WHY A TAX ON LAND VALUES WILL NOT RAISE LAND RENT

by **STEVEN CORD**

I FIND many opportunities to discuss land value taxation in the American history classes I teach, but one of the difficult concepts to explain quickly and clearly is why a tax on land values must be paid by the landowner, who cannot shift the tax to the land user in the form of a higher rent. The non-shiftability of the lvt is a key issue, since if the tax could be shifted it would have no beneficial economic effect.

The superficial common-sense view is that the lvt is not different from other taxes: "Why shouldn't the landowner increase his rent to cover the increased tax just as the gas companies pass on the gas tax in the form of higher gas prices to the consumer?"

Over the years I've developed an explanation for this difficult point which others might find useful. I find it effective to appeal first to authority: "All the textbooks agree on the non-shiftability of the lvt!" This stops the superficial observers, puts them on the defensive, and they are now more likely to pay attention to the basic reasons why this tax is non-shiftable (but stay clear of the technical jargon offered by the textbooks).

The best explanation, of course, is found in Ricardo's Law of Rent, so describing it is the next step I find most useful. This law states that "the rent of any piece of land is determined by the excess of its produce over that which the same application of labor and capital can secure from the least productive land in use." Since lvt cannot possibly increase this differential in production, it cannot increase either the annual rent of land or its sale price. Unfortunately, many modern minds find this law to be too speculative and abstract to be convincing, and so I have prepared this next explanation of lvt non-shiftability which some of my listeners have found more understandable because it fits in with the concrete experience.

If a land value tax is imposed, it is quite conceivable that landowners would try to maintain their accustomed income by passing on the tax increase in the form of a higher rent to their tenants. If they should try to do this, however, some of their tenants will endeavor to economize in their use of land, either by postponing their expansion plans or by using their land more intensely (e.g., by building higher skyscrapers, etc.); marginal land users will go out of business altogether and marginal builders would postpone new construction. The more the landowners try to pass on the tax, the more resistance they will meet on the part of their tenants. The demand for land will decrease thus eventually reducing land rent to the old pre-tax level.

As demand drops, so does price. In this case, the price we are talking about is the annual rent a landowner can charge his tenant. There is only one way by which the lvt could increase the land rent price, and that is by decreasing the supply of land (when supply decreases, prices rise); but the tax can have no such effect because the supply of land is constant and unchangeable.

The result, then, of lvt is that now both the landowner and the government will be sharing the former rent—the landowner getting a reduced rental income and the government getting an increased share of the rent in the form of a tax.

It is instructive to compare a tax on land values to a tax on improvements.

The latter tax *can* be passed on to the user. The owners would attempt to raise their building rents, the users would economize (e.g., by living in more crowded quarters, etc.), demand would be reduced *but so also would supply!*

Here is the nub of the difference between a land tax and a building tax. If a tax causes the demand for building to fall off, fewer buildings will be built and the decreased supply will boost prices. The effect of the decreased demand will be negated by the effect of the decreased supply, and so the rental return to the building owner will remain the same. But since a tax cannot cause a decrease in the supply of land—it is fixed—such a tax can only cause a decrease in demand, then a decrease in the landowner's return from his land—i.e., rent.

Actually, since a land value tax will force landowners to more fully utilize those land parcels which are now only partially improved or perhaps vacant altogether, this tax would increase the *effective available* supply of land on the market and therefore further reduce the land rent collected by the landowner. Instead of increasing land rent, this tax would eventually *decrease* it!

Good luck with these explanations. If your prospect is still not completely convinced, then it might help to explain this interesting idea advanced by Lawrence Abbott in his *Economics and the Modern World* (1960, p. 654):

> Instead of having to pay $10,000 for land with a $600 rental value, the 'buyer' would pay nothing, invest the $10,000 in securities, and use the dividends to pay the $600 tax!