

LAND PROBLEMS AND THEIR SOLUTION IN THE FEDERAL REPUBLIC OF GERMANY

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I start in the year 1960. The introduction of the German Federal Building Law abolished the price control of undeveloped land. For nearly a generation, since 1935, price control had existed. Now landed property became part of the competitive profit system. From now on supply and demand would determine land value in a free market, with all its consequences. The devisers of the Federal Building Law were not happy about this courageous step even though it was the right one. They were afraid of an excessively high rise in land prices, that would be greater than the rise of all other prices, for example building costs or general expenses. This proved to be so. The supply of land of course cannot be increased and building-land can become available only on a limited scale. On the other hand, the demand for land, already high, had been increased by the millions of refugees from the eastern parts of Germany who came to the Federal Republic to find a home and a job.

As a precaution, the legislators established some instruments for controlling the trends of land prices which I have reported on at former conferences of the Union. An example was the local appraisal boards that were established to observe the real-estate market, devise standard land-price maps and make valuation reports. The real-estate market (for building land) was to be made more "transparent" to the buyer. But the local appraisal boards had and have no influence on the evolution of land values.

At former conferences I reported on the introduction of a Building Land Tax whereby land owners would be encouraged to use their land in a way the building law allowed or else to sell the land to others who were willing to build. In that way a supply could be made available on the building-land market. The basis of this tax was the very low assessed-value of 1935. Even so, this step was right to the extent that the real-estate market should be influenced by land taxes. The land-value was certainly too low. Nonetheless it aroused opposition and the representatives of the landed interests went to the legislators and called for its abolition. And in a short time it was abolished.

Since then people have inveighed against land speculation, and the millions of profits from land that flow into the pockets of the land owners while society pays the taxes. In town-planning projects the profits are returned to private ownership while the losses are socialised. People therefore demand that excess planning profits be siphoned off by the communities which produce the higher land values through their town-planning.

A draft of a Bill was presented which aimed to skim off the surplus value (arising from planning permission) at the time of the development of a property. That was politically the "Egg of Columbus". This idea sounded marvellous. But the buyer and user of the land would have had to pay this planning-surplus value. The land price would have been higher and so the total building costs would have risen. Many proposals have been made to deal with the land problem but nothing has been done and the problems are the same as they have been over the last twenty years.

#### The Situation Today

The Deutscher Stadtetag as the representative of the big German cities analysed the trend of building-land prices over many years. In Volume 1/1982, Tiemann and Huttenrauch report in detail about this trend. Their research reveals that: between 1963 and 1980, (a) living costs doubled; (b) building costs nearly tripled; (c) incomes quadrupled and (d) the prices of building-land rose sixfold in the big cities of the Federal Republic.

In the final conclusion of this research it says:

"It should be appreciated that this is not a complete investigation and that the reports are mostly from big cities. On the other hand, although in these areas the problems with land are obvious, there is no great difference in the surrounding built-up areas and on the outskirts of these cities. Even in small towns and in the countryside the trend of prices was quite similar, as federal statistics show."

The authors continue:

"An examination of the reported material shows clearly that the political activities by the communities and the federal government have not had the success hoped for. The communities themselves sold their own parcels of land generally under market prices. But this had no influence on the general trend of prices under the existing circumstances. The communities, because of their financial position and limitations, are not able to speculate in the real-estate market, that is, to buy tracts of undeveloped land when there is economic stagnation and sell in times of boom. In other words, for lack of necessary funds the cities are not able to compete with big land speculators in the property market. Even in times of a slump, existing owners, primarily farmers, are not obliged or willing to sell. A lack of inducement to sell is also obvious on the total property market, particularly because of today's market values, which are about six to seven times the taxation value and even higher in certain instances.

"Also the need of land for development will continue for a long time to come and it is therefore necessary to look for new ways in politics to tackle the land problem, so that land will be available to those who need it at prices that are not prohibitive.

"Of great importance is the fact that the accumulation of land is still one of the best investments. An important aim of land legislation has to be the freeing of the existing stock of building-land to counteract the present imbalance of the market. As development-land taxes are now no longer a point in political discussions, it will be necessary in the long term to consider alternative methods of taxing land."

#### For the Record

In 1960 the land market was set free and since then, supply and demand have determined prices. At present a high demand is faced with low supply because waiting is often more rewarding than selling. Unlike the market for reproducible goods, in the case of land demand does not increase supply. The self-interest that induces the withholding of land should be harnessed to operate in the opposite direction.

## Suggested Solution

### 1) General

For years, all political parties of the Lower House, the Federal Government and the Deutscher Städtetag have had in front of them the proposal for a tax on development land and there are now indications that this proposal is again under discussion. In fact, as a general rule, nowadays taxation is the only method taken into consideration for the solving of land problems.

My own suggestion is the introduction of a uniform land-value tax which would operate throughout the Federal Republic.

### 2) Model of a Land-Value Tax

#### i) Principle

The present land tax, increment tax and planning-value adjustment would, in effect, be absorbed into the land-value tax but the aims of the increment tax and the planning-value adjustment would be adhered to.

#### ii) Basis of Assessment

The land-value tax would be based on the real or market value of the land buildings, etc. constituting the owner's investment would be exempt from tax.

#### iii) Valuation

The market value would be established by controlled self-assessment at short intervals (generally 5 years or, in high-density areas, every 2 or 3 years).

The self-assessment values would subsequently be compared with prices actually paid and appropriate adjustments made. The next valuation, however, would again be based on self-assessment.

iv) Control of the Valuation

To make it possible to bring in this tax solution without delay the control of the first self-assessment should not be too strict; deviations of +50% from the market price should be allowed. This wide tolerance could and should be lowered for the next valuation, say to about +20%, and eventually it should be made much stricter, i.e. +10%.

v) Rate of Tax

- a) It should be possible to adapt the rate of tax (x% of the land value), by decree of the Federal Government, to current market conditions every year.
- b) The State governments should be authorised to determine areas (counties, etc.) in which the communities are permitted to decide upon a lower rate than the federal figure, but this rate must be uniform for the whole area. For rural areas with lower land values, a lower rate should automatically be possible within the framework of the overall system. In this way, the needs of the agricultural communities could be taken into account.
- c) To avoid a change in the residential (i.e. use) structure, certain areas (for instance, those with high land values) should be authorised by the controlling body to decide upon a lower rate of tax.
- d) The rate structure agreed under b) and c) would change in the same proportion as any changes made in the federal rate a).
- e) The taxpayer could apply for partial or total remission of the tax or possibly deferment until death, at which time the amount payable would come out of the estate.

vi) Compensation for Expropriation

In the case of expropriation, the compensation for a parcel of land would equal the land value on which the tax was based.

3) Criticisms

- i) The land-value tax calls for adaptation of the assessment to the current market value. This can be done relatively simply, and with minimal administration expenses, by means of controlled self-assessment. Self-assessment is still used today for tax collection by the financial authorities. Control is only needed for the "black sheep". For this control, the local appraisal boards which already exist under the federal building law could be used. Since 1960 these boards have had to collate and compare market prices throughout the Federal Republic and fix standard land prices for the different areas, this information then being recorded in the form of maps.
- ii) The administration expenses for collecting the land-value tax would be lower than those for collecting the planning-value/adjustment and the land-value increment tax under today's very complicated system of assessed values - a system which was first introduced in 1935. Under the proposed system, the administration expenses would be restricted to those for controlling the owners' self-assessment. If the self-assessment was accepted the ensuing work of tax assessment could be executed by the appropriate authority. In only a few cases would an official valuation be needed to adjust the self-assessment. Even though, in some of these cases, there would have to be recourse to legal remedies, overall a saving of staff could be expected even if the land values had to be fixed at frequent intervals.
- iii) Through adaptation of the rating to the market situation, a real steering effect on the land market would be possible, similar to the way in which the Federal Bank uses the discount rate on the money market.

- iv) Part of the ground rent and, consequently, part of the land value which had accrued largely without any effort by the landowner would be returned to the community through the land-value tax. There would be no complex planning-value adjustment, with its single skimming of the capitalised ground-rent, but a continual planning-value adjustment with continual skimming of the ground rent in the form of the land-value tax. Each increase in land values, brought about through the activities of the community, would automatically be taken into account through the continual adaptation of the tax values to the market values. In this way, the imposition of a special land-value increment tax would be unnecessary.
- v) Instead of the combination of a land tax, a land-value increment tax and a planning-value adjustment, with its aforementioned difficulties, this system would mean just one tax, the land-value tax.
- vi) As this tax is based upon the actual land value, i.e. the value of the land in accordance with its real use potential (consistent with planning regulations) without regard to existing or non-existing buildings, the speculative holding of sites would be expensive; rather would there be an incentive to put them to use. Thus, development orders would be unnecessary.
- vii) The problem of passed-on taxes would to a limited extent be solved, as plots put to their optimum use (again, consistent with planning regulations) are taxed relatively lower than improperly or non-used plots. To avoid hardship, deferment or exemption might be conceded in individual cases.
- viii) This system would eliminate the anti-social effects of the present system whereby those who expend effort and incur risk in order to effect improvements so as to put their land to its optimum use are penalised, while the lazy person just sits back and waits for higher rewards without having made any effort or taken any risks.

LVT gives direct incentive for continued improvement of already developed areas because such improvements bring in higher returns without further tax having to be paid. Thus, pressure on local government to fund reconstruction projects would generally decrease.

- ix) It is internationally accepted that LVT keeps down land prices - see the equation below:

$$\text{LAND VALUE} = \text{LAND PRICE} + \text{CAPITALIZED TAX}$$

- or -

$$\text{LAND PRICE} = \text{LAND VALUE} - \text{CAPITALIZED TAX}$$

- x) The political and legal problems of taxing non-realized profits would disappear. An effort has been made in this way to adapt the ideas of Henry George to the present and to propose an effective method of solving a highly-explosive socio-political problem. But we need patience and tenacity to carry it through.