

LVT and Property Values

by Dan Sullivan

There has recently been a long and rambling discussion over whether land values would fall if land were taxed heavily. It's probably worth noting that there are some statements on this topic that we can make with assurance.

Basically there are three manifestations of land value that differ from one another in important ways: Land price, gross rent, and net or realized rent.

Land price is the most volatile. It is primarily affected by a speculative projection of future rents that the landowner expects to enjoy for himself, but it is also affected by the amount of money and credit available for purchasing land. Aside from how a change in tax policy would affect land price, it jumps up when interest rates go down and when credit policies are more liberal. It falls when interest rates go up.

Net or realized rent is rent collected by landlords, as well as imputed rent enjoyed by owner-occupants.

Gross rent includes rental value of land that is held out of use, calculated at its highest and best use.

Assuming a stable monetary and credit system (which makes this discussion hypothetical), the most dramatic effect of an increase in land value taxes (or site rents, or whatever you want to call it), would be a deflation of land prices. This is because land prices are the most speculative, and are the most affected by monopolization of land. As vacant and underused land comes onto the market, land prices would fall.

We have seen from the Pennsylvania cities that it does not take a big shift to land tax to bring land onto the market. Anyone who finds himself short of funds will put his vacant land on the market, and any vacant land that is not expected to appreciate by more than the tax will also come onto the market.

When the taxes are implemented gradually, and only in particular localities, as is the case in Pennsylvania, a land price drop is not observable. This is because the cities either reduced another tax, increased spending, or improved their solvency. All of these changes attract development that might have gone to other areas. While land

prices in those other areas might have suffered from losing business to these cities, there is no way to measure that phenomenon from Pennsylvania information. Any place other than an island nation will get an immigration effect when it shifts to land value tax, and even an island nation will see an inflow of development funds after a major shift. This prevents empirical data from showing what would happen if a very large country went to land value tax, or if the whole world did.

In any case, once most of the grossly underused land had come onto the market, further shifts from other taxes to land value tax would have very little effect on land price, because the removal of the other taxes would make the land more attractive and more productive, which would raise prices, while the higher land tax would make it less attractive — but without making it less productive.

Gross rent would be affected by two conflicting tendencies. Without LVT, rents are driven up by the artificial scarcity of land. As the best land comes into use, the worst land falls out of use. Because the rent of better land is related to its advantages over the cheapest land in use, rent will fall because the cheapest land in use will be better land than it was before the LVT shift. That tendency, however, is offset by the elimination of taxes tied to productivity. The rental value of lands that are spectacularly productive is held down by taxes that penalize productivity. Because these high-productivity lands generate a lot of sales and income taxes when fully used, and because these sales and income taxes come out of profits, less rent is offered for the most productive locations. The removal of those taxes will increase rents on the best sites.

As a result, the advantage differential between the best and worst land in use could go up, even though the worst land in use under a land tax is much better than the worst land in use in the pre-LVT situation had been. I cannot say with even slight confidence which factor will be stronger, because these opposite influences interplay so much with complex human behavior as to prevent quantitative analysis. In other words, while land prices will definitely go down, gross rent could go up or down.

Net rent, on the other hand, will go up, because net rent does not include rent that is frittered away from disuse or underuse of land. Eliminating that underuse eliminates gross rent — but not net rent. Only the rising of the margin eliminates net rent. As the best land comes into use at high rents, and the land that goes out of use was the worst and lowest-rent land anyhow, the net effect has got to be an increase in rents realized.

The situation would also lead to a great increase in productivity and efficiency, which would also increase net rents more than gross rents.

So far, however, I have only spoken in the context of replacing other taxes with land value tax or site rents. I have not spoken of collecting land rents and giving per capita dividends. I like the dividends from a justice perspective, and I think they also have merit as a popular measure. However, I do not believe that dividends would increase net rents unless we are talking about a small community that uses dividends to attract people from the outside. Even then, dividends will not attract the most productive people —as tax cuts would — and would not have as much of a rent-increasing effect as tax cuts would have. Is that a good thing or a bad thing? It probably depends on whether you are asking a landlord, a tenant, or an owner-occupant.