CHAPTER 1

BASIC PRINCIPLES

> The economic case for a land value tax is simple and almost undeniable. Why then do we not have one already? Why hasn't it been adopted widely in the western world? Even more puzzling is that, right now, as western economies struggle with the global financial crisis, why isn't this form of taxation being seriously considered as an alternative?
>
> **Sir James Mirrlees** (1936–2018): Nobel economics laureate and chairman of the Mirrlees Review, *Tax by Design,* published in 2011

I suggest there are four basic principles or characteristics of LVT that may be expressed under the headings:

1. Community created value.
2. Taxation according to means.
3. A direct tax.
4. Simplicity and clarity.

1.1 Community Created Value

This is the principle of returning to the community, by means of a tax or levy, the value that the community itself has created. This value is measured through land values, which are simply an indication of collective prosperity. With the growth of a community, the value of any site will increase due to the surrounding communal activity or community-funded infrastructure that has the effect of enhancing the value of the site. This increased value falls fortuitously to the benefit of the owner and may be realised in the form of increased rents or capital value at any point of sale. The revenue thus derived is not due to any work done by the owner and is clearly unearned. It is known by economists as the 'economic rent of land' (generally abbreviated to the 'economic rent').

The classical economists, from Adam Smith onwards, were aware of this source of revenue, however it was David Ricardo in his *Principles of Political Economy and Taxation*, of 1817, who first identified the economic rent (see Chapter 13, Definitions). The economic rent still exists, it has never gone away, it is still collected and it still goes into private pockets. The prime purpose of LVT is not to stop this collection but to re-channel it into the public coffers, thereby returning to the community the value that it has created.

The difference between the terms 'land value' and 'site value' as used here, is simply a matter of scale. Land value is the term used when applied to a large geographical area, within which there are many sites. It is more often used in the rural situation. Land value is therefore an expression of the aggregate of all the site values within the area under consideration. The term site value is more appropriately used in the urban context, where the areas concerned are smaller. One may have specific high value sites within an area of general low prosperity and low value sites within an area of general high prosperity.

The value of any property has two parts: the value of the building—the bricks and mortar—and the value of the site. Unlike the building value, the site value, in the urban situation, is determined by its location within the community. As most estate agents would concur, where property valuations are concerned, it is more a question of 'where' rather than 'what'—primarily a matter of location. In the urban context, it would not be incorrect to describe LVT as a location value tax, where the value of a particular site is determined by communal demand at that particular location.

It should also be noted that LVT is proposed as a replacement tax, not an additional tax. To the degree that it is introduced, other taxes should be proportionately reduced or eliminated; the overall tax take would remain the same.

1.2 Taxation According to Means

Taxation according to means is an essential characteristic of any fair tax system. Where this happens, the tax is described as 'progressive.' With LVT the tax burden is imposed according to relative prosperity as measured by land values. The word relative is important here for the practicability of LVT depends on land value differentials. The theory is that these differentials distinguish between areas of high and low prosperity, which are then taxed accordingly. If all land had the same uniform value, there would be no basis for a land value tax. In such a situation a land value tax would be little better than a poll tax, where the measure is on the number of acres rather than the number of heads.

There is always an ongoing discussion amongst politicians and their advisors about where and how taxes should be imposed. The possibilities seem limitless: incomes, sales, transactions, capital gains, property, road use and so on. Rarely is there much agreement; the left say, ‘tax the rich’, the right say tax anything except the rich, who they claim are the ‘wealth creators.’ Nevertheless, whatever the type of tax, there are, I suggest, two basic principles that apply to all taxes:

1. That every able-bodied, able-minded adult who benefits from belonging to a society should make a contribution towards its upkeep.
2. Such contribution should be in accordance with the ability to pay.

Most people would agree with these principles as being fair and reasonable. The first is probably beyond dispute—one could reasonably argue that simply being a member of a community is a benefit in itself. It is with the second that disagreement usually arises, basically over the interpretation of the expression ‘ability to pay’. Most would agree with the old Marxist dictum ‘From each according to his abilities, to each according to his needs’, but much disagreement arises with the definitions of ‘abilities’ and ‘needs’. However, no one has expressed it better, and it remains a guiding principle for all systems of fair taxation.

Taxation of any kind has always involved identification and measurement: identifying what might be taxed and ascertaining to what degree the tax might be imposed, taking into account the means of the payer; that is his ability to pay. This latter consideration has given rise to the principle of progressive taxation, where those most able to bear a tax should pay more in proportion to their wealth or apparent prosperity. Land values provide a measurement of such prosperity whereby the occupiers or owners of high-value sites are generally considered more prosperous, and therefore better able to bear a tax, than those on low-value sites. This may be seen as a blunt instrument of measurement, but it is nevertheless generally true.

1.3 A Direct Tax

LVT has the advantage of being a direct tax. One of the arguments against indirect taxes is that they are indiscriminate—they are paid equally by the rich and poor alike and are therefore unfair. However, they are popular with governments, as they allow the people to believe that they are not really being taxed, they are simply paying higher prices. This phenomenon was noted by Adam Smith, who, in discussing taxes on commodities, commented that 'the consumer, who finally pays them, soon comes to confound them with the price of the commodities, and almost forgets that he pays any tax.'[1]

Indirect taxes also seem to be preferred by taxpayers, for the reason that they are impersonal and clearly paid by everyone equally, no doubt appealing to a sense of fairness, regardless of the fact that the poor pay the same as the rich. Also, indirect taxes are convenient for governments as they are more flexible, being easily adjustable to meet unexpected events without constant reference to electoral promises, and so they are undeniably useful, but for the reasons mentioned above it is better if they are kept to a minimum. Direct taxes, I suggest, are more honest, and I believe, in the long run it is better for governments to be honest with the people.

Direct taxes may be divided into two basic groups:

1. Taxes imposed on existing wealth.
2. Taxes imposed on the wealth-creation process.

To encourage wealth creation and general prosperity it is always better to levy taxes on the first group rather than the second. The first are taxes on ownership, the second are taxes on work and trade.

Among the first group are property taxes (Council Tax and Business Rates), Capital Gains Tax and Inheritance Tax. Capital Gains Tax is more accurately a tax on the realisation of increased value at the point of a sale. Inheritance Tax is a tax on the realisation of value at the time of a transfer of wealth, but they are both taxes on existing wealth. None of these taxes are impediments to wealth creation.

Among the second group are Earned Income Tax* and Employee's National Insurance Contributions, which are taxes on work. Also, included are VAT, Corporation Tax and Stamp Duty, which are taxes on

* Unearned income (on interest, for example) should be taxed under existing wealth.

trade. These taxes act as discouragements to wealth creation. LVT would fall into the first group as a tax on unearned wealth, actual or potential, due to the simple ownership of land—one of the essential elements of production. This would include vacant land being held out of use for speculative purposes. Although land is not in itself wealth (see Chapter 13, Definitions) it is one of the two elements that are necessary for (physical) wealth creation, the other being labour. The ownership of either element implies the ownership of the means to wealth creation.

1.4 Simplicity and Clarity

An important characteristic of LVT, which many other taxes do not enjoy, is its openness, clarity and predictability, which makes it a tax that would be difficult to avoid. With LVT, the basis of the tax would be obvious and apparent to all. Site values would be regularly assessed and published for public scrutiny. The tax due on any site could be calculated by anyone. The figures could not be hidden behind 'creative accounting' or aggressive tax avoidance schemes. Furthermore, land cannot be moved offshore to a convenient tax haven. A tax-avoidance industry, which costs the exchequer billions in lost revenue each year, would be impossible with LVT. Income Tax, VAT and Corporation Tax provide a happy hunting ground for sharp practitioners who flourish in the complexity and obscurity that such taxes allow.

Under LVT, private ownership of land could continue although land speculation as such would disappear.

Excessive increases of house prices, which are caused through the increase of the land-value factor, would be brought under control. Sites would continue to be bought and sold, but any prospective purchaser would know in advance the tax obligation for any site and would be able to enter such commitment into his calculations. There would need to be regular and comprehensive valuations, which would be accessible to all as a matter of public information at all times, as are the existing public registers for Council Tax and Business Rates.