

## Some Problems connected with the Full Collection of Economic Rent

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In 1948 the Danish Government appointed a representative and expert Parliamentary Commission charged with enquiry into a full application of the land value taxation policy—the adoption of *fuld grundskyld* as we term it in Denmark—by which the policy would be carried to the point of collecting for the common benefit the whole economic rent of land with corresponding remission of taxation on industry and trade.

In the terms of reference, as stated by the then Finance Minister, Mr. H. C. Hansen, the Commission received the following instructions:—

To elucidate the questions involved in carrying the *fuld grundskyld* into effect; that is to say with contribution made to the public treasury of that part of land-rent which is not collected or may not be collected through the ordinary land value taxes and the tax on increased land value; to formulate legislative proposals on the basis of that investigation; to examine the relevant problems of land valuation and the position of title-holders and mortgagees during and after the change; and to indicate what may be its effects upon the distribution and use of the land and in easing the burden of taxation.

The Commission has not yet issued its Report. No information about its deliberations can be made public so that I must confine myself to a discussion of some of the questions that will most obviously arise and give only my personal points of view.

It is necessary in the first place to explain the meaning attached to the idea "appropriation of rent".

In this paper I use the short phrase "appropriation of rent" to mean the collection of the economic rent of land for the benefit of the public; and "rent" in this context means the rent of land apart from buildings and improvements. There is now being collected in Denmark an annual land-value revenue of 270 million crowns through the national tax on land values, the local taxation of land values and the tax

on increases in land value. The national tax is levied at the uniform rate of 0.6 per cent of selling value, the local taxation is at a uniform rate within each local governing area but varies from area to area averaging about three-quarters per cent in the towns and nearly 4 per cent in the rural municipalities when country and parish "rates" are taken together. The additional annual tax levied on the increases in land value, as are revealed when the periodic valuation of the whole of Denmark is made, has its application particularly where there is much urban growth and development. Finally, the present aggregate taxable land value of Denmark (assessment being the selling value) is 8,400 million crowns. When deduction is made for capitalised tax levied on increases in land value and for the value of land now liable to pay rent to the State, there remains 8,000 million crowns, which can be said to represent a capitalisation of the economic rent that remains in private hands.

The terms of reference to the Commission presuppose that existing taxes, national and local, on land values still remain and may possibly be extended. The appropriation of rent will then have a bearing only on that part of rent which after payment of the land value taxation is left to the owners. The position of the land owners, after the appropriation as thus defined, will seem to correspond very closely to the actual position of those land owners who now hold their titles on the condition that they pay to the State the rent of the land, being the annual value based at the normal rate of interest on the sum representing the capital value, as that is assessed at each periodic valuation of the whole country.

We have a considerable number of such properties in all parts of the country, seven to eight thousand in all, most of them small holdings and farms but there are also some building sites. The land has been acquired from the State not by purchase but by deed of transfer under which the owner and subsequent owners have to pay only the annual rent and they may dispose of the property by will or free sale just as could an ordinary owner of the fee simple; they can improve it and cultivate it as they think best.\* Their obligation and that of any person to whom the land is transferred is to pay the rent, and the annual rent is fixed at 4 per cent of the currently assessed capital land value.†

All those properties—and a great number of supplementary lots have been acquired on the same terms—are subject to

\*Some special obligations are attached to loans, generally granted by the State, for the erection of buildings until those loans have been repaid.

†For agricultural properties the rent may be subject to variation from year to year within certain limits according to the average net returns of ordinary small holdings, if the first owner at his option arranged for such variations in rent.

the national and local taxes on land values (tax on increases in land values excepted) in the manner and to the same extent as all other properties. They are assessed at selling value having regard to the burden of existing taxes including the ordinary land value taxes but assuming that no rent-charge was payable to the State. Development values are taken into consideration only if their realisation is an actual possibility.

The selling value of land will correspond to the capitalised economic rent if no fluctuation in prices is anticipated. The appropriation of rent may therefore be regarded as making all land liable for a rent-charge to the State on the same terms as those applying to the properties above mentioned—a rent-charge at a percentage of the selling value of the land, corresponding to the ruling rate of interest, the selling value being assessed on the basis already described.

If prices are fluctuating, selling values of land cannot be supposed to correspond exactly with the annual rent capitalised. The expectation of a rise or a fall in net returns or in the rate of interest will influence capital values; and even under constant prices, expectations of future development or other special conditions may influence the selling value of properties.

But when rent has been appropriated by the State, the capitalisation of rent will cease—and accordingly also land-speculation—and expectations of future rise or fall can have no material influence on actual selling-value or on the valuation, which only has to take account of the actual rent that may reasonably be expected until the next valuation.

This fact that the capitalisation of rent will cease to affect selling-prices, raises the question whether the valuation should be in terms of capital value or in terms of annual value when rent has been appropriated. In my opinion this is only a matter of expediency. In countries where the leasehold or tenant system prevails it may possibly be most expedient to assess land values in terms of annual rent, since this will correspond to accepted custom and to actual valuation practice, and it is quite possible that also in other countries when rent has been appropriated it may sooner or later prove to be most expedient to assess annual values.

But in a country like Denmark, where occupying ownership is prevalent and where current conceptions as well as existing valuation practice are attuned to capital values, the adoption of annual value for valuation purposes would be a serious disruption of existing valuation practice and nothing of that sort should happen at the same time as the appropriation of rent, unless absolute necessity commanded. It is evidently of the greatest importance not to imperil the continuity of valuation practice and the exactness and equality of assessment.

In this connection a special point is to be considered. Capital values are influenced by the current rate of interest as well as by the amount of annual economic rent. If the rate of interest is constant and the land value is assessed in accordance with the prevailing rate of interest, capital values will vary exactly in proportion to annual rent; and in a country where differences in the rate of interest are inconsiderable capital value will in all parts of the country be assessed at the same amount for all properties with equal economic rent. But even if the rate of interest is fluctuating or is different in different parts of the country, the same result may be effected; if it is stated that capital value is to be assessed on the basis of a given rate of interest.

In Denmark it should be most natural to take as basis a rate of interest of 4 per cent because the general rate of interest seems to fluctuate about that level, and it is the ruling rate for the greater part of first mortgage loans. This rate of interest also is established as basis of the rent-charge for the properties that are now paying the rent to the State.

The question next to be considered is the relation between the rent as appropriated by the State and the ordinary land value taxation, especially the local taxes on land values. This includes the very important question of the sharing of economic rent between the State and the local authorities, a question that is closely associated with the problems of local self-government.

With regard to State taxation of land values it is evident that our special annual tax on increases in land values must be included in the rent payable to the State. This makes matters so much easier because in our valuation this special charge is in fact treated in the same way as the rent-charge to which land acquired from the State is liable. The land is valued as if this charge did not exist.

Such revenue as the ordinary national land value tax brings in is split so as to devote the larger part to the municipal equalisation fund but the whole of it could also possibly go that way. Then under the changes we are considering, the national exchequer would receive only the appropriated rent; the local authorities would receive land value revenue directly from their local taxes and indirectly from the equalisation fund, both to be taken into consideration in the valuation of land just as now.

The question then remains to what extent the local authorities shall be entitled to levy local taxes on land values, when the rent which is at present left to owners is appropriated by the State. It is an important and a difficult question. It is evident that local taxation of land values is one of the means of making rent common property, and that being so it may possibly alter the amount of rent to be received by the State.

In Denmark, the position is that local taxation on land values is applied at much higher rates in the rural municipalities than in the city and the provincial town. Correspondingly the local income tax (the chief alternative source of revenue) is much higher in the urban than in the rural municipalities. There is this difference between town and country. But there is the further fact that from district to district there is a wide variation in the rate of the tax on land values. For example in some rural areas the county and parish rate combined is not over 2 per cent whereas in others it can be as much as 6 or 7 per cent; and it should be noted that the rate on the taxable value of buildings is  $\frac{3}{4}$  or  $\frac{3}{5}$  of that falling on land values.

The experience is that these great differences in rates of tax do not affect selling prices of real property or land values to any considerable extent; and this remarkable fact it seems possible to explain only in one way: The influence of rates on land values is counterbalanced either by a correspondingly opposed variation in the levy of local income tax or by variation in the value of municipal service to the ratepayers. My conclusion is that at least within the existing limits of municipal services and of corresponding revenue requirements it may safely be left to the municipalities themselves to decide to what extent expenditure should be met by land value taxation, reducing the income tax and giving relief to buildings and improvements. This conclusion seems to be sound enough as far as rural municipalities are concerned, but I think it holds good also for urban municipalities as can be shown from the experience not only of our rural communities with a considerable urban development but also of the cities and minor towns in New Zealand and Australia, where rating on land values is considerably higher than in our towns. At least it should be taken as a guiding principle that municipalities ought to have a prior right to revenue from land values in so far as municipal services create and maintain land values within the municipality.

Further experience may possibly lead to the decision that certain municipal expenses considered to have a direct influence on land values, such as expenditures for roads and sewers, street lighting, garbage removal, public parks, should be met entirely by local land value taxation while a certain limit should be fixed to that means of paying for services which have a less direct influence on the values of real estate. But until such experience is available it seems most natural to rely on self-government in this respect as far as ordinary municipal services are concerned.

In some of our rural municipalities more than 90 per cent of municipal expenditure is met by the local taxes on real property, the main part being levied on land values. Yet in

those municipalities the selling prices of real estate are not markedly lower than in municipalities with a different rating practice; and in them the total expenses certainly could be assessed on land values without interfering markedly with the amount of rent to be received by the State. This should then be possible also in other rural municipalities with a similar structure. In any event the powers of local authorities to shift taxation from one basis to another could be reasonably regulated so that there could be steady progress without too great alterations all of a sudden.

Having discussed the basis of the appropriation of rent and its relation to the powers of municipalities to levy local taxes on land values, we have next to tackle the problem of how to carry out the appropriation and that brings us face to face with questions about compensation to landowners.

Certainly all followers of Henry George agree that landowners have no moral right to a special compensation. It is true as Henry George says about rent: "It is a fresh and continuous robbery that goes on every day and every hour. It is a toll levied on labour constantly and continuously." This robbery simply ought to be stopped. A far more justified claim for compensation is that which might be asserted by those who have been robbed of the fruits of their labour up till now.

I take it also for granted that all are agreed that the appropriation of rent is to be accompanied by a corresponding reduction of taxes on the earnings of industry. This means that landowners as taxpayers will get by tax relief a partial or a total compensation for the rent and possibly also to some extent for the land value they must forego.

Small landowners—always the majority—will profit like those who are not landowners, if appropriated rent or land value taxation replaces existing taxes especially taxes on income earned by labour—and to them such influence as the appropriation of rent will have on the capital value of their property will be generally of little or no importance, except when land is to be sold and the acquisition of other land not contemplated.

It is evident that future increase of rent can be appropriated without any actual loss to anyone excepting the loss of expectations on the part of land speculators. This is even true—at least in Denmark—with regard to an increase in rent caused by devaluation or by inflation because mortgages generally speaking are greater than the value of land apart from buildings and improvements, and mortgages are not increased by devaluation or inflation. It follows naturally that a first step towards the appropriation of rent includes the full appropriation of increases in rent.

It is only where the present value of land is at stake that the full appropriation of rent raises difficulties of a realistic order. The matter is of greater consequence only to "big" landowners in the sense that they have a much greater financial interest in land value than in buildings and improvements or other products of industry; and it is of concern to a somewhat greater number of mortgagees where the security may possibly be affected by the rent appropriation.

Having regard to the weight or amount of existing taxation, even full appropriation of rent (with the taxes reduced to a corresponding amount) is a measure that does not go beyond the bounds of any general adjustment of taxation. This is true because 4 per cent of the present taxable land value does not exceed 10 per cent of the total amount of the national taxation now levied. In recent years there have been new and sudden increases in taxation of considerable amount without reducing any of the other taxes previously imposed.

It has to be recognised, however, that the appropriation of rent affects the selling values of land, and associated with that is the additional annual "expense" falling on the big landowners—the extra expense, from their point of view, being the difference between the rent they would have to pay and such relief as they would get from general taxation. These things combined may cause such disturbance in various other fields of economic life, mainly in connection with our mortgage system, that it seems necessary to proceed cautiously to avoid disadvantageous effects.

The appropriation of rent could be spread over a period of years and carried step by step progressively on defined lines, without encountering any economic disturbance. Thus the beneficial effects will antecede each step that is taken and every subsequent step will be made easier.

On the other hand, if the full appropriation of rent is to be effected at once, it seems necessary to adopt certain measures of dispensation or accommodation. Such measures may take one or other form but all tend to provide that others than the title-holders should share some part of the loss that a part of the title-holders would otherwise sustain.

During the agricultural crisis in the "thirties" the idea was ventilated that landowners should have a right to cause mortgagees to pay some part of appropriated rent. Special interest attaches to the fact that the same idea arose some forty years ago also under a heavy agricultural crisis, when it was submitted by Jakob Lange to Henry George who gave it his approval.

Our mortgaging system developed out of the transition from a feudal leasehold land tenure to occupying ownership and the growth of mortgage debt has always accompanied

the increase in the value of real estate. But mortgage loans are given also to a great extent for the erection of new buildings and improvements and especially so for urban properties. Our mortgaging system is operated by means of transferable bonds, so that the connection between a given property and those who have provided the loans for its purchase is entirely lost. In fact, the mortgagees are an ever shifting and indefinable number of depositors in Savings Banks, insurers in life insurance companies, etc., and I do not think it is fair that such savings should be made liable for greater risks than attach to the ability of the landowners to meet their obligations.

Some justification for accommodating in this way the position of landowners in an all-at-once appropriation of rent may be found when a general fall in prices has increased the burden of mortgage debts giving mortgagees a corresponding profit. Then there is the new owner who has but lately by purchase paid to the previous owner the capitalised increase in rent; and again more especially the man who has paid the price of the fee simple on conversion from freehold. Such are the considerations that play a part in this compensation argument.

Various schemes have been formulated by the Justice Party intended to recompense land owners when all rent is appropriated; and that, by requiring owners of all kinds of property to contribute to a compensation fund. Such a scheme, it may be granted, would make it possible to carry the full appropriation at once with the corresponding reduction of existing taxation; but only by inflicting a most severe burden on property owners in general. Moreover this measure could not but meet very great economic and technical difficulties, especially if the total compensation were to be paid at once; and it would be unjust to very large numbers of people, especially at present, when inflation has caused a considerable depreciation in the real value of bonds, deposits in savings banks and other pecuniary property.

The Danish Labour Party at their Annual Congress in 1945, approving the report of a Special Committee, included in their statement of policy the declaration that: "A reform of land value taxation is to be carried out having the object of appropriating the rent of land for the public". It was proposed that, to effect this declared reform, the landowners while paying the full economic rent would receive from the State bonds of same value as the assessed capital value of the land and bearing interest equivalent to the annual value at the time of the appropriation; the bonds to be amortised over a period of 60 years, interest and redemption being met out of the proceeds of general taxation. That method of compensating landowners obviously affords no



possibility of reduction in taxation, excepting in so far as any future increase in land-rents could be used for that purpose. But the scheme would involve an actual increase in taxation.

Every proposition for compensating landowners carries the danger that the mere prospect of compensation will counteract such tendency to lower prices for land as otherwise should precede the appropriation of rent. The prices of land will even be stiffened if compensation for the total land value is promised. And to the extent that compensation is given to balance the appropriation that is taken, the effects of the reform would be blunted or restricted only to such effects as accompany the revenue from increases in land value, the stoppage of private land speculation and the reduction of selling prices of real estate by the amount of land-value. On the other hand, there would be the countervailing effects depending on the kind of taxation the State would impose to provide for the compensation.

If it is intended to appropriate the full economic rent all at once, and give some compensation to landowners, it is therefore most important that the compensation be procured in such a way as to avoid imposing any heavier burden of taxation upon production or upon incomes earned by labour, and in such a way that the effects of the appropriation of rent are not subverted. Under normal conditions this would hardly be possible but under the present special conditions a reasonable solution of this problem of an all at once appropriation does seem possible.

The inflation of prices since 1940 has brought about great and unearned increases of property values, especially to owners of real estate, at the expense of people with fixed incomes, of mortgagees, of bond holders, depositors in savings banks, etc. For the owners of rent-restricted properties, a corresponding increase in property will be created through the relaxation or abolition of rent restrictions.

This unearned increase in property values cannot be returned to those who have borne the corresponding loss; it should be reasonable then to appropriate this increase and use it to facilitate the full appropriation of rent, with some compensation to landowners, which could be managed without vitiating the effects of the appropriation.

Even so, measures of that sort will encounter very great difficulties both practical and political. If those difficulties cannot be overcome, it will be preferable, as under normal conditions it would be natural, to carry the full appropriation of economic rent step by step through a given period of years and with no special compensation to landowners. The initial step should be the levy of a 4 per cent. annual tax on increases in land value accompanied by a levy at a lower percentage on existing land values, the latter to be raised gradually during

the given period of years to that percentage—4 per cent—which would appropriate the economic rent in full. What the initial percentage tax on existing land values should be may depend partly on the intended relief of taxation and partly on general economic conditions. Under the conditions that now prevail no great difficulty should present itself in starting with a rather high percentage accompanied by a substantial reduction in other taxation, seeing that landowners are now reaping an extraordinary gain through the general rise in prices, while their mortgage liabilities remain unaltered.

Further progress in that direction should be decided upon in advance so that over a period of years the selling prices of real property can be adjusted to future conditions, and so as to ensure that for mortgagees, the security of interest and amortisation may not be imperilled.

The amount of reduction in taxation that can be effected along with the initial step towards the full appropriation of rent may be calculated beforehand from the existing valuation of land. But future reliefs from taxation (on buildings, trade and industry) and the scope of other effects resulting from the rent appropriation cannot be so exactly calculated. It is to be assumed that the reduction in taxation will be followed by a gradual increase in land values, since existing taxation does to a considerable extent increase the expenses of all operations on land and this is especially the case with regard to farming land. If this argument holds good, the result will be a gradual increase in the rent appropriated by taxation, and a still greater reduction in the taxes on industry and trade. The experience of our local authorities, levying their local taxes on land values, seems to support that assumption but it is not likely that this experience can be foretold without qualification for a whole country. It is most likely that the effect of a national reform making rent common property will be to a greater extent an increase in real wages than an increase in rent. If real wages are increased this will tend also to increase the value of buildings and improvements as products of labour to the advantage particularly of properties where building value is high in proportion to land value and to stimulate technical progress.

To what extent such tendencies may unfold themselves or reach their final results cannot be reckoned upon in advance. It is sufficient to outline the course of development and where it tends.

The appropriation of rent must facilitate access to land and promote its best economic and social use. The barriers now raised by land speculation and injurious taxes will be removed. The selling prices of real property will be reduced to the selling value of buildings and improvements. As for land

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holders and their mortgagees, they will enjoy the advantage of a more secure position than at present, since wherever there should be a fall in land value the appropriated rent would be reduced correspondingly.