not building values, rates on land values encourage governments to provide infrastructure, while rates on building values do not; hence, for the property owner who wants the infrastructure, SV rating is a better investment.

HOUSING AFFORDABILITY

Concerning renters and first home buyers:

DON'T complain about first-time buyers being priced out of the market by investors.

DO point out that LVT forces land owners, including investors, to build on their land and add to the supply of housing, improving the competitive position of first-time buyers and tenants relative to sellers and landlords. After all, Howard and Costello get away with similar talk in relation to negative gearing.

DON'T talk in terms of reducing prices and rents.

DO talk in terms of tax reforms that allow faster economic growth, of which the benefit can be shared between all parties, so that improving both the absolute and relative positions of buyers and tenants can

leave sellers and landlords better off in absolute terms, although not in relative terms.

INFLATION

The present tax system is inflationary because (a) the under-taxation of land-like assets leads to speculative bubbles, which in turn increase the money supply as people borrow against speculative asset values, and (b) all productivity taxes feed into prices. In contrast, geoist taxes (a) discourage speculation, and (b) don't feed into prices. While the LVT-for-infrastructure model leads to rapidly rising asset values caused by improving infrastructure, the associated expansion of the money supply is *not* inflationary because it is accompanied by -- indeed ultimately caused by -- greater production of goods and services.

However, it may not be obvious that one cause of rising asset values is inflationary while another is not, and we certainly don't want to give property owners the impression that we are opposed to rising asset values in general. So I suggest:

DON'T emphasize borrowing against rising asset values as a cause of inflation -- but, if asked about it, explain that the cause of the rise in asset values also matters.

DO trumpet the fact that geoist taxes are not passed on in prices.

What about the fact that geoist taxes are not passed on in rents? I don't think we have to worry about that. If property owners want land tax to finance the infrastructure that increases the value of their land, they won't go around saying that land tax is passed on in rents.

INTEREST RATES

Now comes an illustration of how **some of what purports to be moral opposition to land taxation is actually driven by pecuniary interests**

the LVT-for-infrastructure paradigm takes some getting used to. On p.9 of the May-June issue, I

wrote: "Geoist land policies, by reducing the return on a major asset class, tend to reduce interest rates across the board." While that was a perfectly orthodox thing for a geoist to say, it isn't quite right, because the LVT-for-infrastructure model actually promises *increased* returns to property investors, albeit by a productive mechanism.

Of course, the disinflationary effect of geoist policies would remove the need for central banks to drive up real interest rates above the natural level, but the effect of the land market on that natural level would be positive, not negative. I'm inclined to think that the disinflationary effect would be dominant, so that long-term average interest rates would fall. But, to guarantee this, we might have to invoke other policies such as implementing monetary policy through compulsory saving rates rather than interest rates.

So at the time of writing, I'm inclined to say:

DON'T make an issue of interest; but

DO be honest with anyone else who makes an issue of it.

LESSER ROBBERS

That quote from the May-June issue is from the article "Which robber?" All of the "lesser robbers" mentioned in that article have two things in common: they stand to gain from faster economic growth, and they don't stand to lose from geoist tax reforms. Accordingly, as I said at Prosper's Annual General Meeting on May 6, they should all support the LVT-for-infrastructure model as readily as any other geoist model.

Some time later I saw a possible impediment: While we are trying to ingratiate ourselves with the land power, can we afford to have lesser robbers attacking the land power in order to deflect public criticism away from their own rent-taking? Later still, I saw what may be the solution: If the land power supports the LVT-for-infrastructure model, it can defend itself by saying, "We share our economic rent with the community through LVT. How do you share yours?" To which the lesser robbers might respond, "But you still take more rent than we do, even after tax!" But as long as both sides are using geoist arguments and espousing geoist policies, that is not our problem.

Of course it would be unethical and suicidal for a single geoist organization to be advising both sides of that debate. But there is no ethical reason why there should not be some individual geoists on one side and others on the other side -- or, for that matter, one geoist organization on one side and another on the other side. After all, we are used to a political landscape in which the Radicals purport to represent labour, and the Tories purport to represent capital, and the land power controls both sides of the debate. Perhaps, in the political landscape of the future, the Radicals will be the lesser robbers, campaigning for a Mill tax or full site rent collection, while the Tories will be the land power, defending the established LVT-for-infrastructure policy and demanding tighter controls on the lesser rent-takers. And geoists will control both sides of the debate. ■



Mr. Ed managed to get this article in the Winter 2004 edition of the Victorian Greens News

THE ULTIMATE ECO-TAX

Countless indigenous peoples and social philosophers throughout history have reiterated the ageless wisdom that it's plain wrong to own land. Land is the gift of nature, and should be the equal and common birthright of all humanity, yet we find that it's bought, sold, and monopolised like a mere commodity.

We don't just refer to agricultural land. The locational value of urban land is built up by the amenities and services provided by the surrounding population and its tax-funded infrastructure. By rights, land-owners should repay society for their exclusive use of such valuable land, and a system of regularly assessed land value taxation (some call it community ground rent) is the elegantly-simple means.

By tapping into this natural and equitable form of public finance, we would be able to phase out punitive taxes on honest (i.e. non-speculative) wealth production. In other words, "Pay for what you take, not what you make".

Henry George (1839-97) is the inspiration for a revived Georgist (or Geoist) movement which has again taken up this noble cause, and is calling on fellow Greens to go further in their proposed tax reforms. As well the current eco-taxes on air, water, logging, mining and fishing rights, we should be advocating taxes on users of:

- land
- the electromagnetic spectra
- air flight paths and geostationary orbits
- any other part of the Global Common (e.g. as the Dark Night Society proposes, there should be a tax on annoying security spotlights, on stadium lights which upset nocturnal animals, and on any lights which obscure the stars)

But land is the Biggie. Because of its unique qualities, land value taxation (LVT) encourages us to put land to its optimal use thereby minimising urban sprawl and wasteful agricultural practices. Similarly, LVT prevents land speculators from holding land idle in the expectation of future, ill-gotten gains.

At the moment, we're born on to a planet where "all the seats are taken" so that we have to pay the former generation for permission to live. Rising land prices are not "healthy" or "buoyant" for the economy -- rather, it makes the whole problem worse. However, when society collects the full rent of land, the market price of the land (not the improvements on top of it) will have been reduced to around zero (brevity disallows an explanation).

When the economy is turned right-side-up, there are lots more spin-offs, including important environmental safeguards. Furthermore, both tax collection costs and compliance costs will be a tiny fraction of the immensely wasteful burden they are today. And tax evasion will be a thing of the past -- you can't hide land!

Gone, too, will be the intrusive practices of the Tax Commissioner, prying into all aspects of our activities. We should be monitoring carefully those who use natural resources, not people's personal affairs!

We could also afford to invest in public infrastructure such as public transport, as the enhanced land values which result will be "recycled" back into the public purse, rather than enriching landowners.

We belong to the Earth, not vice-versa! ■