Land value

...for public benefit

Jerry Jones

Labour Land Campaign

New extended edition

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CONTENTS page

Preface

The original version of this pamphlet, published in 2004, was based on a series of articles written for the *Morning Star* earlier in the year. This substantially revised edition has been extended to include material from three further articles written for the *Morning Star* from 2005 and 2006, and from two papers produced for the Left Economics Advisory Panel of the Labour Representation Committee in 2006 and 2007. I thank the *Morning Star* and the Labour Representation Committee for allowing me to reproduce the material here.

I would also like to express my sincere gratitude to Julia Bastian, Dave Reed, Alan Spence, Louanne Tranchell, Dave Wetzel and Carol Wilcox, all members of the Labour Land Campaign, who commented on earlier drafts, which greatly improved the presentation and arguments involved.

The views expressed here are, of course, my own, and do not necessarily correspond to those of the Labour Land Campaign, the *Morning Star*, or the Labour Representation Committee.

Jerry Jones

Foreword

Many consider land reform as only a countryside issue, but, as Jerry explains, the most valuable land is in fact to be found in towns and cities. It is city centre land with tall buildings and prosperous commercial and shopping districts that command the most value and that offer the most potential revenue to governments.

Jerry clearly puts the case for land value taxation as a way of fairly redistributing this wealth. Not only would land values created by community activity be repaid to the public purse but also the effect of this modest reform would be to encourage better use of the surface of our planet - the land itself. With an annual tax liability, the owners of empty sites would bring them into use, thus creating new jobs and homes.

With this extra income the government could abolish taxes that harm the economy and perhaps even be able to pay a 'land dividend' to every man, woman and child as first proposed by Tony Benn, supported by the Labour Land Campaign, in his Common Ownership of Land Bill over 20 years ago.

A land value tax (LVT) is cheap to collect and impossible to avoid. Its effects would be to reduce the cost of housing and commercial buildings and thus enable businesses to expand and help workers find affordable homes. As LVT encourages the development of brownfield sites, the tendency for urban sprawl would be much reduced.

So what Jerry is offering us, is not only a new method to collect unearned income from owners of land, but also one that protects our environment, and creates more jobs and greater efficiency in the economy. A real benefit to us all.

Surely, an idea we should all seriously consider!

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1

How land acquires value – and who benefits

Land has no cost of production. It is what nature has provided for free. If an ample supply of land of equal desirability were available, there would be nothing to pay for its use. However, unlike labour and capital – the two other factors upon which the production and supply of all goods and services depend – the supply of land is fixed.

Thus, if there is greater demand for labour, its supply can be increased through working longer hours, or through working more productively as a result of investing capital in more productive technology – or by having more children or by encouraging immigration.

Similarly, if the demand for capital is rising, its supply can be increased by performing more surplus labour (that is employing labour over and above that required to satisfy immediate consumption needs), and through credit in various forms (which is equivalent to the surplus labour that will have to be performed in the future in order to repay the capital advanced).

But the supply of land – which, from an economic point of view, encompasses all natural resources, including minerals below the ground, as well as, among other things, the sea and sea-bed, the atmosphere, the radio spectrum and outer space – cannot be expanded in these ways in response to rising demand.

Another characteristic of land, in contrast to labour and capital, is that although its supply is finite, it does not wear out. It can be used and reused over and again, if not for one purpose then for another. Furthermore, land is often perceived simply as bare, unused land. Once it is built on, people tend no longer to think of the site as land. But land is land whether built-on or not. Indeed, land that is built on almost invariably is the most valuable of all land.

What determines the value of land?

It is precisely the demand for land, and its limited supply, that gives land its value. If demand for land is growing in particular localities, its value will increase. This will be reflected in the price one would have to pay to acquire the land. The demand for land and therefore its value, in different localities, depends upon many factors.

The demand for land may be high in some localities rather than others because the land is more fertile or well endowed with natural resources, or is an area of outstanding natural beauty. More importantly, and more usually, it may simply be because the locality is where more people want to live or work, perhaps because it is near markets or transportation routes, or is well supplied with services, such as water, electricity and gas, or shops, schools, and hospitals, and not too close to railway lines, motorways, airports, or rubbish dumps, which could render such localities less attractive places to live – though these factors could boost the value of land nearby for industries and commercial activities.

In short, the value of land in particular localities is created not by landowners, but first, by nature, and second, by other people and the community at large, through their economic and social activities, and the demand for land that this generates. If one took away such activities – as might happen, for example, when a mine became exhausted – the area would become a ghost town, and the rental value or selling price of land would be reduced practically to zero. On the other hand, the more that people choose to live and work in a particular locality, the more this will encourage investment in new productive activities, including infrastructure and improved services – both by public authorities, using taxes that we all pay, and by the private sector, from the profits derived from our spending. This will raise further the value of land in those areas.

Although the overall trend is for land to rise in value, due to growing populations and economic development which increases the demand for land, it is not necessarily a smooth process. There may be extended periods when land values are falling, and other times when land values rise much more rapidly than average. This may be for a variety of reasons, but generally it reflects what is happening in the economy as a whole and the kind of economic policies being implemented, which affect the demand for land.

For example, in the recent period, urban land values in Britain rose dramatically between 1995 and 2007 due to the huge expansion in credit availability, which, among other things, increased the economic demand for housing, and therefore the demand for land. Now that credit is no longer available on such a scale, this has gone into reverse, and land values are falling.

Meanwhile, the value of agricultural land, after a period of stagnation, has risen considerably due to the sharp increase in international food prices, which has increased the demand for agricultural land. Another reason for the volatility of land values is the extent to which land, perhaps including properties standing on the land, are an asset that is used for speculative purposes.

These issues are discussed in more detail later.

Who benefits from rising land values?

When land is largely privately owned, as in Britain, it is not the community as a whole that benefits from rising land values, but landowners, including owner-occupiers. They are able to sell or rent out their properties at a higher price than otherwise. In effect, they profit freely at the expense of other people, especially those who own no property – and at the expense of society as a whole, whose investments in various economic activities and services, and so on, are responsible for rising land values. And when landownership is highly concentrated among a few wealthy individuals and families, it is they who benefit the most. In Britain, fewer than 200,000 families own two-thirds of the land, while just 4 per cent is owned by Britain's 17 million home-owners (see Appendix 1).

Banks and other financial institutions are also major beneficiaries of rising land values because people and businesses, if they need credit to acquire land or property, have to borrow more than they otherwise would, which means that banks and other lenders earn more interest.

The question of land ownership

Since it is nature that has provided land free for all of humanity, there is the argument that land should not be privately owned at all. This begs the question of how land came to be owned by individuals in the first place.

In fact, until quite recently, in terms of human development, societies everywhere treated land as common property. Where land was in much demand, it would be allocated more or less according to need through various systems of customary tenure. The land was yours as long as you used it, but it could be taken over or re-allocated if you did not. Such systems still exist in parts of Africa and other regions. The private ownership of land – especially when highly concentrated among a few wealthy individuals and families, as in Britain – more often than not, can be traced to its outright theft at some stage by those with political and coercive powers.

This has led many to call for the nationalisation and state ownership of land, thus returning land to common ownership, as the only fair way for society as a whole to benefit from the rising value of land that society itself creates. However, as will be explained in the next section, this is not at all necessary – nor would that necessarily guarantee that society as a whole would benefit.

2

Reclaiming land value for public benefit – the case for a land value tax

It is true that, if starting from scratch, the state ownership of land could be a considerable advantage. People and businesses could be charged rent for the land that they occupy based on its value, and the revenue used to invest in public services and other productive activities for public benefit. This would ensure that society as a whole, rather than private landowners, would benefit from the increasing value of land arising from the social and economic activities of society.

However, state ownership by itself is no guarantee. Without measures taken to value land in relation to its location and quality, and collecting the rent accordingly, those occupying the land will benefit at the expense of the public at large. Moreover, land will tend to be used indiscriminately, irrespective of its value.

This happened, for example, in the former Soviet Union, where all land was state owned, and, moreover, treated as a free good (as was capital). Consequently, there were many instances of land being used inappropriately or inefficiently. In particular, it was common practice for enterprises (almost entirely state owned in the Soviet Union) to hold land vacant indefinitely in case they might need it later. This meant that the rest of society lost out from making the best use of what was often valuable land in a prime location for more beneficial purposes. This also distorted investment decisions, which meant that capital was not necessarily invested in productive activities that made the best use of the land that was available.

Nevertheless, since land use was under state control – as indeed it is in most countries, including Britain – it cannot be said that land use was entirely indiscriminate. The problem was that decisions were based not so much upon the economic value of particular sites, but more according to administrative convenience, and the relative effectiveness of lobbying by enterprise managers, local politicians and other vested interests, and the connections they had with planning authorities.

Meanwhile, in countries such as Britain, where the private ownership of land is thoroughly entrenched, would nationalisation, in which all private titles to land were abolished and land declared public property, be the most effective course for reclaiming land value for public benefit? Is it even necessary?

If a political party included in its manifesto land nationalisation without compensation, one needs little imagination to picture the propaganda war that would ensue – paid for by the wealthy 0.5 per cent of the population who own most of Britain's land. Britain's 17 million homeowners could easily be persuaded that the government was about to steal the land that they had bought in good faith along with their homes, even though the state ownership of land would make no difference at all to their right to the land.

Alternatively, if compensation were offered, and if based on market values – which inevitably would incorporate a speculative element – the amount of money involved would be astronomical. It would also be immoral. As Henry George pointed out, 125 years ago, in his book, *Progress and Poverty*:

'…to buy up individual property rights would merely be to give landholders in another form a claim of the same kind and amount that their possession of land now gives them. It would be to raise for them by taxation the same proportion of the earnings of labour and capital that they are now enabled to appropriate in rent. Their unjust advantage would be preserved…'

In fact, the key issue is not the confiscation of land itself, but that landowners should pay for the land that they occupy according to its value, and the revenue used for public benefit. This would be fair, because it is not the landowners who created the land, or its value. The land was already there, and it is society as a whole that creates its value.

The most effective way of ensuring that the public as a whole benefits from the value of land would be for the state, acting on behalf of society, to collect an annual tax from all owners of land in proportion to its value.

It should be emphasised here that what is being proposed is not a tax that would be additional to the taxes that we already pay, but would be in their stead, and allow other taxes that have an adverse economic impact to be eliminated or reduced. In fact, a land value tax (LVT) is not really a tax at all in the normal sense.

Thus, in contrast to other taxes, LVT does not take anything away from landowners that they have been responsible for creating, since it is society as a whole that creates the value of land. In other words, LVT is in no way a penal tax, and it does not act as a disincentive as does taxation that falls on production or earnings. Rather, it would be a payment by the user of the land for the natural opportunities of climate, fertility or position that he or she exclusively enjoys, together with the opportunities associated with particular sites that are created by the economic and social activities of all of society – which is why some commentators have suggested that LVT should be renamed 'location benefit levy'.

Apart from the moral argument that such a tax would return to society the value of land that society itself had created, it would have a number of other economic benefits. First, it would make more efficient use of land. Landowners would have to pay the tax according to the value of their land even if they could not make the best use of the land in line with prevailing planning regulations – in which case, they would have every incentive to sell it on as quickly as possible to someone else who could make more economic use of the land. It would end the wastefulness of derelict land and decaying buildings standing empty for years on end that blight neighbourhoods. Furthermore, it would more or less end speculation on land, because it would become too costly.

By gradually raising the rate of LVT – and at the same time reducing other taxes – land ownership would begin to lose all significance. Then, the only point of owning land would be to use it. In other words, the income and profit from land would derive solely from the particular economic activity or buildings on the land. There would be no gain simply from owning land, as now, which, as explained above, is at the expense of the rest of society.

The many economic and social benefits of LVT – over and above its huge revenue raising potential for funding public services – is well illustrated by the US city of Harrisburg, which has put into practice a system of land value tax, as summarised in the next section.

3

How Harrisburg in the US was transformed through a land value tax

In the United States, many local authorities, including Harrisburg, the capital of Pennsylvania, operate a so-called split-rate tax system, in which buildings and land are taxed separately. Some bias it towards buildings and others towards land. The evidence is that the more it is biased towards land, the more this benefits the local economy – which is what would be predicted by the theory of land value tax – because the more that land is taxed the more this provides an incentive to invest capital on the land in the form of buildings and other economic activities. That is precisely what happened in Harrisburg after the city authorities more than doubled the tax rate on land, while reducing the rate on buildings, such that the rate for land was three times that for buildings.

In 1982, before the change, Harrisburg, with a population of 52,000, was listed as the second most run-down city in the US. Since then, following the change, empty sites and buildings have been re-developed, with the number of vacant sites by 2004 down by 85 per cent. The city authorities have issued over 32,000 building permits, representing nearly $4 billion of new investment – nearly 2,000 were issued in 2004 alone. Over 5,000 housing units have been newly constructed or rehabilitated, and the number of businesses has jumped from 1,908 to 8,864, with unemployment down by 19 per cent. Furthermore, crime has fallen by 58 per cent, and the number of fires has been reduced by 76 per cent, which the authorities say is due to more employment opportunities, and the elimination of derelict sites, making vandalism less likely. They list 40 other positive benefits, including much improved public amenities. More recently, the bias towards tax on land is now six to one compared with three to one originally. This will likely further enhance the trends from which the city has already benefited.

Meanwhile, the heightened economic activity has increased public revenues, not only from land and buildings, but also from other taxes, thus benefiting public services. And it has increased quite dramatically both the value of land and that of buildings, from around $400 million in 1982, in today's prices, to $1.7 billion now. This has enabled the authorities to reduce the rate of tax on both land and buildings. Not surprisingly, this system of taxation has been politically popular, with Mayor Steven Reed Jr being re-elected continuously since 1982.

One constraint has been the fact that 47 per cent of the land in Harrisburg is occupied by state, federal, educational and charitable institutions, which, anomalously, are exempt by State law from property taxes. However, some of that lost revenue has been clawed back through charges on water, gas and electricity supplies, which are publicly owned – perhaps another lesson that we can learn from Harrisburg.

Meanwhile, another city in Pennsylvania, namely Pittsburgh, has gone in the opposite direction with its split-rate tax system. In 2000, it reduced the rate of tax on land to the same lower rate as that for buildings. Voters were persuaded that they would pay less tax. In fact, for most, taxes have increased, because the council has had to raise the tax rate on buildings to make up for the revenue lost through lowering the tax on land. Within just the first two years, it led to new construction falling by 21 per cent, and businesses moving out of town on a regular basis – which, again, is what would be predicted by land tax theory.

4

Valuing the land – how to measure land values

In principle, the charging of landowners for the land that they occupy according to its value, disregarding what is built on the land or what it is being used for, is simple. But first, the value of land needs to be measured.

The only definite measure is when a piece of bare or cleared land, or its lease, is sold, assuming that the negotiated price (which might differ somewhat from the advertised price) is a measure of its value to the economy, and to society, at that moment.

The trouble is that, mostly, when land is bought and sold, it is along with the buildings or productive activities on the land. How can the value of the land in such transactions be separated out?

Moreover, even for properties as a whole, including the land on which they stand, barely one per cent is actually on the market at any one time. Thus, while it might be possible to know the value of those properties when they are sold, how can one know what the value is of the other 99 per cent of properties? This, of course, concerns all taxes based on property, including, currently, the council tax on homes, and the national non-domestic rates on commercial properties. However, within the property industry, a whole profession of valuers has grown up whose practitioners are able to give reasonably accurate estimates of the value of properties, taking into account their location, and the prices being fetched by similar properties on the market in the neighbourhood. It is on this basis that the council tax and national non-domestic rates are set.

But in the case of LVT, there is still the apparent problem of separating out the land element from the value of the property as a whole.

Valuing land separately from developments on the land

It is often thought that valuing land accurately and separately from the buildings and developments on the land is more difficult than valuing properties as a whole, including the land element – especially since the incidence of bare land being sold, which could provide a benchmark for valuing other land, is rare. However, even now, property developers call upon professional valuers to value particular sites becoming available for re-development, and they do this without difficulty.

In fact, valuing land is less complicated than valuing buildings. That is because the only factors that need to be considered are location and potential use consistent with prevailing planning regulations, whereas for buildings, additional factors, such as the state of repair, what the buildings are being used for, how old they are, their architectural merits, their internal space, and so on, have to be taken into account. The valuation of land, therefore, can be more easily generalised. This allows the extensive use of modern information technology, including computer-aided mass assessment and geographical information systems (GIS).

One method for assessing the value of land separately from the value of buildings on the land is to start with the known market value of the property as a whole (the building plus the land), and then deduct the value of the buildings, which roughly corresponds to the estimated rebuilding costs for insurance purposes, adjusted for depreciation. The remainder will be the value of the land. This is known as the 'residual value' method of assessment. There are a number of other methods, which can act as a cross-check on one another.

By collecting data on valuations and sales of similar properties in different locations, and on the valuations and sales of different properties in the same neighbourhood, including differences between property prices and their values for insurance purposes, and other data, it is possible to arrive at reasonably accurate estimates of land values over the whole country. This and other information can then be used to construct what Tony Vickers, at the School of Surveying, Kingston University, who is pioneering such techniques, has called a 'land-value-scape', with maps, instead of showing contour lines depicting topography, show lines marking off localities and zones with equal land values per hectare or square metre. Thus, simply knowing the area of a site, one can immediately calculate its value by referring to its position on the map, which would be available for public scrutiny.

Once such a system for valuing land is up and running, by recording and tracking property sales and other data throughout the country, it would be possible to update land values more or less continuously. Over time, it would be possible to incorporate new data – perhaps using a points system that would take into account proximity to amenities and services, which would increase land values, or congested roads or unsightly vistas, which would depress values – so that the system of land valuation would become ever more refined.

In short, it is not true that valuing land is problematic, as opponents or sceptics of land value taxation often assert – often the same people who quite happily accept the valuation of buildings, even though this is more difficult. Valuing land, especially in towns, which is where the most valuable land is located (because it is in high demand) is much simpler, because, as discussed, it depends essentially on location. Indeed, in the United States where split-rate tax systems operate, according to a valuer in one city, some 95 per cent of his valuation staff is employed valuing buildings, whilst only 5 per cent is involved in valuing land. Moreover, invariably, there are many more appeals against the valuation of buildings than of land, with authorities winning more appeals on land than on buildings.

Capital values versus rental values

The methods most frequently used for valuing land give its capital value. This is often presented as a problem, because for the purposes of charging landowners for the use of the land that they occupy on an ongoing (normally annual) basis, it is generally assumed that it is the rental value that is required. However, in a modern economy, it makes little difference, because capital values can easily be converted into rental values simply by multiplying capital values by the prevailing discount rate, which is the average going rate of return on capital invested in all economic activities. Conversely, rental values can be converted into capital values by dividing by the discount rate.

For example, if the discount rate is 10 per cent, a site with a capital value or market price of £100,000 would have a rental value of £10,000 per annum (the capital value of £100,000 multiplied by the discount rate of 0.1).

The discount rate is a figure that is readily available because it is used by investors and financiers to decide whether or not to go ahead with a particular investment or the granting of a loan for a project. A way of conceptualising the meaning of discount rate in the present context is to pose the question, would it make more economic sense to sell a site, or rent it out? If a site had a capital value of £100,000 (which would be the amount one would expect if sold), and one could get £10,000 a year in rent for the site, that would represent a 10 per cent return. So, if one decided to sell the site, other things being equal, one would want to be able to invest the cash somewhere that earned at least 10 per cent. That in effect would represent the discount rate.

When discussing rates of LVT, much depends, obviously, on whether one is referring to capital values or rental values. For example, if a site with a capital value of £100,000 raised £2,000 per annum in LVT, the rate of LVT in terms of capital value, would be 2 per cent. The same site, assuming a discount rate of 10 per cent, would have a rental value of £10,000 (see above), so for the same amount of revenue raised, the rate of LVT would be 20 per cent.

There have been occasions when people have been confused into opposing LVT because they believe that such a rate of LVT is referring to a tax on capital values. But even a rate of 100 per cent of rental value would only be 10 per cent in terms of capital value, assuming a discount rate of 10 per cent. And if the discount rate was only 5 per cent, the rate of LVT in capital terms would be just 5 per cent. So when discussing the rate of LVT, it is important to state whether one is referring to capital values or rental values.

The effect of planning regulations on land values

Planning regulations, which exist in every country, including Britain, can have a profound effect on land values. For example, sites in the middle of town, with a wide range of amenities available, if designated a residential or commercial area would have a high land value. Such sites would likely have even higher values with planning permission to build a multi-storey block of flats, compared with, say, those with permission for low rise semi-detached houses with gardens.

On the other hand, land designated as a public park would have a low, or even nil value, since it could not be bought or sold, or built on. However, the park would tend to boost the value of surrounding sites because green views and opportunities for leisure activities would make the area more desirable for homes or work.

Meanwhile, land on the edge of towns designated for agriculture or as common land, perhaps as a measure to contain urban sprawl or to protect a 'green belt', would have a low value compared with, say, neighbouring sites designated for residential or industrial use.

Some idea of the enormous variations in land value according to permitted use may be gleaned from the following figures from the Valuation Office Agency. Thus, in 2007, it was estimated that the average price of land designated for agriculture in England was £9,287 per hectare, while for different kinds of industrial and commercial use it was between £630,000 and £749,000 per hectare, and for residential use it was as much as £2.46 million per hectare.

From these data, it is obvious that the land value of a site can change quite dramatically if planning permission is granted for a new use. For example, a former industrial or commercial site if re-designated for residential use, could see its value rise almost fourfold, while a site on the edge of town formerly designated for agriculture could see its value leap by as much as 200 times if planning permission were granted to build houses on the land.

Furthermore, once a site has been redeveloped following the granting of planning permission, this will affect the land values of neighbouring sites. For instance, if the new development resulted in new economic and social activities coming to the area, thus enhancing its appeal as a place to invest, live, work or socialise, or if it gave rise to improved transport connections, land values in the whole neighbourhood would tend to rise. On the other hand, if planning permission were granted for a new factory or an incinerator, this could cause land values to fall.

The need for regular valuations

The valuation of land needs to be conducted on a regular basis, because land values can change considerably year on year.

First, as just discussed, land values are highly dependent on planning regulations, and can change markedly when planning permission is granted for a new use. This may also affect the land values of neighbouring sites.

Second, land values are highly affected by changing patterns of economic demand for properties and land (that is demand from people and businesses with the means to procure property or land), which reflects changes in the performance of the economy as a whole. If the economy is growing, this will tend to boost the demand for property and land, which will push up land values, while the opposite is more likely to occur in the event of an economic downturn.

What is happening in the global economy also affects land values. For example, between 2006 and 2008, there was a huge increase in the global demand for food grains, mainly from the booming economies in East Asia, which caused international prices to double or more. This increased demand for agricultural land and therefore its value, which, in England, more than doubled during that period.

Furthermore, the economic demand for property and land, and therefore the value of land, is highly dependent on the availability of credit. When credit is only loosely regulated, as in most countries since the early 1980s, this will tend to push up demand and land values – all the more so when banks, in their drive to gain business ahead of their competitors, drastically relax their conditions for lending to home buyers and property developers, which is what happened almost everywhere between the mid-1990s and the early years of this century.

As discussed in Appendix 2, this was the major factor that caused the huge escalation of house prices during that period, which was almost entirely due to rising land values, since building costs changed hardly at all. However, when the availability of credit dries up, as happened in Britain and elsewhere in 2007 and 2008, this reduces the economic demand for property and land, thus causing a fall in property prices and land values.

Other factors may also affect land values, such as natural disasters.

For the purposes of collecting LVT, using out of date land values for a relatively short period does not matter too much, because the land values of all sites will tend to move in parallel, reflecting trends in the economy as a whole, with the land value of sites relative to one another, which is the more important factor as far as collecting LVT is concerned, changing hardly at all. However, over time, changes in the relative values of sites will gradually become larger, which would need to be taken into account.

A reasonable compromise would be for valuations to take place every one or two years. However, once a system of valuing land, as described above, was up and running, it would be possible to assess land values more or less continuously, and at little cost, so that the issue would not arise. The LVT due on a site in a particular year could simply be based on its average land value over the previous year.

Fluctuations in land values also affect the amount of revenue that can be raised from LVT at a given rate of LVT. If it is desired to maintain revenue from LVT at a certain level, this could be addressed by varying the rate of LVT. Alternatively, allowing the amount of LVT due to vary could act as a means to smooth out economic cycles (see Section 7).

Accounting for the effect of LVT when valuing land

When valuing land after LVT has been introduced, the effect of LVT on the market value of land needs to be taken into account. First, consider what the effect would be of introducing LVT when there had been none before.

Take a site valued on the market for £100,000 before LVT was introduced. Assuming a discount rate of 10 per cent, the rental value of the site would be £10,000 per annum (£100,000 multiplied by the discount rate of 0.1). Now consider the effect of introducing LVT at a rate of 20 per cent of rental value. The amount of LVT due would be £2,000 (£10,000 multiplied by the rate of LVT of 0.2). If the landowner was renting out the land, this would mean that out of the £10,000 he or she received in rent, £2,000 would go in LVT. In other words, the market value of the site in rental terms would fall from £10,000 to £8,000. However, the total land value of the site would remain £10,000. It is just that £2,000, out of the £10,000, would now go to the community as a whole – that is those responsible for creating the value of the land – rather than, as now, to the landowner, who would have contributed almost nothing to the site's value.

The fall in market value of the site in rental terms, following the introduction of LVT, would mean also that its capital value on the market would fall. Assuming a discount rate of 10 per cent, the new market value of the site, which would be its price on the market, would be £80,000 (£8,000 divided by the discount rate of 0.1). In other words, the market value of the site, or its price, would have fallen by 20 per cent – the same as the rate of LVT in rental terms.

A similar calculation can be performed using only capital values. Taking the same site valued initially at £100,000 on the market, if LVT was now introduced at a rate of 2 per cent of the site's capital value, the amount raised would be £2,000 per year, as before. The capital equivalent of that sum, assuming a discount rate of 10 per cent, would be £20,000 – which is equivalent to the amount of capital one would require to obtain the £2,000 a year to pay the LVT. This £20,000 represents the amount by which the market value of the site, or its price, would be reduced. In other words, the market value of the site would fall to £80,000, the same result as before. However, the total capital value of the site would remain £100,000, including that part now going to the community.

If the rate of LVT were raised to 40 per cent of rental value, the amount of LVT going to the community would go up to £4,000 (£10,000 multiplied by the rate of LVT of 0.4), and the amount going to the landowner would fall to £6,000, which would be its new rental value on the market. However, again, the total rental value of the site would remain £10,000. The market value of the site in capital terms, that is its price, would also fall – to £60,000, assuming a discount rate of 10 per cent (£6,000 divided by the discount rate of 0.1), though its total capital value would remain, £100,000.

In short, the higher the rate of LVT, the more this will tend to lower the market value of land, or its price, but it will have no effect on total land values, including the amount going to the community in the form of LVT.

Now consider a site valued on the market by valuers for £100,000 once LVT was already operating. When valuers value land, they would merely be looking at the market value of the land – what the site would fetch if sold or what rent it would command on the market. They would not take into account the effect of LVT on market values. Yet the rate of LVT needs to be set in terms of the total value of the site, including the amount going to the community in the form of LVT. The question is, what would be the total value of a site if its market value was £100,000? This can be determined through a simple calculation.

Thus, assuming a discount rate of 10 per cent, a site valued at £100,000 would have a market rental value of £10,000 per annum (£100,000 multiplied by the discount rate of 0.1). Let the total rental value of the site be R. If the rate of LVT is 20 per cent of rental value, the amount of LVT going to the community would be 0.2R. Meanwhile, the site's total value would be its market rental value – in this case £10,000 – plus the amount of LVT going to the community, which is 0.2R. In other words,

$$R = £10{,}000 + 0.2R$$

Therefore,

$$R - 0.2\,R = 0.8\,R = £10{,}000$$

$$R = £12{,}500$$

Thus, if the rate of LVT was 20 per cent, a site with a market rental value of £10,000, would have a total value in rental terms of £12,500 (R), and the amount going to the community in the form of LVT would be £2,500 (0.2R).

The total capital value of the site can be obtained simply by dividing the total rental value of £12,500 by the discount rate. Thus, if the discount rate was 10 per cent, the total capital value would be £125,000 (£12,500 divided by the discount rate of 0.1).

(The same result can be obtained by performing a similar calculation using only capital values. Thus, the total value of a site would be its market value as determined by valuers, plus the amount of LVT going to the community expressed in capital terms, which would be the LVT paid annually divided by the discount rate. Let the total capital value of the site be C. If the rate of LVT is 2 per cent in capital terms, and assuming a discount rate of 10 per cent, the total capital value, C, of a site with a market value of £100,000 would be £100,000 + (0.02 ÷ 0.1)C, so that C will be £125,000, the same result as before. And the amount of LVT going to the community would be 2 per cent of £125,000, or £2,500 a year – again, the same result as before.)

All these calculations are, of course, somewhat theoretical. Their purpose was to explain why LVT will tend to lower the market value of land, the more so as the rate of LVT is raised, and to show why it will not affect the total value of land, including the amount going to the community in the form of LVT. In addition, the calculations showed how one can calculate the total value of a site either in capital terms or rental terms for a given rate of LVT. Another purpose of the calculations was to address an issue that has caused some confusion, which is the implication that if the LVT was levied at a very high rate (as would be the case if LVT was extended to replace other taxes to an increasing extent, thus to realise fully its economic benefits), it would lead to the declining value of land, and therefore declining revenues from LVT. In fact, as shown, other things being equal, only the market value of land would decline, not its total value, and the revenue from LVT at a given rate based on the total value of land would not decline at all.

In practice, tax-raising authorities will not be particularly concerned about the rate of LVT, whether in rental terms or capital terms, or whether it was based on market values or total values. They will only be interested in the amount of revenue that they can raise from LVT. They would therefore tend to decide first the amount of revenue that they wish to raise, and then set the rate of LVT accordingly, using either rental values or capital values, and either market values or total values, whichever they find the more convenient – and, in any case, as shown above, they can all be converted quite readily one into another using simple mathematics. In general, the most straightforward approach probably would be to start with the market value of a site, that is the price it would fetch if sold, which is a concept that everybody is familiar with, then use that figure to calculate the site's total rental value, and base the rate of LVT in rental terms on that.

The overall impact of LVT on land values

The above calculations were also theoretical in the sense that they disregarded the impact of economic growth on land values and the impact of LVT on economic growth. They will offset the tendency for LVT to lower the market value of land, as will now be explained.

First, the requirement to pay LVT would act as an incentive to invest in various productive activities, including housing, with the aim of making the best use of the land, according to prevailing planning regulations. Such investments would create new job opportunities, and when those employed spent their wages, this would have the effect of increasing the economic demand for goods and services. This, in turn, would stimulate more investment to meet that demand – creating further new job opportunities, and so on.

In other words, LVT would have the effect of boosting economic growth, which would increase the demand for land, and therefore land values and land prices. In short, the net effect of LVT would be to make land prices lower than they otherwise would be, but not necessarily lower in absolute terms.

Furthermore, because land prices would be lower than otherwise, business premises and homes would be more affordable, because they would have to spend less on land, so that more money would be available for spending on investment and on consumption. This would increase economic growth, and therefore raise land values all the more. On top of that, rising land values would yield more revenue from LVT, which would mean that other taxes that have an adverse impact on the economy could be reduced. This would give a further boost to economic growth and land values. All of these factors would be enhanced as the rate of LVT was raised.

As discussed Section 3, this positive effect of LVT on economic activity and on land values was precisely the experience of Harrisburg when the rate of tax on land values was raised, and that on buildings reduced.

To sum up, following the introduction of LVT, it is possible that in the short run, the market value of land, in other words, land prices, will tend to fall. This would be less likely if, initially, LVT merely replaced existing property taxes (see Section 9) – though if many landowners, sitting on unused or underutilised land, or on sites with empty buildings, when faced with having to pay LVT, chose to sell their land, in effect, increasing its supply, this could still cause land prices to fall in some localities. However, in the long run, the tendency for LVT to push down the market value of land, as LVT was extended, would be offset by the extent to which LVT boosts economic growth, and therefore land values.

In other words, the net effect of LVT, other things being equal, would be to make land prices and property prices lower than they otherwise would be, but not lower in absolute terms. Prices would merely stop rising, or not rise to the same extent, as they would have done.

On the other hand, if, there were an economic downturn, for whatever reason, that coincided with the introduction of LVT, this would likely result in lower property prices. This would cause the demand for land and property, and therefore land values to fall. It would not be because of LVT.

In short, the overall effect of LVT would be to make land and property prices more stable, especially as it would more or less eliminate speculation in land. In particular, as discussed more fully in Appendix 2, LVT would help prevent the formation of property price bubbles (actually, land price bubbles), which not only distort investment and the whole process of economic development generally, but cause considerable havoc, including the destruction of value and capital, when they collapse.

5

Differences between a land value tax and other taxes on land and property

Up to now, governments in Britain have shied away from introducing a full-blown system of land value tax. Instead, they have sought to reclaim land value for public benefit through various piecemeal measures. These measures have raised nothing like the revenue that would be possible from LVT. Moreover, they have proved costly to implement, not least because the legislation involved has been complicated, and subject to complex sets of rules and regulations, with various exceptions and offsets. Moreover, they have often have had effects opposite to what was intended.

The measures include: development land taxes under various guises, which are one-off taxes on the uplifted value of sites following the granting of planning permission for a new use; the stamp duty land tax, paid when properties change hands; Section 106 agreements, in which developers are required to finance infrastructure or affordable housing or other things as a condition for the granting of planning permission, and therefore are a form of tax; so-called planning charges or community infrastructure levies, which have partially replaced Section 106 agreements; and a new empty buildings tax.

The council tax and the national non-domestic rates, which are largely taxes on property – though paid by the occupiers of the property rather than by the owners – should also be included, since they involve an element of tax on land values. The special problems with these taxes are discussed in Section 6.

Development land taxes

What has misled politicians into supporting development land taxes – including the so-called 'planning gain supplement', proposed by the Barker Review on housing supply in 2004, which the present government was considering introducing, but has since abandoned – is their focus on the huge jump in land values when planning permission is granted for a new use. For example, if a landowner gains planning permission to convert agricultural or commercial land into residential use, he or she could be in for a windfall gain of several million pounds. Development land taxes are perceived as a means of reclaiming a significant portion of that gain for public benefit.

However, the amount of revenue such taxes can raise, compared with LVT, is severely limited. First, a development land tax is only collected when a site is sold or developed, and therefore only taps land value on a few sites at one point in time. In contrast, LVT, instead of being merely a one-off payment, would become due every year in perpetuity. Therefore, the revenue stream for public benefit would far exceed what it would be from a development land tax. Moreover, the LVT would be paid not only on the increased value, but also on the value of the land before planning permission was granted – the so-called residual or 'current' value.

In addition, the new development is likely to bring new economic and social activities, or improved transport connections, to the area, which would increase the land value of neighbouring sites, so that additional LVT would be collected from these properties, too. In short, if LVT were in place, all of the uplifted value would be recovered, perhaps many times over, because the LVT would rise in proportion to the increased land value once planning permission was granted. Moreover, the extra LVT would be due immediately, thus providing a big incentive for the site to be developed as quickly as possible.

Meanwhile, any windfall gains following the granting of planning permission as a result of the land being sold on could be recovered through other taxes – such as capital gains tax or income tax. This would be fair because, much of the windfall gain would have arisen from the increased value of the land created by planning authorities acting on behalf of the community, so that the tax would merely allow the community to reclaim it back for public benefit.

Another major problem with development land taxes, as evident from the whole history of introducing such taxes, including the Development Charge in 1947, the Betterment Levy in 1967, and the Development Land Tax in 1976 – all brought in by Labour governments, only to be abolished a few years later by incoming Conservative governments – is that they tend to inhibit the development of land. That is because owners of land can withhold land from use without penalty, but are penalised, in effect, as soon as the land is brought into use. In addition, through tacit collusion, landowners and property developers can withhold land to pressurise governments, or future governments, to repeal the tax. Meanwhile, they can simply sit back and watch their landholdings rise in value as the demand for land goes up. All these things happened when those development land taxes were introduced previously. Furthermore, because of various kinds of exemptions and offsets, the taxes turned out to be severely complicated and costly to implement, and the revenue that they generated was considerably less than had been expected.

Stamp duty land tax

The stamp duty land tax is charged on properties over a certain value when they are sold (currently those over £125,000). Nominally, it is paid by the buyer, which, in effect, makes properties more expensive to acquire than they otherwise would be. However, if it is a buyer's market, the tax, would tend to fall more on the seller, who would have to reduce the price to compensate for the tax that the buyer has to pay.

The main problem with the stamp duty land tax is that it discourages the change of ownership of properties. In effect, therefore, it penalises those wishing to move to a more convenient location, or more suitable premises, and therefore encourages the inefficient use of land and buildings.

Section 106 agreements

Payments or investments under Section 106 agreements, which oblige developers to finance infrastructure, or affordable housing, or other things, are essentially a form of development land tax. They therefore have all the disadvantages of such a tax, as just discussed. A further problem is their ad hoc nature, and the lack of clarity of criteria used for arriving at such agreements. Nominally, they can only be levied in order to 'mitigate harm' that would otherwise arise from the development, such as increased traffic congestion on local roads, overcrowding in local schools, or the tendency for developments to favour luxury housing at the expense of affordable housing required by people who work in the area. This, of course, is all a matter of interpretation. Section 106 agreements, therefore, are notoriously variable and unpredictable between – and even within – planning authorities, and half of all planning authorities are not even using such agreements.

Meanwhile, much depends on the negotiating skills of local planning authorities, which, if genuinely acting in the public interest, will want to extract the maximum contribution from property developers. The latter, on the other hand, will seek to keep their obligations to a minimum. Consequently, negotiations can be protracted, perhaps involving expensive legal advice and lawsuits, or appeals against decisions made by the planning authorities. This can make Section 106 agreements costly to implement, not least because of the delays before society will benefit from the developments being proposed.

Furthermore, as pointed out by Tony Vickers (in *Location Matters: Recycling Britain's Wealth*, Shepheard Walwyn, 2007), because of the opaqueness of Section 106 agreements, it is often hard to dispel the whiff of corrupt 'paying for planning permission', which will often favour big national and international property developers, at the expense of local builders who might have a more genuine interest in the local community.

Planning charges

Now that the government has dropped the 'planning gain supplement', its latest proposal is a system of tariffs, or 'planning charges', also known as 'community infrastructure levies' These are similar to the infrastructure tariff that has been operating in Milton Keynes for some time, which is a levy proportionate to the size and scale of a development. Again this is a form of development land tax. Under the system, according to the government's current proposals, in exchange for receiving planning permission, developers have to agree to pay planning charges when told to do so by local authorities, so that infrastructure can be provided. The system, therefore, would partially replace Section 106 agreements, which would be curtailed to the provision of affordable housing and costs associated with particular sites.

However, under such a system, as in the case of development land taxes in general, landowners and property developers would still be able to withhold land from use, watching its value rise, simply by not seeking planning permission. And, of course, the planning charges are again merely a one-off payment, and paid only by the developer, and not by neighbouring properties benefiting from the development, which limits the amount of revenue that can be raised.

The empty buildings tax

This new tax on empty commercial buildings, which came into effect in April 2008, is designed to penalise speculators – landowners and property developers withholding land and buildings from the market in the expectation of obtaining higher prices later – and to encourage investment by making it easier for businesses to acquire premises more cheaply. However, this tax is likely to have an effect opposite to that intended.

In particular, in order to avoid the tax, developers have threatened simply to knock down the buildings, leaving derelict sites rather than keeping the buildings available for rent, perhaps on short-term leases while planning permission is being sought to upgrade the buildings, or making some other use of the land.

If LVT were in place, the empty buildings tax would be redundant, since landowners would have to pay LVT irrespective of whether there were buildings on the land. Property owners therefore would have an incentive to let the buildings in order to offset the tax, or else sell the site to others who were prepared to make the necessary investments to make the best use of the land according to prevailing planning regulations. And, of course, unlike the empty buildings tax, LVT would encourage brownfield sites already cleared of old buildings, and land banks held by property developers, to be brought into use.

Conclusion

LVT would obviate the need for development land taxes in whatever guise, and it would have none of their adverse impacts on land use, and on the economy. On the contrary, LVT would help boost economic development, and allow the land that is available to be used more efficiently. Moreover, LVT has a far greater revenue-earning potential, which would provide the government and local authorities with funds to make the necessary investments in infrastructure and public services for the benefit of everyone, and, at the same time, would allow other taxes that have an adverse impact on the economy, and on welfare, to be reduced or withdrawn.

6

The case for replacing the council tax with a land value tax

The council tax is the main source of funding for local authorities that is under their control, and accounts for around 25 per cent of their revenue. Apart from various fees charged by local authorities for certain services – which, on average, contribute around 8 per cent of revenue – the rest comes from central government. Around 45 per cent of local authority income comes from direct grants from central government, including the revenue support grant, the dedicated schools grant, and other specific and special grants. And a further 22 per cent on average comes from central government indirectly through the national non-domestic rates levied on commercial properties, which are set by central government. Though collected by local authorities, the revenue from the national non-domestic rates is pooled, and then redistributed back to local authorities on a per capita basis.

The regressive nature of council tax

The council tax is a deeply unpopular tax. Its biggest problem is that it is severely regressive. The structure of the banding system and the difference between the levels of council tax paid in different bands means that the rate of tax actually falls the greater the value of the property on which it is levied. For example, someone in a house worth £1 million in 1991 pays only twice the amount of someone living in a house worth £70,000, and only three times the tax paid by those in the poorest accommodation.

On top of that, no account is taken of people's ability to pay the council tax, except that single person households receive a 25 per cent reduction in their council tax. This reflects the fact that the council tax is a hybrid tax, partly a poll tax and partly a property tax, and assumes a two person household. In addition, those on very low incomes are entitled to the means-tested council tax benefit, which is claimed by almost half of all households in the lowest band. However, the trouble here is that this creates a 'poverty trap' when people's incomes go up, due to the withdrawal of benefit as earnings rise above a certain level. Furthermore, the take-up of council tax benefit is only around 70 per cent, so that many people, especially pensioners, lose out from not claiming their entitlement.

The 'gearing ratio' problem

Another problem with the council tax is the so-called 'gearing ratio'. Since council tax is the only source of funds under the control of local authorities, accounting for just 25 per cent of revenue, if a local authority wishes to raise total spending by, say, 5 per cent, it will require a council tax increase of 20 per cent, which is a gearing ratio of 1:4. For poor areas, where central government support accounts for a greater proportion of revenue – such as in the London Borough of Tower Hamlets, where the gearing ratio is 1:9 – increasing spending by 5 per cent can mean an increase in council tax of as much as 45 per cent.

In addition, the council tax has to bear the brunt of any shortfalls in revenue caused by central government deciding to cut its support if local authorities are to maintain the same levels of service.

Both factors help to explain why, since 1997, council tax, on average, has jumped by 70 per cent. This has greatly added to the unpopularity of the tax – especially as it is in your face all at once when the annual bill arrives, unlike, for example, value added tax, where the tax is practically invisible, and income tax, which is deducted from earnings on a weekly or monthly basis (though this problem is mitigated to some extent by monthly payment and direct debit arrangements, so that the bill does not actually have to be paid all at once).

The effect of escalating property prices

Also of concern is the effect of the huge escalation of property prices since the last valuation in 1991. This could mean that some people would be in for a sharp increase in council tax. However, it should be pointed out that it is not absolute property prices that determine the level of council tax, but relative prices. Thus, following a revaluation, there would likely be winners and losers, according to whether one's property went down or up a band or two. The losers would be households in areas where house prices have risen more than the national average.

In Wales, where a revaluation has already taken place, 35 per cent of households ended up paying more, because they had moved up a band or two, and 8 per cent ended up paying less, because they had moved down a band. There was no change for 57 per cent, because their properties remained in the same band. However, such is the unpopularity of the council tax, and the uncertain effect that a revaluation might have on households, that the government has twice postponed a revaluation in England, because it was thought to be an electoral liability.

Alternatives to the council tax

The current arrangement for local authority finance is widely recognised as deeply flawed, particularly with regard to council tax.

Some have advocated replacing the council tax with a local income tax. But this is not straightforward. First, because so many people live in a local jurisdiction different from where they work, its collection would be more complex and more costly compared with council tax, especially if it included unearned income not covered by PAYE. It would also be more costly if local authorities themselves became the tax collectors instead of HM Revenue and Customs (in the unlikely event that central government would allow that). Furthermore, it would be inequitable because of the large difference between the mean income in more affluent areas and in poor areas.

On top of that, getting rid of the council tax, would get rid of Britain's only widespread wealth tax – that is, apart from the mis-named inheritance tax, which is often dubbed the 'voluntary tax' because, for those able to afford good tax advisers, it is so easy to avoid (such that, according to some estimates, only around 3 per cent of those to whom it should apply end up paying it).

Another suggestion has been to make the council tax more palatable by increasing the number of bands, especially at the top end, and raising the ratio of tax paid by those in the top band and those in the bottom, from the current 3:1 to, say, 30:1. This would make it less regressive, one of its biggest drawbacks.

But far better would be to replace the council tax with LVT. As proposed in Section 9, this could be the first step towards introducing LVT on a wider scale, nationally. However, as shown by the example of Harrisburg described earlier, even if LVT is retained only as a local tax, perhaps also replacing the national non-domestic rates levied on commercial properties, this would not only benefit the finances of local authorities, but would lead to marked improvements in the local economy, and in the general well-being of the local community.

The Vale of White Horse study

In 2004-5, Oxfordshire County Council conducted a detailed study in Vale of White Horse District to test the feasibility of replacing the council tax and the national non-domestic rates with a land value tax. It demonstrated conclusively that it would be feasible. The only significant problem was that since land use has evolved historically in line with prevailing tax structures, there would be winners and losers following the change. However, as discussed in Section 9, the transition to LVT could be mitigated in a number of ways.

In this particular example, the issue of winners and losers was perhaps more prominent because the area selected for the purposes of this study was isolated from the rest of the county. In practice, if the aim was to collect the same amount of revenue from LVT as currently collected through the council tax and national non-domestic rates, the number of winners and losers in the Vale of White Horse District would be moderated by the amount of revenue collected overall at county level from localities with very high land values, such as the city of Oxford and other urban areas, including derelict or brownfield sites located in those places.

7

Land value tax and overall tax policy

Nobody likes paying taxes. But, leaving aside imperialistic wars of aggression dressed up as defence, and provided the tax system is fair and is seen to be so, people generally accept the need for governments to collect revenue for the provision of services and amenities from which everyone benefits – and which otherwise might scarcely exist. However, different taxes have different economic impacts, some tending to enhance economic activity, thus extending employment and raising earnings, and therefore help to improve social welfare, while others may have the opposite effect.

Pros and cons of different taxes

A famous historical example of a bad tax was the tax on date palms introduced by Muhammad Ali, the Ottoman ruler of Egypt, from 1805 to 1848. The peasant farmers responded by uprooting their trees to avoid paying the tax. But when this tax was replaced by a tax on land, this gave farmers the incentive to grow more palms in order to raise the revenue to pay the tax. This resulted in a bigger crop of dates, which benefited the economy of Egypt and its people.

In today's terms, it is the difference between imposing a tax on the development of land – as proposed in the Barker Review on housing supply, and as put into practice by previous labour governments – and a tax on the land itself. Whereas a development land tax acts as a disincentive to build houses or invest in other productive activities on the land, an annual tax on land according to its value would encourage such investments, because not making optimal use of the land is penalised.

Income tax, which accounts for just over a quarter of government revenue in Britain, should also be regarded as a bad tax because it tends to penalise enterprise and economic activity – the more one works, the more tax one has to pay.

Here, it should be noted that the incidence or burden of a tax does not necessarily fall on those nominally paying it. In the case of income tax, it will depend on workers' relative bargaining positions, which, among other things, is determined by the overall level of unemployment, how much in demand are particular skills, and how well organised workers are. When workers are in a weak bargaining position, more of the tax burden will fall on workers. This would reduce the incentive to work beyond a certain amount because of the higher effective tax rates on additional earnings.

However, when workers are in a strong bargaining position, the tax burden will fall more on the employer, because for a given take-home pay, they will have to spend more on wages than they would if there were no income tax. This will reduce the incentive to employ more workers, and would be at the expense of investment.

Of course, employers, as far as possible, will seek to pass on to consumers the extra amount that they have to spend on wages, in the form of higher prices. How far they will be able to do that will depend on the level of competition for the particular product or service being produced or supplied, as well as overall economic demand. If employers do succeed, it will mean that the income tax burden would have been passed on to consumers. As a result, consumers would have less to spend, which would reduce overall economic demand, and therefore the incentive to invest in new economic activities and jobs, thus having a negative impact on economic growth. It would also weaken workers' bargaining positions, so that more of the tax burden would fall on workers.

Similar arguments apply to other taxes on incomes, including corporation tax, as well as taxes on consumption (which, in effect, is the same as people having to pay out more tax on their incomes), such as value added tax, excise duties, and council tax.

Deadweight losses due to tax

The extent to which a tax acts as a disincentive for people or society to work, invest or consume, and therefore has an adverse impact on welfare, is called a deadweight loss by economists. It is the element or fraction of the tax in which the social cost of the tax exceeds the social benefit – or, in other words, that which prevents mutually beneficial transactions from occurring, such as an employer offering a job, or a consumer or business purchasing some item. The larger the number of transactions impeded by a tax, the higher the deadweight loss.

In the early 1990s, Nicolaus Tideman and Florenz Plassmann, economists at the Virginia Polytechnic Institute and State University, estimated that the British economy was achieving only 55 per cent of its potential due to such deadweight losses (see'Taxed out of Work and Wealth: The Costs of Taxing Labor and Capital' in Fred Harrison (ed.), *The Losses of Nations*, Othila Press, 1998). It was on this basis, updating the figures to 2001, that Ronald Banks, in his book, *Double-cross* (Centre for Land Policy Studies, 2002), calculated that every year, Gordon Brown (then the Chancellor of the Exchequer), 'deprives each man, woman and child in Britain of £15,000 … on TOP of the taxes he collects from us'.

However, neither of these studies took into account the offsetting knock-on effects derived from governments spending the tax revenues. Thus, whether spent on wages or on capital goods for the public sector, new economic demand is created. This stimulates investment and employment in the production and supply of goods and services to meet that demand, leading to further growth of economic demand, and so on.

Furthermore, they disregard the extent to which some people and businesses strive to work longer hours in order to compensate for the tax that they have to pay, which, if invested intelligently by governments, would lead to higher growth and improved welfare. And they ignore the welfare gains arising from the existence of public services and social security that should be part of any civilised society, and which depends on government revenues from taxation.

Nevertheless, the studies do beg the question of how to raise revenue and at the same time minimise deadweight losses.

This could be achieved by biasing taxation towards those activities or commodities for which supply or demand is least affected by variations in price or cost – or, in economists' parlance, those whose supply or demand is least elastic.

The most obvious examples used by mainstream economists are those commodities that are most highly taxed in Britain, namely tobacco, alcohol and petrol. Their effective tax rates range from 50 to 90 per cent. Another candidate would be food, but this is regarded as too important for people's welfare to tax, especially as so many people at the moment are paid so badly that they can barely afford the foods that they need even without tax.

But the best example of a commodity whose supply is almost wholly inelastic, and therefore a good candidate for tax, is almost entirely ignored by mainstream economists – namely land. If land is taxed according to its value – which is mainly determined by the demand for land in particular localities – there would be no deadweight loss. Based on this argument, land should be the most heavily taxed item of all.

The advantages of a tax on land value

Apart from the fact that a land value tax carries virtually no deadweight loss, its revenue earning potential is huge. Thus, various studies, including that of Banks mentioned above, have estimated that introducing LVT into Britain could raise at least £200 billion a year in 2002 prices. That was more than the combined revenue of £174 billion from income tax, corporation tax, capital gains tax, inheritance tax, stamp duties, insurance premium tax and all council taxes and national non-domestic rates, in that year, corresponding to around half of all government revenue.

Moreover, as discussed, because LVT would stimulate investment and economic activity, which would raise the demand for land, and therefore land values, the amount of revenue that could be collected through LVT would tend to increase considerably over time.

In addition, a land value tax is inherently a fair tax, because the value of a site upon which the tax would be based is determined not by the owner or occupier, but by its location, and the social and economic activities of society as a whole, and by what nature has provided, which should be shared by all. And unlike other taxes, LVT does not take anything away from landowners that they themselves might have created. In fact, LVT provides automatic compensation for those sites that are disadvantaged in some way as a result of other developments, such as proximity to a busy road, a rubbish dump, or whatever.

Also, LVT is fairer because it is practically impossible to avoid. People do not end up having to pay more tax to compensate for those who evade it. In the case of income tax and taxes on business, there is a flourishing 'shadow economy' and a whole army of tax avoidance experts totally geared to helping people and businesses evade tax, making extensive use of the various offshore tax havens. But you cannot siphon out land into an offshore tax haven!

A further advantage of LVT is that it has a built-in counter-cyclical mechanism. When there is an economic downturn for whatever reason, land values tend to fall so that for a given rate of tax the amount of LVT due would also fall. This would mean that people would have more to spend, thus helping to boost economic demand, and therefore investment and employment, and businesses would have more to invest, all of which would help to offset any economic downturn.

The government, of course, would get less revenue, but this could be compensated by the government accumulating the higher revenues obtained from LVT when the economy was expanding, which would tend to raise land values. This counter-cyclical effect of LVT, of course, would depend on the regular updating of land values.

Proposals for a fairer and economically more beneficial tax system

The economic benefits of LVT – and the fact that it is practically impossible to avoid – has led some enthusiasts to advocate abolishing all other taxes and replacing them entirely with LVT. However, LVT is unlikely to provide enough revenue to finance all the needs of a modern state – especially if governments became more actively involved in pre-empting market failures and economic downturns, which it is becoming increasingly obvious is needed now that prevailing neo-liberal economic policies are running into the sand.

In short, other taxes will continue to be required, albeit at lower rates. In addition, such taxes can frequently play an important role in achieving other policy objectives.

For example, a progressive income tax in a highly unequal society such as Britain's helps the tax burden to fall more heavily on those who can afford to pay. Once society became less unequal, income tax would become less important in this respect. It is therefore proposed that income tax should be gradually phased out as LVT was extended.

The only exception would be tax on very high incomes – such as the earnings of footballers, pop stars, actors, opera singers, high court judges, and top managers, whose situation is analogous to land in that their skills are practically unique, yet are in high demand. Supply, therefore, cannot be increased in line with demand. In other words, a large part of the value of their skills, which is reflected in their high earnings, is created by society, so that it is only fair that society should get back a proportion of that value in the form of tax. It is therefore proposed that income tax – perhaps re-named surtax – be retained for very high incomes, and at a higher rate than now, especially as the tax would carry no deadweight loss.

Meanwhile, it is proposed that recurrent expenditure on pensions and healthcare should continue to be financed through contributions out of people's earnings, perhaps topped up by employers' contributions. As argued elsewhere, this is by far the most cost-effective and the fairest way of providing these services (see Jerry Jones, *The future of pensions – how to ensure a decent retirement for all*, CPB, 2006). It is recommended that these contributions be ring-fenced, and paid into a National Pension Fund, and National Health Fund, respectively, managed by statutory authorities, under democratic control, independent of the government of the day. People could then be sure that the money that they were paying out is actually going into those areas. The contributions should be seen as a part of people's wages or salaries that are deferred until they retire, giving an assured income until death, or as an insurance premium to cover healthcare when people or their families are in need of it.

If these payments were clearly earmarked for the purposes intended, and kept quite separate from the government budget, they would be widely accepted, and would carry no deadweight loss.

Next, it is proposed that a corporation tax (that is a tax on profits) be retained and, beyond a certain threshold, the rate raised in steps to 50 per cent (which is what it was in most countries in the 1960s and 1970s). The argument in favour is that some productive activities are inherently more profitable than others, yet are dependent on less profitable or unprofitable activities. Such a tax on profits would help finance those less profitable, but nonetheless essential, activities, especially public services and infrastructure, upon which all productive activities depend.

A further argument for such a tax is the fact that, under capitalism, the bulk of company profits derives from surplus labour appropriated from employees and from customers and suppliers. In effect, therefore, the higher profits of the more profitable activities are derived from the rest of society, and it is therefore only fair that they be taxed.

In addition, it is proposed that all exemptions and allowances, which companies can use to set against tax, and which are subject to so much abuse, should be abolished.

A recent investigation by the *Financial Times*, for example, found that several major corporations in Britain, including some foreign banks, are currently paying almost no tax. They achieve this by arranging for most of the profits to be made by foreign subsidiaries, often based in offshore tax havens – such as by taking out large loans from their subsidiaries and setting the interest payments off against tax, or through transfer pricing.

A problem with raising the rate of corporation tax under the current neo-liberal regime is that some businesses might seek to relocate in order to avoid the tax, thus putting people out of work. Thus, it would probably be impractical to follow through with this policy immediately. It will have to await for the folly of current neo-liberal polices to become more universally recognised, which will happen as they get into increasing difficulties, so that it becomes acceptable once again for governments to make use of capital controls and other types of interventions (such as taking over businesses threatening to relocate and turning them into worker-owned enterprises).

Such a policy would also depend on the abolition of offshore tax havens – or making dealings with affiliates based in offshore tax havens illegal. It was precisely the mushrooming of transactions through offshore tax havens that undermined such policies previously.

Furthermore, it is proposed that taxes on consumption, including value added tax and excise duties, which currently account for almost a third of government revenue, be retained – or preferably turned into a simple sales tax at different rates for different products (though, at present, this would contravene EU commitments). In addition to raising revenue, the object here would be to encourage restraint on the excessive consumption of natural resources, and, by varying the rates, to favour economic activities that have a smaller environmental impact, and generally shift the economy towards a more sustainable basis.

Along with land value tax, therefore, such a tax can be regarded essentially as a 'green tax'. Like land value tax, a sales tax also has the advantage that it is hard to avoid, even in this increasingly mobile world, since residents and visitors alike would have to pay it. Its regressive characteristics could be drastically reduced by making incomes much more equitable than they are now. Over time, the rates of tax could be reduced by raising the rate of land value tax, thus reducing the disincentive effect of such a sales tax.

In addition, it is suggested that other environmental taxes be retained, or extended, to stimulate investment in measures to reduce or recycle waste, to reduce carbon dioxide emissions, and to combat the adverse effects of climate change.

Finally, it is recommended that certain other taxes that do not necessarily raise much revenue, but are important mechanisms for preventing the avoidance of other taxes, and are in the interests of fairness, be retained.

For example, other things being equal, it would be possible to avoid income tax or corporation tax by reclassifying income from earnings or profits as capital gains. Hence the need for a capital gains tax. Similarly, the inheritance tax, among other things, helps to combat individuals transferring profits or income to heirs in order to avoid tax.

It should also be pointed out that having a broad range of taxes allows revenue to be raised at a lower rate for each tax than otherwise, thus lessening their burden, and reducing the incentive to find ways of evading the particular tax.

To sum up, it is proposed that LVT should become the core source of funding for public expenditure, which would be topped up by other taxes that also benefit society in various ways.

8

A strategy for introducing a system of land value tax in Britain

Obviously, moving to a system of land value tax and allowing it to displace other taxes will cause some disruption. But much can be done to ease the transition. The important thing is to get the process started, so that society, rather than landowners, begins to benefit from the land value that society itself creates, and advantage taken of its profound economic benefits.

Completing the registration of land

The first task would be to complete the registration of land still not registered, which is mainly that owned by big wealthy landowners. This would be the responsibility of the Land Registry, first established in 1925. The process could be accelerated by requiring owners of unregistered land to register it by a certain date, after which local authorities could be given the power to lease out any unregistered land. Meanwhile, the steps required for introducing LVT could go ahead anyway.

Setting up a system for valuing land

The first step would be to set up a system to value all land using methods that are already available. As noted earlier, once the system of land valuation was up and running, it would be relatively easy to update land values more or less continuously. This is desirable since land values can fluctuate considerably for the reasons already given (see Section 4).

Apart from certain industrial sites occupying a large area, or other specialised sites, it would not be necessary to value every site individually. Using modern computerised techniques, it would be possible for most land to be placed in bands of similar value per hectare (or square metre) in a 'land-value-scape', as described in Section 4, so that once the area of a site is known, its value can easily be ascertained, which would be in the public domain.

This would not only have the advantage of reducing the costs of valuation. It would also reduce the costs of appeals against valuation decisions, because such appeals would mainly be confined to sites close to the border between two different bands. This is born out by the current system of local taxation. Thus, the cost of appeals against valuations for the council tax, for which properties are placed in bands, is fairly trivial in relation to the number of properties. But for the national non-domestic rates, for which properties are assessed individually, the cost of appeals is considerable – indeed, some four times the cost of producing the ratings lists in the first place.

However, for the purposes of LVT, it would be desirable to expand the number of bands considerably beyond the number used for council tax purposes.

How best to introduce LVT

Next, how best to introduce LVT would need to be decided. On balance, it would make sense to introduce LVT gradually, which would allow time for the economy to adapt to the new system of taxation.

The disadvantage of a more gradual approach is that it would give a chance for vested interests, such as big landowners, to mount a campaign against LVT before its beneficial effects had begun to be realised. It would be up to the government, and hopefully opposition parties, to face down such a campaign, and be resolute in demonstrating the very real economic and social benefits of LVT, pointing out that LVT is not strictly a tax in the normal sense, but, in effect, a payment to the community for the space one occupies, and therefore much fairer than some of the other taxes that it is seeking to replace.

The most obvious starting point for introducing LVT in Britain would be to use it to replace the much-discredited council tax, and the system of national non-domestic rates – and perhaps also the stamp duty land tax.

After that, the next step, logically, would be to extend it gradually to replace central government grants going to local authorities which, currently, on average, account for nearly half the revenue of local authorities. This would be a first step towards substituting LVT for income tax – which, in effect, is what funds central government grants going to local authorities.

It would be important to reduce other taxes pro rata as LVT was extended beyond local level, and as the rate of LVT was raised, so that LVT would be seen genuinely as a replacement tax, and not an additional tax burden.

Measures to ease the transition

Since economies, as well as land use, tend to evolve alongside prevailing tax structures, it is inevitable that the process of replacing existing taxes with LVT will give rise to winners and losers. There will therefore need to be a number of transitional arrangements.

Of major concern during the transition period would be the extent to which LVT would penalise those living in areas where the value of their properties had increased sharply over the years (due to rising land values), while their incomes had not grown proportionately, or perhaps had gone into decline if they had become pensioners or unemployed, or had been widowed. This could also apply to established businesses. The problem could be mitigated in a number of ways.

First, people – and also businesses – could simply choose to increase the occupation of the premises, for example, by taking in lodgers or sub-letting. Alternatively, they could move to smaller properties or to areas where land values were lower. This, indeed, is one of the long-term objects of LVT – to encourage the more efficient use of the land that is available.

Second, for residential properties, pensioners and others with low incomes could be allowed to defer (or roll over) the payment of LVT, either wholly or in part, until the property was sold or transferred. This would enable people to carry on living in their properties at no extra cost, and, if they so chose, to pay less tax than they do now.

However, it is only fair that the tax plus interest should be paid eventually, because the increased value of their properties – or more precisely, the value of the land on which their properties stand – would have been created by the activities of the community as a whole, and not by those who happen to occupy the particular site. Meanwhile, local authorities could obtain the revenue that they otherwise would have received from low cost loans, using as collateral the stream of income that they would eventually receive.

A third suggestion has been to introduce a 'home allowance' for main residences (similar to the personal allowance on income tax), which would act as a threshold before LVT was levied. This, it is claimed, would help ease the tax burden of people on low incomes.

However, the problem here is that since the LVT levied would be lower than otherwise, this would have the effect of raising the land value of the site, so that more tax would be paid, which could more or less neutralise the effect of the 'home allowance'. Furthermore, because the effective rate of LVT would be lower, this will tend to make property prices higher than they otherwise would be, so that people would lose out when seeking to acquire a new property. (And it would defeat one of the objects of LVT, which is to minimise the price of land in order to maximise investment on the land, and in the economy at large.)

Far better would be to address the issue of low incomes directly, for example, by arranging for those on very low incomes to receive something like the current council tax benefit – at least until wages and pensions have been raised sufficiently for people to be able to afford their various outlays, including LVT.

The continuing role of planning regulations

Planning regulations would continue to work alongside a system of LVT. It is sometimes suggested that LVT would lead to increased urban sprawl as people and businesses sought areas on the outskirts of towns with lower land values in order to save money. However, planning regulations, preferably with greater transparency than now (including bringing the newly centralised planning authority under democratic control), would prevent that.

Furthermore, there may be instances when the local community might, for one reason or another, want to preserve the productive activities of certain businesses in the neighbourhood, for good social reasons. If located where land values are high, perhaps in the centre of towns, it is likely that some businesses might lose out to those better able to afford the LVT levied on the site, which would be a loss to the community.

However, this could be prevented simply by placing restrictions on how a particular site was used, through the planning system. This would reduce land values in these particular cases, and therefore their liability for LVT. Similarly, parks and open spaces, including school sports fields, could be exempted from LVT because planning regulations would, in effect, reduce their land value to zero.

Should a land value tax be local or national?

So far it has been assumed that local authorities would collect the bulk of LVT, at least in the first instance. However, if it remained local, this could give rise to a number of problems, not least the tendency to perpetuate the considerable inequalities that exist right now among different localities, especially if local authorities were free to set their own rate of tax.

In particular, there are huge variations in the costs of services that different local authorities have to provide – related to such things as the age structure of populations and the number of people on low incomes in the different localities – and therefore variations in the amount of revenue that they need to collect. Furthermore, many areas with high land values have large concentrations of poor people, who, perversely, might find themselves having to pay more LVT compared with more affluent areas, where land values are lower. Moreover, many poor people live in badly rundown areas, where the amount of LVT collected would be insufficient for the investment in public services and in other economic activities required in order to meet people's needs, and to regenerate the area.

Then there is the issue that land values are not only, or even primarily, generated locally. The higher land values in many large towns and cities, notably London, derive not only from their citizens' own efforts and resources, but also from the economic activities taking place far beyond, perhaps in the nation as a whole, or even in other countries. The land value that these activities generate, therefore, cannot be said to belong solely to the inhabitants of those towns or cities.

In short, if LVT were collected only locally, some local authorities would be in a position to raise the revenue that they require from a relatively low rate of tax, while others, say, in the hinterland of large towns or cities, or beyond, where land values are low, might find themselves having to set a higher rate of LVT in order to obtain the revenue that they require, because they would receive nothing for the contributions that their citizens make towards raising land values in the nearby towns and cities.

A way out of such problems would be for central government to set the rate of LVT nationally, and for all revenues from LVT to be pooled centrally, which would then be redistributed back to local authorities, partly on a per capita basis, and partly according to assessed needs. This is roughly the system now. Thus, the revenue from national non-domestic rates is pooled centrally and redistributed on a per capita basis, while the various central government support grants, which make up around half of local authority revenue, are distributed more or less on the basis of need. Only the council tax element of local authority finance, together with the fees charged for various local services, which account for around a quarter of local authority revenue, is decided locally, and even that is governed to some extent by rules set by central government.

A disadvantage of a centrally controlled scheme for LVT – in which both the rate of LVT, and how the proceeds of LVT are allocated to local authorities, is decided centrally – is that it would, in effect, divorce the collection of LVT from the services provided by local authorities. This, arguably, would undermine the relationship and accountability of local politicians to their constituents, representing a 'democratic deficit'. Indeed, this is very much one of the criticisms levelled at the current system of local authority finance, in which some 75 per cent of revenue derives from central government, either directly, or through the redistribution of the national non-domestic rates.

However, under such a centrally controlled system, local politicians would still largely be responsible for how the funds at their disposal are spent, for which they would be answerable to their constituents, so to that extent democracy would prevail. Furthermore, local politicians, acting on behalf of the citizens whom they represent, would always be able to lobby central government agencies for more funds for particular purposes, under the various formulae and rules devised for deciding how the revenue from LVT is allocated. This could be made more democratic through the creation of an independent appeals body comprising elected representatives of local authorities.

In short, provided the system and rules for redistributing LVT back to the local areas are reasonably transparent, it is a bit of an exaggeration to claim that the centralised system of LVT as proposed here would result in a 'democratic deficit'. In any case, surely, reducing the current inequalities among different neighbourhoods and localities is also a democratic issue, which only a more or less centralised system can address.

Over time, once those inequalities have been ironed out reasonably, it is possible that more power can be given to local authorities to set a rate of LVT to cover their expenditure. Meanwhile, as LVT increasingly replaced income tax and other taxes that finance central government expenditure, setting the main rate of LVT would, obviously, have to be the prerogative of central government – or more appropriately Parliament, to which the central government is accountable.

If this system is eventually adopted, it would mean that, once the land value of a particular site is determined, a certain percentage rate of LVT would go to local authorities, which would be set by local councils, and another, perhaps somewhat larger, percentage would go to central government, and would be set by central government.

Getting the argument across

It is all very well to argue in theory that society as a whole should benefit from the rising land values that society itself creates, rather than just the individuals who happen to own or occupy particular sites, and who are not responsible at all for their rising values. But winning over people and governments to a policy to achieve those ends through a system of land value tax, has a number of difficulties to overcome.

First, how land acquires value independently of the value of buildings or productive activities based on the land is not immediately obvious. It should, of course, be part of the geography curriculum in schools, but rarely is. Even economics courses in universities, and the economics textbooks that they use, do not normally cover this issue.

Similarly, although many articles have appeared in the press recently on house price inflation, few have shown any understanding that this is due almost entirely to rising land values, since buildings tend to decline in value over time due to wear and tear, and obsolescence. This confusion is not helped by the legal definition of land, which, unlike the economic definition, includes buildings on the land.

Furthermore, a land value tax in the public mind is often confused with other types of land tax – notably land development taxes under various guises that have been introduced by governments from time to time, and then abandoned because of their problems. As explained previously (Section 5), such taxes, more often than not, have had a negative impact on land use and on the economy. This has helped to give any tax on land a bad name.

Then there is the perceived difficulty of valuing land. It needs to be understood, as discussed in Section 4, that it is easier to value land than to value buildings, particularly with the availability of modern information technology. It is also fair to point out that in spite of the greater difficulty of valuing buildings, this has not deterred governments from imposing taxes on property (that is the buildings together with the land on which they stand) – and the general public has more or less accepted such taxes (albeit, perhaps, as a necessary evil).

The task for supporters of LVT is to convince people to have trust in the system of land valuation, and that taxing land values is a matter of natural justice, and fairer than most other forms of taxation.

Finally, people need to be persuaded that they will be better off under a system of LVT. The trouble here is that some of the benefits of LVT take time to be realised. For example, the incentive that LVT gives to developing sites to their full potential, thus creating jobs and homes, will not happen overnight. Moreover, much would depend on other economic policies, and developments taking place in the global economy.

Meanwhile, it needs to be ensured that LVT is genuinely a replacement tax and that for most people, when LVT is introduced, there would be a noticeable reduction in other taxes.

Addressing concerns about the effect of LVT on property prices

Since some 70 per cent of Britain's population are either homeowners who own the freehold of the land upon which their homes stand, or have a vested interest in owner-occupied properties as heirs, how LVT might affect property prices is an important issue, both for the general public and for governments thinking about introducing LVT.

First, if, as recommended here, LVT was introduced initially simply as a replacement for existing property taxes – namely, the council tax for domestic properties and the national non-domestic rates for commercial – it would have little or no effect on property prices. That is because those existing taxes would already have had the effect of making property prices lower than they otherwise would be. However, it is true that once LVT was extended beyond that, so that it began to replace other taxes, this would tend to reduce land and property prices.

But, as explained already (see Section 4), this would be offset by the increasing land values due to economic growth, which LVT would tend to enhance. Besides, over the period during which LVT would be gradually extended, as proposed here, property prices would likely be much more affected by other factors – in particular the availability of credit, and the performance of the economy as a whole, including the international economy. This would tend to mask any effect LVT would have on property prices.

Counteracting propaganda against LVT

The downside of introducing LVT gradually or in stages is that it would allow time for powerful opponents of LVT with considerable financial resources and political clout, such as big landowners and their allies in the media, to mount a damaging propaganda campaign against LVT. Once introduced, they would likely use any excuse or economic setback to denigrate LVT, and to argue against its extension (which is what would be needed for its full fruits to be realised), never mind that such events had nothing to do with LVT.

A government seeking to introduce LVT, therefore, would have to be prepared to face down such opponents, exposing their vested interests – perhaps making use of the arguments advanced in this pamphlet!

The point is that even capitalists would gain from a land value tax – even big landowners if they sold their land and invested the proceeds in other productive activities. The only exception would be those engaged in land speculation.

Conclusion

As shown here, and as is evident from other countries that have implemented some form of LVT, the benefits of LVT are overwhelming. Not only does it have huge revenue earning potential for governments to pay for infrastructure and public services upon which the rest of the economy depends, but also it has a major positive impact on economic development, first because it stimulates investment, and second, because it enables other taxes that have a harmful effect on the economy to be reduced or eliminated.

Once people and governments have been won over, experience from other countries shows that the actual mechanics of introducing LVT is relatively simple. But first people and governments have to be won over – hopefully through a concerted all-party campaign across the political spectrum, since the social and economic benefits of LVT cut across economic systems and political ideologies.

Summary of proposals for a new fairer tax system

1. Abolish the council tax, stamp duty land tax, and the system of national non-domestic rates and replace with a system of land value tax.

2. Phase out income tax at the standard rate, and gradually raise the rate of land value tax to compensate.

3. Retain an income tax or surtax for very high earners.

4. Continue to fund recurrent expenditure on pensions and healthcare through employee and employer contributions, but paid into a National Pension Fund and National Health Fund, respectively, managed by statutory authorities under democratic control, independent of the government of the day.

5. Retain the corporation tax or a profits tax beyond a certain threshold, eventually, raising the rate of tax in steps to 50 per cent (once governments have been persuaded to abandon the prevailing neo-liberal economic policies).

6. Abolish value added tax and excise duties, and replace with a simple sales tax extended to all products, but at varying rates according to the product, which, in addition to raising revenue, would be geared to achieving various other policy objectives.

Appendix 1: Who owns Britain's land?

Information on land ownership in Britain is not easy to come by. Kevin Cahill discovered this when researching for his book, *Who Owns Britain* (Canongate, 2001), from which much of the information contained here is drawn. The Land Registry, in existence since 1925, has managed to register not much more than half. What's missing is the land owned by the rich.

However, during the course of piecing together information from press cuttings, and records of wills and estates, Cahill heard about a 'second Domesday Book', a report submitted to Parliament in 1876. He asked the Royal Agricultural Society if they had a copy. They assured him that there was no such thing. In fact, as Cahill discovered later, the Society possessed several copies in its library. The Country Landowners Association at least admitted to having a copy but refused to let Cahill see it. Eventually he was able to obtain a copy of extracts from Ealing library, and later a view of the whole thing in the Devon and Exeter Institute.

The report, entitled *The Return of Owners of Land*, contains the names, addresses, acreages and valuations for all landowners of over one acre. As Cahill put it, 'the UK's large landowners had been appalled by its appearance and moved, with their academic friends, to bury it. In this endeavour they were eminently successful, with nothing of significance written about it in 126 years.... It had, in effect, vanished'. Having rediscovered it, Cahill was able to trace most of the missing estates, and in many cases discover their current owners.

He found that just 189,000 families own two-thirds of the UK's 60 million acres, of which nearly three-quarters is owned by the top 40,000. The biggest individual landowner turned out to be the Duke of Buccleuch with 277,000 acres, and the wealthiest was the Duke of Westminster with 140,000 acres, including 100 acres in London's Mayfair – which alone, in 2001, was valued at £3.35 billion – as well as 200 acres in Belgravia, its even more expensive neighbour. Land owned and controlled by Britain's Royal Family, comprising the Crown Estates, the Duchies of Cornwall and Lancaster, and private land, amounted to some 677,000 acres. Meanwhile, Britain's 16.8 million homeowners accounted for barely 4 per cent of the land, about the same as that owned by the Forestry Commission, the top institutional landowner. But Cahill still could not account for some 5.6 million acres, or nearly 10 per cent of Britain's land area.

Most of the big private estates can be traced to appropriations and handouts from the reigning monarch in bygone days, and more recently through purchases by those who had made money through large-scale theft in other ways. The 'first great land grab' came with the Norman Conquest when William donated the lands acquired to himself and his brigands. The second came when Henry VIII dissolved the monasteries, and distributed their 10 million acres to those followers and barons willing to accept the new Church, now free from domination by Rome, and impose it in their local areas. Thirdly, some major redistributions and awards of land according to political allegiances took place during Cromwell's rule and following the Restoration.

Private ownership of land in Britain was consolidated further between 1700 and 1900 when common land used for grazing was incorporated into private estates through the various Enclosure Acts pushed through Parliament by the big landowners or their representatives. Most freeholds of owner-occupied houses and businesses that exist today derive from the big landowners cashing in from selling off small parcels of their land to property developers.

Appendix 2: How a land value tax would help resolve Britain's housing crisis

The main manifestation of the housing crisis until recently has been the huge increase in house prices, which has put home ownership beyond the reach of many people. Between 1996 and 2008, house prices rose by 150 per cent in real terms. Meanwhile, the shortage of rented accommodation has pushed up rents. Thus, for many people, a decent home has become unaffordable. Furthermore, people desperately seeking to procure a home of their own have often been trapped into borrowing far beyond their means, and at considerable risk to themselves.

Now, however, the housing crisis is taking a new form. First, rising interest rates for home loans are pushing up the cost of mortgage repayments. This is creating considerable financial difficulties for many families. And it is leading to a growing number of defaults, resulting in people losing their homes. In addition, credit is less available now, so that it is more difficult for people, especially first-time buyers, to obtain mortgages unless they have a sizeable deposit. Another problem is that house prices are beginning to decline, such that many homeowners – mainly those who took on mortgages when prices were at their peak – are experiencing negative equity, or owing more than their house is worth.

The causes of escalating house prices

The huge increase in house prices over the recent period was due almost entirely to rising land values, and the increasing demand for housing relative to supply. The actual cost of building houses has changed hardly at all.

One reason for the rise in land values and house prices, as implied already, is quite simply economic growth. Economic growth increases people's disposable income, and therefore their purchasing power. This increases economic demand for all goods and services, including housing, and therefore demand for land for housing. Since the supply of land in locations where people want to live cannot be increased, the higher demand for housing will result in higher land values and higher house prices.

Another factor that has pushed up the demand for housing, and its price, is growth in the number of households. First, this is due to Britain's rising population. Second, it is because of the increasing number of single person and single parent households – a consequence of an ageing population and other social trends.

However, none of these reasons is sufficient to explain the huge scale of the increase in house prices.

The major reason was the huge growth in the availability of credit. This was the result of banks and other financial institutions inventing new ways of re-packaging housing debt into bond-like securities with various hedging devices, and selling them on in the world's capital markets, mainly to financial institutions seeking a steady flow of funds which mortgage repayments can provide. In other words, banks were borrowing from the world's capital markets, using their mortgage assets as security.

This allowed them to expand hugely the amount of credit that they could make available to house buyers. Furthermore, in their drive to gain business ahead of their competitors, banks greatly relaxed their conditions for home loans in the belief that they had hedged against defaults making use of the various complex hedging devices traded on the capital markets, and were therefore prepared to take much greater risks in their lending. In particular, they allowed people to borrow much more in relation to their income compared with previous times, often without even requiring a deposit.

In short, this easy availability of credit meant that people had more money to spend on homes. This pushed up demand, and therefore prices, because, first, it takes time for builders to build new houses in response to the growing demand, and second, it pushed up land values in the areas where people wanted to live, and where planning permission had been granted for building more houses.

Moreover, the higher house prices increased the value of the collateral that people could put up to take on loans using their houses as security, and therefore the amounts that they could borrow. This raised further the demand for houses, which pushed up prices even more. In other words, as long as banks made credit easily available, the rising price of housing, in effect, fed on itself.

In addition, this huge expansion of credit availability had knock-on effects on the rest of the economy, which also tended to push up house prices. As the increased funds that people had at their disposal filtered throughout the economy at large, this created new economic demand for goods and services in general. This stimulated investment to meet that demand, thus creating new employment opportunities, which led to further growth of economic demand, stimulating more investment, and so on.

In other words, it allowed the economy to grow faster than it otherwise would. The expansion of credit, therefore, not only had a direct impact on demand for housing which pushed up prices, but also had an indirect effect in that it led to faster economic growth, which pushed up land values, causing house prices to rise even more.

A further major cause of rising land values and the increase in house prices was the speculative element and tacit collusion among house builders and property developers. First, many purchasers of property, especially those buying property to let, were driven by the expectation of higher prices later, enabling them to profit from the capital gains to be had when they sold on their properties (which, in the case of buy-to-let, allowed profits to be made over and above the income from the high rents that they could charge). The profits to be had from the buying and selling of property attracted more buyers onto the bandwagon, which further increased demand. This had the effect, of course, of increasing prices all the more, so that investing in property became a self-fulfilling, one-way bet.

Meanwhile, many large landowners, including house builders, have been withholding land from the market in the expectation of making higher profits later when the land, with or without housing, was eventually sold. In London, for example, according to the Royal Town Planning Institute, there was enough land with planning permission in 2007, to deliver some 30,000 houses each year until 2016. And in some areas of the country, it is reported that local property developers have land banks that are likely to last until 2050.

On top of that, it was estimated in 2008 that there were some 750,000 properties standing empty in Britain – over 40 per cent long term empty.

In short, there is evidence that an artificial shortage in the supply of housing has been created. This, obviously, has had the effect of pushing up house prices, allowing property developers to profit at the expense of people seeking places to live.

The shortage of affordable rented accommodation

The shortage of affordable rented accommodation is also a factor that has pushed up house prices because people who might otherwise have settled for rented homes were pushed into seeking properties to buy, thus adding to the already high demand.

A major cause of this shortage has been successive governments and local authorities selling off public sector housing at subsidised prices, and their refusal to replace stocks sold off. In 2007, for example, just 251 housing units were built by local authorities, compared with 16,600 in 1990.

Private sector landlords, meanwhile, have been taking advantage of this situation by charging exorbitant rents to people unable to get onto the housing ladder, or who are stuck on waiting lists for social housing. In 2008, almost 1.7 million households were on council house waiting lists – up by 60 per cent since 2001. And once the credit crunch takes effect (see below), it is expected that this figure by 2010 will grow to 2 million – affecting some 5 million people including children. Furthermore, the number of homeless has risen to over 80,000 households. And this is a conservative estimate, since only those regarded as homeless by local authorities are counted, and it does not include people – especially young people – who are forced to stay with parents, relatives or friends, because they cannot afford a home of their own

Many local authorities now are wanting to raise funds to expand their housing stock to deal with these problems, but are hamstrung by government restrictions on their powers. A further problem is that even if local authorities were able and willing to invest in more public sector housing, they are constrained by the high cost of land. This applies also to housing associations – on which the government and local authorities have become increasingly dependent for providing social housing.

Britain's planning system and its effect on land prices

Britain's planning system has sometimes been blamed for the apparent shortage of land for affordable housing because it makes land prices higher than otherwise due to the restrictions it places on land use. If there were no such restrictions, if there were a market free-for-all, land for building, it may be argued, could be a fraction of the price it is now. Thus, if planning constraints did not exist, it is likely that land prices would tend to converge. It would make prices of agricultural land, especially in the so-called green belt areas around towns as they exist now, much higher, and the price of land already built on, eventually, much lower, especially on the outskirts of towns, as supply of land for building on caught up with demand.

But it would also lead to considerable urban sprawl spreading deep into the countryside as in the United States, where planning restrictions are more relaxed. Furthermore, derelict or brownfield sites in towns would be even more of a problem than now – also a characteristic of US towns – because it costs more to develop brownfield sites, which have the extra costs of demolition and clearing, than to develop greenfield sites.

In Britain, across the political spectrum, nobody advocates a land free-for-all. And there is a general consensus that the countryside should be more or less protected for agricultural and recreational uses. How therefore may the supply of land for affordable housing be increased that is consistent with planning regulations?

Though releasing some land in a controlled way from the green belt could certainly contribute, the first priority, surely, must be to ensure the efficient use of land in towns – especially making use of brownfield sites, which are not only a waste of resources, but are often an eyesore.

By far the most effective and proven measure to accomplish this, as discussed already, would be the introduction of an annual tax on land values. If, unlike now, the owner of a high value site, had to pay an annual tax set at an appropriate level, whether or not he or she brought it into use for the designated purpose, there would be a powerful incentive to start developing it as soon as possible, or else sell it on to someone who will. In effect, this would increase the supply of land, and therefore tend to dampen the price of land. And derelict land in towns would soon become a thing of the past. The example of Harrisburg, given earlier, well illustrates this point.

In due course, as buildings in an area came to the end of their useful lives, if there was the need, planning authorities could re-designate the land for denser housing – or if the priority were more jobs, for commercial use.

In short, Britain's planning system, alongside a system of land value tax, would go a long way towards making more land available for building on, which would help overcome the current shortage of affordable housing.

Why house prices are now falling – and the consequences

The primary cause of falling house prices now, which reflects falling land values, is the sudden large decline in the availability of credit. This has had the effect of reducing economic demand for houses (that is people wanting houses and with means to procure them).

The reason for the decline in credit availability was the sudden drying up of funds from the world's capital markets upon which, as noted already, the huge expansion of credit in the previous period depended. This problem originated from the fact that banks, in order to retain their share of the mortgage market, or, if possible, to get ahead of their competitors – and in the belief that they had safeguarded themselves against defaults – took ever greater risks. They extended their lending to people who would likely struggle to keep up mortgage repayments, especially in the event of rising interest rates, or due to an economic downturn when borrowers were at risk of losing their jobs.

In the United States in particular, between 2001 and 2004, mortgage brokers and the like were arranging home loans for anybody and everybody, whether or not they had any collateral security or steady jobs. This was when interest rates were below 2 per cent, making such deals quite attractive to borrowers, even those on low incomes. The worst lenders were luring people on low incomes into buying houses by offering loans with interest rates starting very low for a limited period, with no indication of what would happen once the market rates of interest began to apply. When, later, interest rates more than doubled, many borrowers had trouble keeping up their mortgage repayments and fell into arrears.
This paved the way for a growing number of repossessions and debt write-offs.

Once this began happening on a large scale – at first, mainly in the United States, where this so-called sub-prime lending had gone the furthest – the various dealers in structured debt securities began realising that they were not such a good bet after all, and would not provide the steady income that they had anticipated. The net effect was that banks suddenly found that their access to funds on the capital markets through such mortgage-backed securities was cut off, which meant that they could no longer continue lending on such a large scale.

On top of that, banks found themselves in a liquidity crisis. In their struggle to gather funds to offset the growing number of defaults and the costs of repossessions, banks were much less willing to lend to one another, and the rate of interest on the inter-bank market shot up. At the time of writing, this had already led to the insolvency of three major banks – Northern Rock in Britain, and Bear Stearns and IndyMac in the United States. And there have been major interventions from central banks to try to ease the situation.

In short, banks are no longer willing or able to extend their lending on the previous scale, and they are far more selective about whom they lend to – mainly restricting themselves to those who can come up with a large deposit and demonstrate long term solvency, in other words, the better-off. This has reduced dramatically the economic demand for houses, and is what is causing prices (and land values) to fall.

Furthermore, the growing uncertainty in the economy in general is having an impact on house prices. As noted above, a significant factor in pushing up house prices previously was growth of the economy in general, which was enhanced by the easy availability of credit, having the effect of pushing up economic demand throughout the economy, stimulating economic growth. Indeed, it is now being realised that most of the economic growth in Britain between the mid-1990s and 2008 was fuelled by the huge expansion of credit issued by banks to people using escalating property prices as collateral, which, as noted already, caused property prices to rise all the more, allowing banks to advance even more credit.

The trouble is that there are always limits to economic growth based more or less wholly on debt, simply because the collateral eventually becomes exhausted, and because more and more people become involved in paying off their debts plus interest. This, inevitably, is at the expense of growth of economic demand and therefore growth of the economy as a whole, which is the major problem now.

In short, the current fall in house prices (and land values) is due, first, to the reduced availability of funds for home loans, and second, to the economic downturn caused by the fact that debt is no longer growing to the same extent, which is what mainly drove economic growth during the previous period.

A major problem now is that the reduced availability of mortgage funds is deterring house builders and property developers from building more houses because of the uncertainty as to whether they will be able to sell them at a profit once they are built. Meanwhile, since local authorities are no longer prepared to invest in public sector housing – and in any case are restricted from doing so by central government – they cannot provide the stimulus for builders to build more houses, either.

Theoretically, the fall in land values, and therefore the market price of land, should reduce the cost of building new houses, because it would cost less to acquire the land required. The trouble is, as already mentioned, many of the major property developers and house builders already own the land required, so this is not a constraint as far as building houses is concerned. The problem is that, currently, it costs landowners nothing to sit on their land until economic circumstances change, and land values and property prices, start to rise again.

Thus, the housing crisis – the chronic shortage of affordable homes – continues.

The main beneficiaries of house price inflation

The housing crisis has not been a crisis for everyone. On the contrary, it has been a boon for some. Land speculators holding large land banks obviously have benefited by slowly releasing the land at inflated prices.

But the biggest beneficiaries have been banks. As prices went up, people seeking a place to live needed to borrow increasing amounts, which, of course, increased the revenue from interest, and hugely boosted the profits of banks and their shareholders. In effect, because the main element of house price inflation was rising land values, this was equivalent to banks appropriating a significant portion of the higher value of land.

Estate agents have also benefited from house price inflation because the commissions that people have to pay when selling are related to property values.

Now that prices are falling, those benefits will be reduced. Banks, in particular, are losing out – which, it should be said, is a result of their own profligacy. They are having to make provisions for bad debts and cover the costs of repossessions – though, as in the past, they are likely to claw these costs back through higher interest rates and fees charged to their solvent clients.

Finally, people already on the property ladder benefit at the expense of those who are not. Although everybody, including tenants, creates land value, at present, only property owners and landowners (and the beneficiaries of wills) gain from the rising value of land (especially those on the property ladder earlier, which would make their mortgage repayments, or cash outlays, much less). Meanwhile, tenants are penalised with increased rents.

A system of land value tax would end those injustices.

How a land value tax would have helped prevent the current crisis

Had a system of land value tax (LVT) been in place, the house price bubble, as it turned out to be, would never have grown to the extent that it did, and not at all had the availability of credit been better regulated. First, the escalating market value of land, the main component in the huge increase in house prices, would have been kept under control, because the bulk of the increase in land values would have been collected as LVT. Next, it would have eliminated the speculative element that has pushed up prices, since it would have made no economic sense to withhold land from the market in the expectation of higher prices later, first because with LVT in place, such price rises would hardly have occurred, and second because landowners would have been penalised by having to pay LVT.

Furthermore, owners of land, once they had received planning permission, would have had the incentive to develop the land for housing as rapidly as possible. It would have ended the practice of house builders holding large land banks out of use for decades. In other words, it would have boosted the supply of housing, and dampened the tendency for house prices to rise.

Finally, lower land prices would have made it more affordable for local authorities and housing associations to acquire land for social housing, thus increasing the supply of accommodation at affordable rents. In addition, the greater availability of social housing would have meant that private landlords would have been less able to charge exorbitant rents, which, in fact, are quite often subsidised by taxpayers through housing benefit.

An additional effect of LVT, and if also there had been credit controls, is that this would not only have more or less eliminated house price inflation, but also would have allowed the Bank of England to lower interest rates with less risk of inflation. This would have made home loans more affordable (especially as house prices would also have been much lower), and it would have benefited business, and therefore the economy as a whole.

Moreover, as discussed in the main body of this pamphlet, LVT would have benefited the economy in other ways. In particular, it would have prevented the funnelling of money into property that creates no wealth, and have allowed more to go into savings for pensions and for genuine investment in new productive activities, upon which economic development depends, including expanding and improving the stock of housing.

The effect of introducing LVT now

Introducing LVT now would begin to address the current housing crisis head on, and would help prevent the recurrence of such crises. However, much would depend on the outcome of the current economic downturn, and how protracted it turns out to be.
This should not affect the timetable for extending LVT. Indeed, the more the rate of LVT can be increased so enabling other taxes to be reduced, the more this will help overcome the economic downturn, because of the additional economic activity that that would stimulate, as discussed already.

But even if LVT were introduced initially at a relatively low rate, simply as a replacement for the council tax and the national non-domestic rates, as proposed in Section 8, this would provide some incentive to develop or release land for housing, thus increasing its supply – because unlike now, all land would be subject to the tax, including derelict land or land held in land banks. And, in due course, as the rate of LVT was raised, and other tax rates reduced, the incentive would be all the greater.

Next, there is the likely impact on house prices in the current economic circumstances to consider. As discussed previously, as long as there is economic growth, the effect of extending LVT to replace other taxes, which would tend to depress the market value of land and therefore property prices, would be offset by the tendency for prices to rise due to the effect of economic growth on land values.

However, during an economic downturn, this is less likely. Indeed, as explained above, the current economic downturn is already causing house prices to decline, and, other things being equal, extending LVT beyond replacing existing property taxes would likely add to that trend. But over time, the extent to which LVT would encourage economic growth, especially if other policies were adopted to promote economic growth, and if the revenue from LVT and other taxes were invested wisely, this would offset that effect.

None of this would be significant for people who already own houses purely for their own accommodation. If property prices do decline, for whatever reason, they would get less when they sold, but would pay less for the houses that they intended to move to. Their heirs would also get less, but mostly, they, too, would not lose out because most people tend to use their inheritances for acquiring homes of their own – or for trading up into larger accommodation or moving to a better area – which would cost less.

The main problem that would need to be addressed – particularly affecting those who had stepped onto the property ladder more recently, when prices were at or near their peak, and who were lured into taking out large mortgages that they now find hard to service now that interest rates are higher – is the growing number of homeowners getting into arrears and having their homes repossessed. This is likely to become more serious as the current economic downturn takes hold, and people start losing their jobs.

One approach would be for local authorities, through a special fund created by central government, to simply take over the houses in exchange for bonds offered to banks, so that the houses would become part of the public sector housing stock. This would allow people to stay in their homes.

In addition, other measures will need to be introduced if the housing crisis is to be resolved. First, because of the urgent need for more affordable housing for rent – not just for key workers, but for all who need them – local authorities need to be granted the power and the financial resources, such as low interest loans from central government backed up by special housing bonds, to enable them to begin building council houses again. This would be facilitated by LVT, because it would reduce the cost of acquiring land for that purpose.

Second, regulations need to be re-introduced to control the release of credit into the economy, as existed in the 1950s and 1960s. This would help prevent credit bubbles from occurring, and the unpleasant consequences when such bubbles burst. (Even better would be if banks were limited to the credit released only by the Bank of England, which would allow the public to benefit from the seigniorage arising from the money created in the process, instead of private banks, as now – but that is another story.)

To sum up, LVT, together with the re-introduction of credit controls, would make booms and slumps in the housing market – and the adverse impact they have on the economy as a whole – a thing of the past. And it would end the inequalities arising from unearned wealth accumulation derived from landownership.

The Labour Land Campaign

The Labour Land Campaign advocates a more equitable distribution of land values that are created by the whole community. We are a voluntary group working for land reform within the Labour movement. Our members are members of the British Labour Party, Trade Unions or Co-operatives, or are individuals who support our aim to share land wealth through a system of land value tax.

If you would like to join our Campaign or simply would like to find out more, please visit our website at www.labourland.org, or contact our secretary, Carol Wilcox (address below). If you would like to attend one of our meetings, or arrange for a speaker from the Labour Campaign to lead a discussion or seminar with your organisation, please email carol.wilcox@labourland.org.

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Jerry Jones

Labour Land Campaign

2008

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