Defining Consumption

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What Is "Consumption"?

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To consume most goods and services is to eat them up, burn them, wear them out, see them break or rust out or crack or tumble down. But how about land, does anyone think of that? Land as space is not used up. To consume it is to preempt its service flow without impairing its substance. To consume land is to occupy it for a time-slot, which may be as brief as beating a red light or (rarely) as long as the pyramids last[1]. After us life goes on, on the land once left to us, which we then leave to others. "Time-sharing" was not invented by the vacation condo industry but is inherent in the nature of land and life.

How do macroeconomists and national income accountants handle that? They don't. It is a great gaping void in conventional theory and public accounting. To handle it explicitly would destroy the theoretical postulate that consumption, defined as "spending on consumer goods," makes jobs.

One need not actually enjoy or occupy land to consume it. The essence of consuming land is preempting the time-slot from others. Thus, holding land without using it, using it below capacity, is a form of wasteful consumption. If you hired a brain surgeon at his usual hourly rate to weed your garden and dust your sills, economists would recognize it as wasteful consumption; but if you hold onto a $5 million Malibu beachfront to visit twice a year, that's ignored.

Land is reusable. As there is never any new supply, the old has to be and is recycled periodically, and will be in perpetuity, without changing form or location. Melded briefly with fixed buildings, land always survives them to go one more round of use. Even while melded with capital land always is fit for another use, unlike the capital on it. Land value in cities has been defined as "what is left after a good fire," and arsonists have taken that quite literally.

The opportunity cost of capital is fleeting. Capital loses most of it the moment it is committed to a specific form, whose physical alternative use is often only as scrap. Land's "opportunity cost" is real and viable at all times. The scrap value of capital is often zero or negative (radioactive waste supplying an extreme example).

Capital, once formed, soon withers away unless there is capital recovery enough to return the original amount over economic life, and the capital recovery is reinvested. Capital recovery is cash flow less interest on the unrecovered balance, with the latter always a prior charge.

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[1]The other six "Wonders of the Ancient World" have all disappeared without a trace. Relative to land, human works are evanescent. "Like snow upon the desert's dusty face, lighting a little hour or two" they are gone.

Capital is kept in existence from age to age not by preservation or permanence but by constant replacement; while land <u>is</u> the place on which generations of capital come and go.

When we speak of land turnover it refers only to ownership turnover, i.e. the percentage of the fixed supply that changes hands each period. There is no real turnover in the sense of wearing-out and replacement. And even the ownership turnover is very slow compared with capital. Capital turns over constantly, in the normal course of production and consumption.

Something like 3-4% of land parcels turn over annually. Larger, high-valued holdings turn over more slowly, so perhaps one or two percent of the land, measured by value, changes hands yearly. On the other hand, the entire inventory of consumable goods changes hands, normally several times a year, in the natural flow of production. A large share of "durable" capital returns half its value within four or five years. Ownership turnover is inherent in physical turnover.

As noted, to consume land economically is merely to preempt a time-slot from others, <u>regardless of what one does with it</u>. The unreaped harvests of idle land flow down the river and out the gates of time like water wasting through a desert. Lost water may sometimes be useful downstream; lost time never returns. To keep others from using a time-slot is to consume it.

The value of preemption is the highest and best use that might have been made of the land preempted. That is the economic cost. The land is not responsible if the manager fails to realize its value at optimal capacity. Neither are the persons who are excluded. Only the preemptor is responsible, as a manager. This person deserves credit for performing above par and blame for falling below.

A great deal of land in fact is not allocated to its highest and best use. The shortfall of realized ground rent below potential ground rent is properly a debit to the manager's account, not the land's; and the party responsible for the manager is the holder of title.

Most economic theorizing has failed to bring out this point. The tendency is to treat ground rent as a residual, a waste basket for all the errors and dereliction of responsible economic actors. This has resulted in greatly understating the value of land relative to other factors of production. Institutional and social factors, too, often obscure the opportunity cost of land.

Theorizing lags behind practice. In dividing value between land and a building affixed to it the standard practice of appraisers, and speculative buyers too, is the "building-residual method." The land is appraised as though vacant; the building gets the remaining value, if any. The building, once attached to a specific site, loses the mobility of place and form that fluid capital possesses and has no opportunity cost but scrap value, often negative. Land, always lacking mobility of place, retains mobility of reuse because of its versatility, permanence, and irreproduceable location.

What can it mean to "consume" land, when it does not get used up? It can only mean to occupy or preempt a time-slot of space. That has the most profound implications for the meaning of "consumption" in economic thinking, and "consumer taxation" in fiscal policy. Economists have neglected and papered over these matters almost completely. Let us pursue the point.

How shall we measure land-consumption by owners, where no rent is paid? Is it purely subjective? Does it vary with the owner's mood and health? It is simpler than that, and fully practicable. The measure is the market opportunity cost of land, e.g. the price times the interest rate.

Holding an urban site has been likened to holding a reserved seat at a play, ballgame, or concert. The seat-holder properly helps pay for the event, whether or not there to enjoy it. As a result, very few paid customers fail to show up. Likewise, people who pay cash rent for land seldom leave it vacant. Doubtless if people paid regular cash taxes to hold land, they, too, would consume (preempt) less.

Proponents of "consumer taxation" almost universally overlook this point. I am not aware of one who has proposed including land-consumption in the tax base. Aaron and Galper, propounding a "cash-flow tax," explicitly allow for letting each succeeding owner expense land purchase, effectively exempting land rents from taxation 100%. So do Hall and Rabushka in their "Bible" on the flat tax, and so do most current agitators for a national sales tax or VAT.

So-called consumer taxes actually imposed now and in the past bear heavily on the necessities of median and poor families. We deride the salt tax of the French ancien regime, and of pre-Ghandian India. We recognize them as instruments of tyranny and class warfare, even as we tolerate modern legislators who now impose comparable burdens on ourselves, and economists who rationalize such taxes by belittling the necessities of life.

Doing so, they compound the deception in the label "consumer taxation." Much of what is taxed in the name of taxing consumers is actually used for another kind of capital formation. This is what the puritans of early Plymouth called "Inward Wealth," and what modern economists call "human capital." The same economists who say human beings are or contain capital, and we need more of it, turn around and tell us to tax the formation and maintenance of such capital, by calling it "consumption." Coupling this with their proposed exemption of land-consumption we have the ultimate victory and application of semantic cleansing. Inconsistency, thy name is neo-classical economist.

Leading modern philosophers of fostering "human capital," like Gary Becker and Theodore Schultz, think of it as post-graduate education, which happens to be their profession. Logically, though, it should include undergraduate education, and secondary education before that, primary before that, and why stop there? Parenting is part of education. Before that comes conception; before that (usually), marriage; before that, courtship; and so on. There is no logical stopping point, back to Adam and Eve. That leads us to realize that much, perhaps most of what sales-taxers stigmatize and down-value as "consumption" is actually human capital formation.

Bottom line? To tax consumption properly we should tax all land held for housing above some reasonable minimum needed for health and children; all land held for recreation; and all land held without using it at all. And we should NOT tax much of what economists today carelessly call "consumption."