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INTEREST AND AFFORDABLE HOUSING

The interest rates assumed are for borrowers, not for savings deposits, so the scenario is not so unrealistic in these peculiar times of low interest rates and high asset values.

The relative values assumed are slightly biased towards construction value, rather than towards location value, because the aim is to understate the effects of changes, and not to be accused of exaggerating the case for government collecting location values. The inverse of interest, being number of years purchased, is perhaps over simplified, but gives a fairly reliable insight into what actually occurs.

An imaginary 4 bedroom detached house in the South East has a market value of £850,000 of which £300,000 is the cost of Building and £550,000 is the capitalised location value. Given a low-ish interest rate of 1%; the rental for the building would be £3,000 and the annual location value would be £5,500 which would remain fairly constant given that the surrounding environment (both natural, and amenities such as schools, hospitals, GPs, shops, entertainment venues etc.) would remain similar with changes to the interest rate.

Now imagine the interest rate to double to 2%. Then the rental for the building would be £6,000, but the capitalised location value would fall to £275,000. This would mean a new market value lower at £575,000, and the total annual rental for both the building and location value would be higher by £3,000 at £11,500. This increase in interest rate dramatically shows an incentive to buy outright rather than going for a rented property.

The collection of some annual location value by local or central government would be similar in both interest rate scenarios but, easier to introduce when interest rates are higher, because the exclusion of annual improvement value in the new assessment, would not necessitate a higher collection.

Now let us look at another imaginary terraced house with a market value of £300,000 of which £200,000 is the cost of building and £100,000 is the capitalised location value. At 1% the rental for the building would be £2,000 and the annual location value would be £1,000. At 2%; the rental for the building would be £4,000, but the capitalised location value would fall to £50,000. This would mean a new market value lower at £250,000, and the total annual rental for both the building and location value would be higher by £2,000 at £5,000 which would be even more devastating than that for the detached house. It is clear that an annual tax on improved assets is very harsh on the poorer members of society.

Although this may not indicate the real complexity; it does indicate the harshness on the poorer sections of society, unable to purchase, and compelled to rent. All due to an ignorance of the (annual) existence of location value on a time basis.

Capitalised Land Value capture, whether shared by governments with a developer or not, would not affect future annual location values – which illustrates the folly of collection of what is, in effect, not a location value capture at all, but, once again, a development tax on improvements.