CHAPTER TWELVE

Recoupment of Betterment by Capital Levy

This chapter, contributed principally by Nathaniel Lichfield, is based on Lichfield and Connellan's working paper *Land Value and Community Betterment Taxation in Britain: Proposals for Legislation and Practice* (2000a).

Introduction

Another method of LVT outside the ambit of annual taxation is capturing capital value by recouping development gains, but herein it is assumed that there is no appetite in present Labour Party circles to repeat the failed experiments tried by various post–World War II Labour governments.

What is favoured (following Prest 1981) is the introduction of an enhanced capital gains tax (CGT), coupled with a greenfield tax, which would help redress the balance of previous disappointments in attempting to recoup betterment for the benefit of the community by capital levy.

Background Review

Three different approaches to capital levies legislated by former Labour governments—the development charge of the Town and Country Planning Act (1947), the betterment levy of the Land Commission Act (1967), and the Development Land Tax (1976)—were scrapped after a comparatively short period by succeeding Conservative governments. Thus, no machinery was left for collecting betterment for the community. A tax on development gains (as opposed to the general capital gains tax already extant) was the only scheme for land value capture ever introduced by a Conservative government (in 1973). It in fact survived in principle when the incoming Labour government of 1974 adopted the proposal under the title development gains tax (DGT) for a limited period until it was superseded by development land tax (DLT) in 1976.

Would it be appropriate to revive any of these four approaches, either singly or in combination, but modified with the benefit of experience? The answer would appear to be *no* for the three major Labour innovations and *yes* for the combined Conservative/Labour DGT. The reasons are varied.

The DGT/CGT, introduced by a Conservative government and applied by Labour, fits more acceptably into the bilateral approach of capital gains taxes enacted earlier in the U.K. by the Finance Act of 1965. The 1965 act allowed the taxation of capital gains from the disposal of assets, including land, whether by outright sale or by the grant of a lease. As such, it has continued as an enduring feature of the British taxation system, except that it is now seen as part of general taxation and is not specific to land itself. Accordingly, some alternative approach is now looked for.

Incorporating the Capital Gains Approach

Prior to the merging of capital gains on land with general taxation, the DGT was conceived by the Conservative government and enacted in the Finance Act of 1974 by the succeeding Labour government. The complex process of tax calculation is summarised as follows:

> With effect from 17 December 1973 "Development Gains Tax" was charged whenever there was a "disposal" or "notional disposal" of land or buildings with development value or development potential. The incidence of the tax, and the amount of chargeable gain, were derived from the application of a mathematical formula.
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> The taxable gain was the least of the following.
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> 1. The disposal proceeds less 120% of the cost.
> 2. The disposal proceeds less 110% of the current use value at the date of disposal.
> 3. The full gain less the increase in current use value over the period of ownership, or since April 1965, where land was owned before that date.
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> In making these calculations a "threshold" of £10,000 (£1,000 in the case of companies) with relief up to £20,000 (£2,000 in the case of companies) was allowed. Gains calculated in accordance with this formula were taxed at Corporation Tax rates in the case of companies, and at Income Tax rates in the case of individuals. Any gains not subject to Development Gains Tax under the formula would be subject to Capital Gains Tax. In effect general and specific betterment were being distinguished with the charge to tax being made first on the specific and then on any general betterment remaining.
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> DGT became chargeable where there was a disposal of the taxpayer's interest in the land and buildings concerned. In addition, a chargeable event occurred where material development had been carried out, and the buildings were subsequently let. In these circumstances the "first letting" was to be treated as a disposal for the purposes and as giving rise to Capital Gains Tax and to DGT.

> DGT was superseded from 1 August 1974 by Development Land Tax (DLT). (MacLeary 1991, 136–137)

Extending Capital Gains Tax

Prest (1981, 176) favours working with the extant CGT, rather than introducing any revised version of DGT. We support the idea of such an extension of an existing mechanism for capturing land gains, which has recently been given a sharper edge by the amendment of the indexing procedures (see Chapter 3). If specific types of land deals were to be subjected to special taxation, it would be necessary to bring in amended legislation, perhaps an enhanced form of CGT as a higher level of tax for such targeted transactions, and make special provisions to avoid rollover procedures and with restrictions on offsetting losses (see Chapter 10).

Basically, CGT is a tax on disposals (generally calculated on the actual gain between acquisition and disposal prices) and obviously will not bite until the land changes hands. But some argue that an enhanced form of CGT could be targeted on an accrual basis: as capital values of land increase, such accruals could be taxed despite retention of ownership. Such a course would rely on a periodic valuation process with all the attendant administrative and appellate consequences. Other tactics could certainly be introduced, as Prest describes:

> If we are prepared to go as far as a special tax on all increments of land values, why does one need anything more that the existing capital gains tax?. . . One [objection] might be that a capital gains tax is a tax on realisations rather than on accruals and that the latter is preferable in principle. But. . . if realisation is accepted as the base for some land and all non-land gains why is anything more needed in the case of land gains associated with development? And if more is needed, one can consider various devices such as accrued interest from some critical date, a system of periodic valuation on the lines of the capital gains tax rules for discretionary trusts in the period 1965–71 or even the restoration of constructive realisation at death. If it were possible to argue persuasively that the rates of tax on land gains should be higher that for the generality of gains or that there should be restrictions on loss offsets this could be done without too much difficulty. And similarly, any demands for rollover provisions in respect of development gains or for indexation could be met by reference to existing practices or proposals in respect of capital gains generally. (1981, 177)

Greenfield Tax

Another possibility for recouping betterment is a greenfield tax on previously undeveloped land, usually outside the urban fringe. This was originally proposed by the Department of the Environment, Transport and the Regions in response to a debate that flowered suddenly, in 1998, when the rural lobby protested the

possibility of dramatic encroachment on greenfield land, to build housing to accommodate some 4.4–5.5 million new households that would appear between 1995 and 2016. The proceeds of the greenfield tax would be used to subsidise development in the brownfield land, which would cost more to prepare (e.g., in dealing with contamination) and might have little or even negative value. It is also interesting that the Georgist Group on Action for Land Taxation and Economic Reform (ALTER 1998, 5) regarded a greenfield tax as an interim solution pending the full implementation of LVT.

However, while attacking a proportion of the development value released by the granting of planning permission on greenfield land would appear to be a very close cousin of the philosophy behind the three earlier Labour schemes, it can be justified by a recognition that all development rights in the country are virtually nationalised (and indeed, as such, have survived the privatisation and deregulation energies of succeeding Conservative governments). From this it could be argued that a government policy to allocate the provision of the additional homes for the predicted extra households would constitute the granting of those development rights from the national estate.

From this viewpoint, it would be quite illogical and inequitable for the government to allow the owners of the greenfield sites to reap the maximum possible development values while leaving the owners of the brownfield land to cope with the site clearance and reclamation costs, which would lead them to look for public subsidy. A more logical and equitable approach calls for the very cross-subsidisation promoted. Otherwise, the government policy to further restrict development of the greenfield sites would mean that the taxpayer would have to subsidise the brownfield land development.

A brownfield subsidy would not necessarily apply to all "previously developed land." Some brownfield land could well have a positive development value (e.g., if it were redeveloped at high density). In that case, the market could be expected to find developers. Only land with negative development value would need the subsidy. The hypothecated greenfield tax could well be a major source of gap funding to make feasible the redevelopment of brownfield land with negative development value.

Capital Gains and Greenfield Tax in Combination

A CGT on land and a greenfield tax could be imposed side by side since their purpose and incidence would be different. The capital gain on land (a form of DGT) would be levied on disposal, when the profit element had been secured, and the greenfield tax would be levied when greenfield land was developed in accordance with local planning policy. It would be justified not only because the landowner would profit from the development but also because the landowner

should pay for the permission to use the state's development rights, in light of national policy. Clearly there would need to be mutual adjustments to avoid hardship, such as the charge of double taxation.

Summary

A possible addition to an annual ongoing LVT is an enhanced form of CGT perhaps coupled with a greenfield tax as a viable, contemporary method of value capture by capital levy. One reason for this proposal is that it would fit in more easily with current Labour Party thinking than past "Old Labour" ideas have.