CHINA SHIFTS TAXES TO LAND

by Scott Baker, New York, NY

(This commentary originally was posted in Op Ed News.)

Goldman Sachs just revised its growth target for China downward to "just" 7.1%/year for 2015. See here: http://blogs.barrons.com/asiastocks/2014/09/24/goldman-china-likely-to-lower-2015-growth-target-to-7/
However, Goldman uses the classic Western rationale:

> In economics, there are three factors that contribute to economic growth: labor growth, capital growth and technological advance. Labor growth in China is set to slow. The Chinese society is aging rapidly and the younger generation chooses not to pop out more babies even though Beijing has relaxed its one-child policy. Capital accumulation can only go so far as well and "the current pace of debt accumulation is unlikely to be sustainable in the long term." As for technological advance, China has already played much of the "'catch-up' given the shrinking gap with the highest-productivity nations.

But, China just made a major move to change the way it taxes its people, and this will have a major impact on both its growth and its sustainability. Says Canada's The Globe and Mail: "China moving quickly to roll out property taxes nationwide" - http://www.theglobeandmail.com/report-on-business/international-business/china-moving-quickly-to-roll-out-property-taxes-nationwide/article20294761/

> For years, Chinese property owners have enjoyed a free ride to wealth driven by scorching growth in home prices and a lack of property taxes to whittle away the gains. A condo in Beijing has been like a piece of gold: an asset that can sit and gain value, with little cost of ownership.
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> But three years ago, Chinese authorities began taxing a small fraction of the country's real estate, with pilot projects in two major urban areas, Shanghai and Chongqing.
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> Now Chinese authorities say they are moving to rapidly roll out property taxes nationwide, in a bid to reshape the country's financial structure and curb some of the incentives for local governments to trammel the rights of farmers and others left behind by China's extraordinary wealth gains.

My group, Common Ground-NYC, has been advocating a land-heavy property tax for years, in a series of comments on both Western and Chinese media, as have more influential Georgist, or Georgist-sympathetic, economists like Michael Hudson and Former Assessor of Greenwich, CT, Ted Gwartney, who have both had high level meetings with officials in China and other Chinese groups going back to the 1990s. Hudson has written in July, 2013: "China -- Avoid the West's Debt Overhead: A Land Tax is needed to hold down Housing Prices."

> How can China avoid the "Western financial disease" -- a real estate bubble followed by defaults and foreclosures? The U.S. and European economies originally sought to avoid this fate by taxing the location's site value. A rent tax was the focus of Progressive Era reforms.
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> Enacting a rent tax remains China's main challenge to accompany its privatization of real estate and natural resources. If land rent were fully taxed, it would not be paid to banks as interest for rising mortgage loans -- and governments would not have to tax income and sales. Holding down housing debt will reduce labor's cost of living, but not its living standards.
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> While Western economies shrink in response to debt deflation and fiscal austerity, China continues its unprecedented 30-year growth. Many Western forecasters warn that it must suffer a Western-style financial crash, as if this is a universal path. But China has been industrializing and raising living standards by public credit and infrastructure investment similar to the mixed private/public balance that raised America, Germany and France to world powers as their Industrial Revolutions gained momentum in the late 19th century. Its keys are active public investment in infrastructure, subsidized education and urbanization, rising wage levels and progressive taxation.

Gwartney's justification for China to tax primarily land can be seen in much greater detail here: se.xmu.edu.cn/jzyc/UploadFiles/20143718303170554751157 76.pdf. A small portion of this report is shown below:

> China is looking for new methods of raising revenue to support its government and services for its people. This paper will introduce the concept of collecting land rent which will provide the needed public revenue for China's economy. It will show how to implement the concept of collecting land rent and methods for valuing land rent. An example of a proposal to fund all of California state and local governments from land rent is presented.
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> Real estate consists of land and buildings. The nature and characteristics of land and buildings are totally different and the revenue raised from each has totally divergent effects on people, communities, commerce, growth and economic well-being. Buildings are created by man's labor and incur a cost to produce. They deteriorate over time, lose value and need to be replaced. They should be built in suitable locations in order to preserve farm land and natural resources. Land is defined as everything that is freely supplied by nature, which includes all natural resources, such as air, soil, minerals, airwaves, forests and water. Everything not made by man, is categorized as land. Land has no cost to produce and is nature's gift to mankind. Land's uniqueness stems from its distinctive location, fixed supply and immobility. Land is (cont'd on p. 13)

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required in the production of all goods and services. Land is our most basic resource and the source of all wealth.

Land rent is the value created from ecological and social endowments, not the personal activities of individuals. Land rent is an amount that should be paid annually for the exclusive right to use a land site location or other natural resource. Land rent varies by location and available amenities. It changes by people's competitive desire to use the same land site. Since land is fixed in supply and cannot be expanded, demand is the sole determinant of land rent. As land demand increases, the rent will increase proportionally. Buildings are not a part of land rent. Land rent is the only source of public revenue that could be taken for public purposes without having any negative effect on the productive potential of the economy. When a community collects land rent for public purposes, both efficiency and equity are realized. ....

China has raised revenue from taxes and land use development fees. It has invested in infrastructure, schools, police, fire protection, utilities, and recreation and public services. This investment has increased the rental value of land. China owns its land and each land user should pay land rent to enable China to provide high quality public services to everyone. Land rent exists whether the community collects it or allows people to retain the values that were produced by the community. Collecting land rent will enable China to attain a sustainable and growing revenue base for funding the local and provincial governments. As the demand for land increases the land rent increases.

The burden of paying land rent reduces land speculation, premature land use and the detrimental use of farm land and the rural environment. The requirement to pay land rent fosters the most efficient, highest and best use of land. The rental value of land should be sufficient to finance all public services and to obviate the need for raising revenue from taxes. Public revenue should not be supplied by taxes on people and enterprise unless all of the available revenue has first been collected from the natural resources and the community-generated land rent. Only if land rent were insufficient would it be necessary to collect any taxes.

The fact that this pilot tax is being rolled out in the most seriously land-inflated areas like Shanghai and Chongqing means they are finally serious about curbing unproductive and socially destructive land speculation. Not only will this raise needed revenues for the government, it will allow them to untax actually productive activities, like wages, sales and fixed capital (including buildings if China continues to emphasize a higher tax in dense urban areas). The Land Value Tax - described by Milton Friedman as "the least bad" tax, and Henry George as the "Single Tax" to replace all others, could have the power to permanently and sustainably keep growth in the 3%-5% range all by itself. Coupled with China's demonstrated control over its currency production - producing more Yuan in downturns, when Western models allow private banks to pull back and starve the economy of credit-money - might add another 2%-4%. Smart industrial policy and highly competent Central Authority (the reverse of America) will do the rest. China will succeed on its own terms, not the West's. Those who look for Westernization of China will be as disappointed as those who sell China short (the same group, actually). China's construction of "Ghost cities" is well known. But if the Land Value Tax was applied to these cities as well, the holders (read: speculators) of these lands would be forced to sell to a lower bidder, and China's huge migrant population would finally be able to afford to live in them.

China has learned from the West, but not just from the positive things like rewarding innovative technological growth, but from the negative experiences too. If they continue to be smart, they will avoid our boom/bust cycles, which, together with an austerity model governed by the banks instead of by Governments, threaten to permanently destabilize and retard the economies of Europe - which is entering its third recession in 6 years - and America, which has had a trillion dollar/year Output Gap since 2008, according to the Congressional Budget Office.

America too, has choices. It can tax the Land, not the People, as China has slowly started doing, and as it has done in some small cities in Pennsylvania, most recently Altoona. It can also produce Government issued debt-free money to fill the Output Gap with public works projects, including the sort of infrastructure buildup China is doing - almost inconceivable under the Hodge-podge Western Growth model - using the Constitution's Coinage Clause (Article 1, Section 8, Clause 5), first practiced by President Lincoln in 1862 -1863.

It can do both of these things and more, but not if it remains institutionally bound and theoeconomically moribund, to the banks' austerity models.

It kind of makes you wonder: Which is the Land of the Free?

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SAVE THE DATE for the IULVT and CGO joint conference at Detroit-Southfield August 4-9, 2015.