



Palgrave Entry on Land Tax

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Article citation:

Gaffney, Mason. "Palgrave Entry on Land Tax." No date. The Palgrave Dictionary of Economics.

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LAND TAX

by Mason Gaffney

Taxation is the form of socialization used in market economies. Choosing what to tax is choosing what to socialize. Rather than socialize labor or repel capital it is possible to tax land.

Land holds a unique place in the distributional ethic because it is (by definition) of natural origin. Man did not create Earth with its resources but rather fights over it. Land is also (with exceptions) more nearly permanent than man or his works. Thus, rent as private income neither elicits the supply nor preserves it. Its main function is to allocate the fixed supply among uses, but it is arguable that land taxes, when based on land's capacity-to-serve, are at worst neutral to this function and at best improve on it.

The philosophical rationale for land taxes is strongest under an organic theory of the polity. It is no accident that Henry George (prominent protagonist of land taxes) crystallized his ideas after reading Andrew Bisset's Strength of Nations on feudal levies. Landholders have a privilege from the State and in return are liable for taxes in perpetuity.

The entire value of land, now and forever, is here regarded as a benefit received from government. This is consistent with A. Marshall's concept, "the public value of land", where value is the product of three things: nature; government; and spillover values from development of adjoining and linked lands. All these values being unearned by the individual landholder they are fit to be taxed.

The organic view distinguishes the land from its holder. Land taxes may be paid by income the land earns, not by the holder as a person unless we identify him with the land and regard him as having a prior right to own land free of liabilities to the public from which he holds title. The contractual theory, by contrast, treats government as a kind of business extending services to specific lands whose holders need pay only for recent benefits received, construed narrowly.

The rationale for land taxes presumes a functional attitude toward distribution, regarding property not as an end in itself

but a means to get things done. A land tax based on market value, not varying with actual use, is a fixed cost that sharpens marginal incentives. Critics today seldom argue otherwise, but oppose land taxes precisely because they do force landholders to respond to the market, which may have its own faults in a world of "second-best".

Land taxes are in rem and so disregard the holder's personal circumstances, a drawback in some opinions. On the other hand landholdings are much more concentrated than the receipt of income or taxable consumption or payrolls, and land taxes are not shifted, making the tax inherently progressive even though but loosely correlated with taxable income. Avoiding land taxes is next to impossible, even though collection enforcement is limited to seizing the land, not the person or any other asset.

The rationale includes a concept of landholder stewardship. A limited number of land titles were issued in order to get land under tenure to assure best use. So far so good, but those not receiving or inheriting land need a counterpoise to assure they receive their share. Land taxes do so in three ways: by supporting government; by pressing landholders to produce goods and services; and pressing them to hire workers to do so. Land taxes act as a kind of social audit and performance standard of stewardship to promote equity towards those excluded.

There is also more equity among landholders, which in turn promotes efficiency. Absent land taxes there is pressure on governments to do as much for A's land as for B's. Efficiency however calls for specialization and differentiation, meaning high values for some land and low values for other, with windfalls and wipeouts. Land taxes automatically compensate the losers from the gains of the winners, thus freeing land planners to maximize the joint benefits.

The rationale of equity for the excluded says that lands with open general access like parks and roadways should be exempted in whole or part. But such exemption can lead to overcrowding, to meet which it is clear that some user charges on such land can be construed as special kinds of land taxes. An obvious example is a charge on large trucks in downtown streets. Lacking any such constraint the crowding might in turn lead to indefinite expansion of the exempt land use.

The rationale is only partly consonant with personal ability to pay. Landholding confers potential ability to pay, but that is only realized upon one's using the land well. And earned cash is not tapped at all. A land tax is a fixed periodic charge. It is based on qualities inherent in the land with few concessions to the landholder's personal illiquidity, weakness, setbacks or aging. "Use it or sell it" is the message, which many consider too harsh.

What is harsh for the distressed holder, however, is accommodating to frustrated buyers, and it boils down to which group shall be accommodated. Since liquidity is known not to increase in step with total wealth, imposing taxes on landed but illiquid holders has a strong progressive effect. The regular flow of land taxes also accommodates governments, especially small local ones needing steady revenues that are not turned on and off at the convenience of others.

It is not always a question of selling complete units. Land around homes and enterprises is subject to sharply diminishing marginal utility or productivity and a function of land taxes is to constrain horizontal extension of holdings, to the end that the nucleus of each holding may be closer to others to facilitate trade, cooperation, linkages, sharing common costs, and other synergies. The "highest and best use" of land is usually that which most relates to and complements its neighbors and trading partners, who must not be held too far distant.

There is also a diminishing return to time as buildings age, and a function of land taxes, in conjunction with building exemption, is to advance (and/or stop retarding) renewal of sites, neighborhoods, cities, regions and whole economies.

Locke, Quesnay, Adam Smith and others have shown a tendency to shift all taxes to land, whatever the nominal base or event, assuming elastic supplies of labor and capital. This leads some to conclude that all taxes alike just tap land rent. But one cannot tap rent where there is none. Taxes on other bases simply abort the taxed input or activity at the no-rent margins of land use, both extensive and intensive. This excess burden in turn puts an upper limit on the possible tax rate, thus sparing much rent from being taxed at all while destroying other rent completely. The only way to tap much rent is to tax land directly.

Land value and capital are not convertible into one another (excepting exhaustible minerals, not treated here). From this it follows that efficiency does not require equal tax rates on the two, but only uniformity within each class. Uniformity is impossible with capital because of differential concealability. But land is uniformly non-concealable. The case for neutrality of land taxes is stronger under uniformity, but mainly requires that the tax not be a function of use.

A land tax may be based on the current potential rent, or on value. In most countries other than Britain it is the latter. Values are not simply proportional to rents because many land values are elevated above that by expected higher future rents. In such cases taxes rise high relative to cash flow, and at a stiff rate may even be higher. This subjects the holders to a cash drain. The extra tax may be shown, however, in general to tax the unrealized increment, in the manner advocated by Haig-Simons, at the time it accrues. There is some recent falling-away from Haig-Simons, and to one school now this is "double taxation", an issue currently mooted.

The most controversial question in land taxation is the effect on appreciating land. Most hands agree the land tax advances conversion to the higher use. To Henry George this "sovereign remedy" would correct a market failure and unlock speculative holdings with profoundly beneficial effects. To several modern writers following Richard T. Ely the advance of conversion is unneutral and somewhat wasteful. Speculation is seen as inefficiently keeping land from premature commitments. To this writer it seems mathematically obvious that an efficient adaptation to rising future incomes would result in advancing, not retarding conversion. But the issue is now moot.

Land taxation at the local level has a natural cap in local particularism as expressed in "Don't swamp the lifeboat". Land taxation by a central national government might go much heavier, and accordingly statesmen like Austen Chamberlain in Britain and James Madison in America have contrived to divert land taxation to local governments. Colin Clark, on the other hand, has published a plan to nationalize land through taxation without depriving the poorer localities. He would rank the local jurisdictions in order of land value per capita, and apply a central government surtax starting from zero but graduated upwards according to this ratio. The scheme basically has central government apply to local ones the same principle of direct land taxation that local governments can apply to individuals, tapping the rich rents without destroying marginal rents. Clark, like George, may have been reading Bisset's Strength of Nations.
