

Why all taxes do not come out of rent

Harry Pollard

(reprinted from an email exchange, 18 January 2018)

I'll give you a brief history of how I arrived at my thinking. It began a long time ago – perhaps in the 60s and maybe at the HGS Atlanta conference. I gave a presentation in which I said that all taxes came out of rent. Consternation! I was accused of saying we didn't need a land value tax. I had fingers waved in my face as I struggled to say I didn't mean that at all.

Among the noise I heard that some guy called Gaffney had come to a similar conclusion that ATCOOR (All Taxes Come Out Of Rent).

As it happened, both Gaffney and myself were wrong but I wasn't to discover this until a long time later when I realized the difference between Economic Rent and rack-rent.

First we should be clear about urban Economic Rent. It is the community created free market value that attaches to an location. It must be measured in a free market or our entire argument is invalid. This Economic Rent indicates the advantage given to someone who uses the land location. The whole point of Georgist theory is that exactly this advantage should be collected by the community that created it. In other words, if the Economic Rent of a location is \$1000 a week, the community will collect \$1000 a week – no more. Nothing will be taken from the user of the location. His wages will remain intact.

Unfortunately, we don't have a free market in land. An optimum free market exists when there is no restriction on production and no restriction on movement to market. Neither applies to urban land locations. In a city, the number of locations is limited. While locations can change shape or can be divided, in practice, one has a limited number of attractive locations. And, of course, we can't move some cheap desert land into the city to compete.

Nothing can be done without land so demand for locations is continuous. In a marketplace when heavy demand meets limited supply, prices rise. So location rents rise above Economic Rent.

The only source for these higher rent payments is wages and as land costs rise higher, wages sink towards subsistence.

This a long way from the free market that provides us with Economic Rent, so what do we have instead? I use an old name which is appropriate – rack-rent, which may be defined as the highest amount that can be extracted from a tenant while maintaining production. (Henry George was less mealy-mouthed. He suggested any higher extraction would lead to death.)

(I'll leave out a discussion of landholder psychology which makes the situation even worse.)

So the important parts of the rack-rent economy are wages which for many are barely enough to live on, and rack-rent. Any taxes which are imposed cannot come from Labor – they must be extracted from rack-rent. So, way back in the '60s, Mase and I were almost correct. All taxes come from rack-rent.

As does the income from other privileges. The only source of privilege income is rack-rent. (This should be noted as it means more trouble for a Georgist economy.)

So let us impose a modest land value tax on rack-rent. Considering the source of rack-rent we would be taxing labor at secondhand. Rack-rent takes it from Labour and we take it from rack-rent. But, we could use the revenue to help people at the bottom of the economic heap. I'm sure you are ahead of me. Rack-rent will simply increase to press labor back to subsistence.

So let's increase the amount of LVT – more and more. In due course, the amount collected will make payment difficult for landholders who keep their land vacant or underused (slums). So, they will begin to unload.

When land locations that have perhaps been underused for decades tumble onto the market, rack-rents and rack-prices will collapse. We'll be back to land values that will be Economic Rent. The enormous land values that depended on a monopoly market will have disappeared. The \$23 trillion, Scott, is a measurement of the rack-rent and its corollary – land prices – that have been extracted from Labor for years. They won't exist in a Georgist economy.

Harry