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The Case Against Land Rent Taxation

Robert Heilbroner

Probably the most widely read history of economic thought, is Robert Heilbroner's *The Worldly Philosophers*, first published in 1953. It has done as much as any other book to form the opinion of Henry George held by economists, social scientists, and the educated public today.

Unfortunately, Heilbroner shows advanced symptoms of that affliction of textbook writers diagnosed by H. G. Brown, the "single tax complex." George is depicted as a good-hearted but simple-minded amateur, driven by childish enthusiasm and self-assurance, who gravely underestimated the difficulty of the world's economic problems. Heilbroner does not waste space explaining George's actual theory. He devotes seven pages to colorful (and partly fanciful) biography; about a page to George's economics. "We need not spell out the whole emotionally charged argument," he says. (Heilbroner, 1986: 188)

What explanation he does provide distorts George's views unrecognizably. Heilbroner fails both to convey the basic principles of George's economics, and to suggest the richness of George's philosophy as a whole. Moreover, even in the "completely revised" sixth edition of 1986, there is no hint of the fact that later writers have formalized and vastly extended the Georgist approach.

"The argument was not too clearly delineated," Heilbroner writes. (188) "George's mechanical diagnosis is superficial and faulty." (189) Actually, George's argument was painstakingly delineated over the course of several hundred pages, and while it may be faulty, superficial it surely is not.

More damaging, however, is the fact that Heilbroner ascribes to him a patently absurd position—the "equation of rent with sin." (189) Henry George, we are told, wanted to "abolish" rent! In fact, of course, George believed that rent is a social surplus which would steadily grow as progress goes on; what he wanted was to have rent collected publicly rather than privately.

Heilbroner pauses somewhat longer to give a few of the standard arguments against the single tax. He refers, for example, to George's treatment of land speculation, but only to reject his explanation of the business cycle as a far-fetched exaggeration. "Land speculations can be troublesome," he declares, "but severe depressions have taken place in countries where land values were anything but inflated." (189) No evidence or reference is offered. (The innocent reader presumes that economists have by now achieved consensus as to the true cause of depressions.)

"The single tax," chuckles Heilbroner, "in abolishing rent ... would be—there is no other word—the ultimate panacea." (188-189) The reader is led to infer that no trained economist today is seriously interested in George. Just as Brown complained seventy years ago—and Geiger, fifty-three, and Bruchey, twenty-four—students have been forewarned that George was a crackpot, and that it is not worthwhile to look further in his direction.

It is no surprise that Heilbroner misses the irony of his next words:

> But something else was going on in the underworld, something more important than Henry George's fulminations against rent .... A new and vigorous spirit was sweeping England and the Continent and even the United States .... The age of imperialism had begun, and the mapmakers were busy changing the colors that denoted ownership of the darker continents. (191-192)

Joseph Schumpeter

In his *History of Economic Analysis*, Schumpeter makes clear that he has no use for the single tax "panacea." (Schumpeter, 1954: 865) He indicates that he has "compunctions about the analytic value of the proposition: God gave the earth in common to all men." (458) He disparages one writer (Oppenheimer) for "his Henry-George attitude toward private property in land." (854) Despite this, Schumpeter shows relatively few symptoms of the single tax complex. He allows that George's program benefits from good analysis, insofar as it causes minimum disruption of economic efficiency. He recognizes George as "a very orthodox economist" except with regard to the "Single Tax." (865) His specific criticisms are rather well-aimed, and worth recalling.

Schumpeter imputes to George the thesis that the existence of private property in land "reduces, of necessity, total real wages" (458), and is the reason why land is a scarce factor at all (854 note). In this, he has identified what may be the key argument of *Progress and Poverty* - an argument which, indeed, may not be quite strong enough to support the weight it carries.

The suggestion implicit in Schumpeter's remark is that to transfer land rent from private to public hands would not, of itself, affect wages. Against this it may by noted that, by financing an ever-growing public sector, the single tax would, if not raise wages, at least raise real *incomes*, insofar as workers (like other citizens) are enabled to consume progressively more government-financed goods and services. Surely, too, to collect land rent in lieu of taxes on labor and products will obviously and directly raise after-tax real wages, in the short run at least. But George does not rely on this argument. In fact, he says in another place that under the existing land tenure system, a decrease in taxes made possible by greater economy in government will, in the long run, benefit landowners, not laborers. (301)

George's primary defense of the assertion that his tax plan will raise wages is the claim that LVT will curb land speculation, thereby raising the margin of production, which determines the equilibrium level of wages:

> Labor and capital would thus not merely gain what is now taken from them in taxation, but would gain by the positive decline in rent caused by the decrease in speculative land values. (George, 1879: 442)

Whatever be the truth to this, there is some internal difficulty in George's view. On the one hand, he vehemently rejects Malthusianism, arguing that land is so plentiful that the Earth could comfortably support a population many times larger than that which prevailed in 1879. This seems to imply that the present population could comfortably occupy just a small fraction of the space available. Yet on the other hand, George argues that land speculators, by withholding some land from use, collectively wield tremendous power to exploit labor and capital. The evident contradiction is perhaps not entirely eliminated by supposing that speculation not only reduces the amount of land in use, but also diminishes the efficiency with which that land is used.

Schumpeter finds a second flaw in the logic of *Progress and Poverty*. This is the "untenable theory that the phenomenon of poverty is entirely due to the absorption of all surpluses by the rent of land." There may be a suggestion here of the familiar argument that land rent is merely one surplus among many, which I discuss below. Schumpeter may also be referring specifically to George's argument that all the gains from population growth and technological advance ultimately go to the increase of rent. Although other classical economists are equally to blame for holding an all-devouring rent thesis, this does not excuse George; in particular, he might have seen that technological change may be land-saving instead of labor-saving, particularly as land becomes scarcer relative to labor. He might also have seen that as technical progress goes on, access to education becomes an increasingly important factor in income distribution.

It is one thing to argue that the elaborate classical system which George constructed to support his central thesis contains errors. It is quite another thing to show that the central thesis is unsupportable. About this, Schumpeter has little to say. Despite his reservations, he concludes with the enigmatic but not unsympathetic comment that George's proposal is "not *economically* unsound, except in that it involves an unwarranted optimism concerning the yield of such a tax." (865, italics added)

Is the reader to infer that the principle of rent taxation is economically sound, except that it is inadequate as a single tax? Is the tax perhaps *ethically* or *politically* unsound? Whatever be the intent of Schumpeter's negatively phrased affirmation, his pessimism concerning yield, which he shares with Heilbroner, is unfair and probably unwarranted: unfair, because government budgets were far smaller a century ago—George's contemporary critics feared that the yield of the single tax would be excessive, giving undue power to government. Unwarranted, because there are good reasons to suppose that the yield of a single tax on the full rent of land would be far larger than his critics today suppose, as I shall indicate below.

Arguments Against Rent Taxation

Opponents of the Georgist program have offered numerous additional counterarguments. Many of those which recur frequently are either unsound or irrelevant. A few have value and warrant careful attention, though none vitiates the fundamental Georgist insight.

It is argued, for example:

- that a switch to heavy LVT is unfair to vested interests;
- that the tax would not reach most of those who have, in the past, benefited from private property in land;
- that land rent is merely one among many surpluses;
- that rent is not a surplus at all, but a reward for putting land to its best use;
- that land values sometimes fall;
- that land taxation will not raise real wages;
- that many low- and middle-income households own land;
- that LVT will throw the urban poor out of their homes;
- that LVT will bankrupt small farmers;
- that LVT puts government in the business of land management;
- that the value of land cannot be distinguished from that of capital improvements;
- that "land" denotes no meaningful, distinct economic entity;
- that the supply of land is not perfectly inelastic as the theory allegedly requires, since more land can be produced—or, since land can be turned from one use to another;
- that land value taxation distorts intertemporal resource allocation by hastening development;
- that land speculation is efficient, and should be encouraged;
- that the tax will worsen speculation, or have no effect upon it;
- that the tax will cause severe cash flow problems for owners of appreciating land;
- that land speculation is not a cause, or the primary cause, of business cycles;
- that LVT induces land abandonment;
- that LVT will cause overbuilding, further congesting urban areas and destroying open land;
- that rent taxation discourages conservation, and induces ecologically

unsound exploitation of resources;

• that the single tax gives inordinate power to government, and leads inevitably to institutionalized corruption; or,

• that land rent constitutes an insignificant share of national income, so the tax would raise little revenue and would have a barely noticeable effect on economic behavior.

Textbooks continue to repeat old errors. Most textbook discussions of George confine their analytical comments to a cursory exposition of the inelastic-supply argument for land tax neutrality. Sometimes, the conventional theorem that a tax on rent cannot be shifted is denied, on the ground that a rise in rent will bring a large supply of land to market, or even stimulate production of more land.

There is also usually a mention of distributive impact; the program is generally felt to be unfair. Income and other taxes are promoted, as capturing alternative sources of surplus. These are generally pushed on grounds of equity and revenue adequacy. Income taxes share few of the efficiency properties claimed for rent taxation. On the other hand, none of these writers has fully come to terms with the Georgist view of economic justice—this despite evidence that, because of wholesale tax (and subsidy) shifting, our ambitious and costly redistributive programs have had little sustained effect upon the distribution of disposable income. (Holcombe, 1987: 286-288)

It is not my intent to confront most of these objections. I discuss two of the more prevalent ones below, before going on to discuss further developments in Georgist economics. My aim is to show that the case for using rent as a source of government revenue is far wider and richer than is commonly realized. The various superneutrality arguments are virtually unknown. Also, economists have neither understood nor challenged the Georgist view of the abundant revenue potential of rent taxation.

Problems of Transition to a Georgist World

There is one objection which occurs even to those who are sympathetic to George's vision of economic justice and who understand the efficiency arguments. This is the objection that, even if a Georgist world is in principle to be preferred to our own, for an established economy/polity to undertake a transition to heavy or exclusive reliance on rent taxation would cause unconscionable harm. It would unfairly penalize the wrong individuals, violate vested interests, and shake public faith in government. The essence of this complaint is that it is not fair to change the rules in the middle of the game. Georgist tax reform would result in windfall losses to some individuals (and gains to others).

Since LVT cannot be shifted, the entire burden of the program falls on the backs of those individuals who happen to own land at the time the tax is announced. The tax neutrality/nonshiftability argument, usually seen as the first pillar of LVT theory, thus becomes a potent political and ethical argument against it. Voters accept income taxes, sales taxes and the rest precisely *because* they are shifted around, their burdens diffused widely and in imperceptible ways.

Georgists have several responses, none of which convinces everyone.

They hold that rule changes consequent upon public resolve to correct a newly recognized injustice tend to promote, rather than erode, public faith in government. Moreover, land is different. Georgists point out that in common law, real estate ("regal estate") is the property of the State, and that private rights to land are conditional on the use being consistent with the public interest. We accept zoning as well as some degree of land value taxation, for example, as well as the principle of eminent domain, which, where it is applied, can be far more disruptive of vested interests that would be a well-orchestrated transition to a regime based on resource rent taxation.

Anyhow, legislatures and courts make rule changes every day. Some cause significant redistribution of welfare, as when tax codes are overhauled. Taken too literally, the vested rights protest becomes an absurd defense of the *status quo*. Defenders respond, of course, that to "make land common property" by taxing rent is an exceedingly drastic step. (One wonders what advice these conservative writers might have offered to the countries of the former Soviet Union and Eastern Europe.) George observed that slavery was rightly abolished with no compensation paid to slave owners. Defenders of vested interests recall the Civil War.

Some land taxers have regretted George's blunt words, emphasizing that their purpose, however radical, is achieved by a simple, gradual, unobtrusive adjustment of the rates of familiar taxes.

Perhaps the argument most convincing to economists is that, if Georgists are right, the proposed regime change constitutes a potential Pareto-superior move. Depending on transaction costs, it may be possible to arrange a compensation system during the transitional period, paying net losers out of the winnings of the net gainers. This may not be as difficult as it sounds. A gradual, rather than abrupt, shift to heavier land taxation provides a significant degree of compensation automatically, since the present value of future taxes, capitalized into lower current land prices, is smaller, the longer the reform is postponed. It also allows investors to adjust their plans to a new set of rules. Moreover, since an increase in the LVT rate would be accompanied by a decrease in other taxes, there would be very few individuals (in the United States at least) who, on balance, stood to suffer a net loss of appreciable magnitude. Those other taxes had been shifted at least partly to land. Even individuals who lose in the short run are likely to find themselves better off in the long run than they would have been without the reform.

A related argument against the Georgist plan is that a rent tax would fall only on current landowners, many of whom are recent buyers; it wholly exempts past landowners—who have already realized their unearned gains. The injustice to which George objects, if it is an injustice at all, is a regrettable but immutable fact of history. As Heilbroner observed:

> A vast body of rents goes to small landholders, farmers, homeowners, modest citizens. ... Rents are not frozen in archaic feudal patterns, but constantly pass from hand to hand as land is bought and sold, appraised and reappraised. (Heilbroner, 1986: 190)

George's reply to this line of argument was that the purpose of his reform, like any other, was intended to correct, not past, but present and future injustice. (The complaint carries more force in the United States than in some other places, such as where the legacy of European colonialism includes the *latifundia* [great estates] of a powerful aristocracy—much like those which, George reminds us, weakened the Roman Empire.)

The real issue is whether the efficiency and equity benefits of the proposed reform would be sufficiently large to justify the necessary expenditure of political will and disruption of expectations. The first constructive task, as Brown observed, is to predict the likely effects of the Georgist plan once it is in place. If they are desirable, the reasonable next step is to search for the most satisfactory way to achieve the transition.

One obvious place to begin is with the vast resources not yet subject to private property. Raise logging and grazing fees on federal lands to market levels—or higher, to reflect the environmental costs of these activities. Charge polluters for permission to foul the air, water, and soil; negotiate international agreements to allow fair, efficient, and sustainable use of the global commons. At the level of local politics, one place to start is by gradual reform of the real estate tax, just as cities in Pennsylvania and New York have done.

All these are already on the agenda in the United States. Ironically, public opinion seems in some respects to be bending unwittingly in George's direction.

One Surplus Among Many

A second persistent argument against the Georgist proposal is that, while land rent is surplus, there are many other important sources of surplus (or unearned income) as well. This view, only suggested by Schumpeter, is central to Heilbroner's critique:

> ... (L)andlords are not the only passive beneficiaries of the growth of society. The stockholder in an expanding company, the workman whose productivity is enhanced by technical progress, the consumer whose real income rises as the nation prospers, all these are also beneficiaries of communal advancement. The unearned gains that accrue to a well-situated landlord are enjoyed in different forms by all of us. (Heilbroner, 1986: 189)

"Neo-Georgist" Kenneth Boulding agreed that rent taxation is equitable as well as efficient, and that the tax system is the ideal instrument with which to socialize rent. However, he emphasized that land rent is only one of several varieties of taxable surplus; the "single tax" alone is insufficient to capture it all. (Boulding,1982: 8) Boulding suggested that graduated income taxes are appropriate to achieve the redistribution George desired.

Perhaps the movement that undermined George's influence more than any other was the rise of the progressive income tax, most of which took place after the publication of *Progress and Poverty*. In the opinion of most economists and men of affairs, this represented a method of redistribution, even the capture of economic surplus, which was more general than any land tax. (17)

Even if they reach some surplus, however, income taxes tap both earned and unearned income indiscriminately; they share few of the efficiency properties claimed for land value taxation. Moreover, since they are easily shifted, there is no assurance that income taxes affect the distribution of welfare as anticipated. George wrote that the goal of the progressive income tax—a more equal distribution—is worthy, but that its enforcement encourages bribery and evasion, and involves needless restriction of freedom. Worse, "Just in proportion as the tax accomplishes its effect, there is a lessening in the incentive to accumulate wealth, which is one of the strong forces of industrial progress." (George, 1879: 320)

In any case, Heilbroner's suggested alternative surpluses are suspect. In the first place, the gains received by a "stockholder in an expanding company" are interest and profit, not "surplus"; without such gains, corporations could not attract scarce capital, especially for risky ventures. Whereas a new buyer in the land market merely raises the price of the fixed stock of land, a new buyer in the stock market increases the aggregate of corporate capital.

LVT is not intended to capture entrepreneurial profit, which is a reward for risk and ingenuity. One who acquires land by purchase in a well-informed market and possesses no monopoly power enjoys no "unearned income" in the accepted sense unless there are land gains not foreseen and capitalized in the purchase price. If a certain landowning entrepreneur is able to extract a net income which exceeds the opportunity cost of the land, as measured by the market rent, then that excess is profit; it is not, and should not be, captured by a rent tax.

Ordinary monopoly profits, George knew, are indeed another source of unearned advantage. His preferred solution was either to abolish the entry barrier which produces the monopoly, or, in the case of natural monopoly, to have the activity regulated by government. Either way, there will be nothing left to tax.

In the second place, rent is a surplus only in the sense that land would exist regardless of who received its rent. More to the point, rent is the social opportunity cost of land occupancy. Rent rations scarce land services, which are rival benefits: one person's enjoyment of these general gains interferes with another's. By contrast, the rising real wages and incomes enjoyed by workers and consumers "as the nation prospers" are clearly nonrival benefits; one person's enjoyment deprives no other. These widely shared "surpluses" are a cause, not for alarm, but for celebration.

Heilbroner tells us that George wanted to "abolish rent" because rent has made some people rich. He was "outraged" at the sometimes "fabulous" incomes of fortunate landlords. (Heilbroner, 1986: 188) However, George was not at all opposed to wealth. On the contrary, he wished we could all be rich; he praised the technical and social advances which promise to make the wish come true. His book inquires, not why some men are rich, but why, despite a century of undreamed-of material progress, so many are poor.