



Taxation: Philosophical Perspectives

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CHAPTER

10 The Politics of Land Value Taxation

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Abstract

This chapter aims to show that land value tax has both theoretical and practical merit. The author traces the classical normative arguments for land tax in Adam Smith, Tom Paine, David Ricardo, Henry George, and Lloyd George, and the current academic literature, and then shows how some of difficulties of inheritance (estate) tax can be resolved by a land tax. It would also improve on the UK's current ragbag of property taxes. In the final sections, issues of practicability, and of winners and losers, are addressed. The examples almost all come from the United Kingdom, but the arguments are intended to be general.

Keywords: Adam Smith, maxims (canons) of taxation, Tom Paine, Henry George, David Ricardo, Lloyd George, Winston Churchill, Ricardian rent

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This chapter aims to show that land value tax has both theoretical and practical merit. I trace the classical normative arguments for land tax in Adam Smith, Tom Paine, David Ricardo, Henry George, and Lloyd George, and the current academic literature. I then show how some of the difficulties of inheritance (estate) tax can be resolved by a land tax. In the final sections I address the issues of practicability, and of winners and losers. The examples almost all come from the United Kingdom, but the arguments are intended to be general.

This chapter is organized as follows. In section 10.1, I present the classical arguments in favour of a progressive, neutral system; and the classical anti-argument (there is only one). In section 10.2, I review the switch from indirect to direct taxation between Adam Smith's time and now, before discussing the special properties of land in section 10.3, followed by a discussion of the political and administrative practicality of land value taxation in section 10.4. The chapter concludes with a brief examination of property, theft, and estate or inheritance tax in section 10.5.

10.1 Classical Justifications of Taxing Land Values

It may seem perverse to open a section on classical justifications with a review published in 2011, but Sir James Mirrlees and his colleagues (Mirrlees et al. 2011) stand on the shoulders of giants. Sir James is no dwarf, having won a Nobel Prize in economics for his work on the theory of optimal taxation. Mirrlees and his colleagues recommend

a progressive, neutral tax system. Each of the three key words of that formula—‘progressive’, ‘neutral’, and ‘system’—is important....A good tax system should be structured to meet overall spending needs....[N]ot all taxes need to address all objectives....A tax system that treats similar economic activities in similar ways for tax purposes will tend to be simpler, avoid unjustifiable discrimination between people and economic activities, and help to minimize economic distortions....Third, achieve progressivity as efficiently as possible.

(Mirrlees et al. 2011: 471–2)

p. 186 The Mirrlees Review was published by the UK’s leading public finance think tank, the Institute of Fiscal Studies (IFS), which had earlier published a similar review chaired by another Nobel Laureate, Sir James Meade (Meade 1978). These reports build on classic insights by Adam Smith, Tom Paine, David Ricardo, and Henry George among economic thinkers; by Winston Churchill and Lloyd George among campaigners; and by William Pitt the Younger, Sir Robert Peel, George Goschen, Sir William Harcourt, H. H. Asquith, and Lloyd George (again) among finance ministers. The philosophical issues have been set out in recent left-libertarian writings which themselves have an important heritage that I have no space to explore separately (but see, e.g., Steiner 1994; Steiner and Vallentyne 2000, 2001; Otsuka 2003). If intellectual authority counted for everything, then the case for taxation of land values would be indefeasible.

It does not count for everything. Politics counts for a lot. Louis XIV’s finance minister, Jean-Baptiste Colbert (1619–83), reportedly said that “The art of taxation consists in so plucking the goose as to obtain the largest possible amount of feathers with the smallest possible amount of hissing.” Colbert led the mercantilist school which is the special target of Adam Smith’s anger in *The Wealth of Nations* (Smith 1981 [1776]).

Smith’s four maxims of taxation are set out in Book V of the *Wealth of Nations*. Each maxim is introduced in a single sentence, which Smith proceeds to gloss (glosses not copied here):

I. The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.

II. The tax which the individual is bound to pay ought to be certain, and not arbitrary.

III. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it.

IV. Every tax ought to be so contrived as to take out and to keep out of the pockets of the people as little as possible, over and above that which it brings into the public treasury of the state.

(Smith 1981 [1776] V.ii.b.3–6; pp. 825–6)

Smith does not claim that his maxims are original. He says that their ‘evident justice and utility...have recommended them more or less to the attention of all nations’ (V.ii.b.7). Smith is a very careful writer. He says what he means and means what he says. The maxims (‘canons’, as Henry George and many since have called them) had been recommended to the attention of all nations; but all nations were tempted down

Colbert's path, or down the path of favouring rent-seeking special interests (about which Smith is savage), or both.

p. 187 A Smithian tax system is progressive and neutral (I shall defend the "progressivity" of Smith's maxims in a moment). It is also transparent. A Colbertian system is as non-transparent as possible—the goose must not know that it is being plucked—and ↳ in general is neither progressive nor neutral. Perhaps the most Colbertian tax in the UK is Employer's National Insurance contributions. They are big, contributing about 9 per cent of the total UK tax yield (Mirrlees et al. 2011: Table 1.1). The real incidence of these is on the employee, not the employer. To the employer they are just part of the cost of employing somebody, and therefore the employee's wages are reduced pro rata. But almost no employee knows how much he or she pays by this indirect route. Therefore there is no hiss. One of the most certain, and also most transparent, taxes is the tax on domestic property, called Council Tax in the UK. Although it violates Smith's maxim I, it satisfies the others. In the UK, it is only half the size of employer's contributions (4.6 per cent of tax yield). But its very certainty makes it conspicuous. Bills are issued direct to households once a year, and the tax is usually taken by monthly Direct Debit out of the householder's current account. The hissing is tremendous. As I hope to show below, it is not hard to redesign Council Tax to satisfy Maxim I: it then would look remarkably like a land value tax. There would still be hissing, but quieter.

Why is Maxim I 'progressive'? The technical definition of tax progressivity is that the marginal rate is always higher than the average rate. Thus, for instance, personal income tax is progressive in every jurisdiction I am aware of. In the UK, that is obvious because there are higher rates of tax which each kick in when the taxpayer's taxable income exceeds a certain threshold. Above that, the taxpayer's marginal rate is 40 per cent or 45 per cent: for every extra pound that she earns, she pays 40/45 pence in income tax. Her average income tax bill is, however, less than 45 per cent of her income. But a moment's thought reveals that even a flat rate of income tax is progressive: provided that, as is surely the case in every jurisdiction, there is a tax-free allowance for those who earn too little to come into the net. If the UK had a flat rate of income tax of 25 per cent, then every taxpayer's marginal rate of tax would be 25 per cent. But her average rate (tax paid as a proportion of income) would always be below 25 per cent because of the tax-free allowance.

Now let us revert to Adam Smith's world. The kick in Maxim I is in the phrase after "that is". As before, read him with the attention he gave to writing: *that is, in proportion to the revenue which they respectively enjoy under the protection of the state*. Rich people enjoy more revenue under the protection of the state than poor people. Some people are too poor to pay any tax, except perhaps regressive taxes such as excises. (An excise duty, say on tobacco, always takes a higher proportion of the income of the poor than of the rich. If poor people smoke more than rich people, an excise may take absolutely more per head from the poor than from the rich.) Therefore a tax that obeys Maxim I is a progressive tax. The tax system may not be progressive, if regressive excise duties outweigh progressive taxes (such as, in Smith's day, land tax: the poor owned no land). But any tax that obeys Maxim I is progressive.

If still in doubt, consider what Smith says specifically about land taxes.

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Both ground-rents and the ordinary rent of land are a species of revenue which the owner, in many cases, enjoys without any care or attention of his own. Though a part of this revenue should be taken from him in order to defray the expences [sic] of the state, no discouragement will thereby be given to any sort of industry....Ground-rents seem, in this respect, a more proper subject than even the ordinary rent of land [which is]...owing partly at least to the attention and good management of the landlord....Ground-rents, so far as they exceed the ordinary rent of land, are altogether owing to the good government of the sovereign.

(Smith 1981 [1776] V.ii.e.10–11)

Tax on ground rent therefore fits Maxims I and IV beautifully. It also does not distort economic activity, unlike any other practicable tax. Adam Smith is not as much a friend of Margaret Thatcher as he is often made out to be, nor vice versa. I come to Baroness Thatcher's view on land tax later in this chapter.

In the next generation, Smith had two influential readers: Tom Paine and David Ricardo. Paine (1737–1809) was at the heart of both the American and the French Revolutions. He was lucky to escape from the latter with his life. His reputation has always been more as a pamphleteer than as an original thinker. Nevertheless he was a great synthesizer. His most remarkable publication in this context is *Agrarian Justice* (Paine 1995 [1797]). He proposes a scheme of universal benefits, to be given to each citizen at the ages of 21 ('to enable HIM or HER to begin the World!') and 50 ('to enable them to live in Old Age without Wretchedness, and go decently out of the World'). Paine takes Smith's idea about the special character of ground rent further and mixes it with John Locke's idea that originally the earth was the "common property of the human race":

the value of the improvement only, and not the earth itself,...is individual property. Every proprietor therefore of cultivated land, owes to the community a *ground-rent*.

(Paine 1995 [1797]: 418)

Paine wants ground rent to be extracted in the form of an inheritance or estate tax:

the subtraction will be made at a time that best admits it, which is, at the moment that property is passing by the death of one person to the possession of another.

(Paine 1995 [1797]: 421)

David Ricardo (1772–1823) was a very different sort of writer, whose work nevertheless has implications as radical as Paine's. One of the pioneers of the marginal principle in economics, he builds up his theory of rent from the observation that land is brought into production just up to the point that the most marginal land from which a marketable crop can be raised is brought into use. Beyond that point, land is left uncultivated. All the land more productive than the most marginal parcel earns extra, some of which is kept by the landlord in the form of rent. Like Smith and Paine, Ricardo insists that "rent", as usually described, must be broken into two components: the rent for unimproved land, and the rents for improvements, such as drainage, roads, and buildings put up by the landlord. The latter are payments for services; the former are not. Like his predecessors, Ricardo argues that taxation of the rent on unimproved land is the least distorting tax. Rent, so properly defined, is that portion of the produce of the earth, which is paid to the landlord for the use of original and indestructible powers of the soil (Ricardo 2004 [1817]: 67).

Many thinkers less subtle than Smith and Ricardo drew the conclusion that the tax on land values should be the *only* tax. One of these was the American journalist Henry George (1839–1897). Having observed that the only people whom the San Francisco gold rush made rich were land speculators, he concluded that '*We must make land common property*' (George 1929 [1879]: 433; emphasis in original). He reached back to the French physiocrats (contemporaries of Smith, who criticized them heavily) for the view that the way to do this was by a single tax on land. Quoting Smith's maxims without attribution (George 1929 [1879]: 408), he maintained that the single tax on land was the tax most compatible with them. George anonymized Smith's maxims, and may have been the first person to label them the "canons of taxation".

George's ideas peaked in influence in the first two decades after his death. They helped to drive the politics of the "People's Budget" of 1909. The most eloquent Georgeite was the young Winston Churchill, a minister in the Liberal government that introduced the People's Budget. Young Winston's statement of the case has never been bettered:

Roads are made, streets are made, railway services are improved, electric light turns night into day, electric trams glide swiftly to and fro, water is brought from reservoirs a hundred miles off in the mountains—and all the while the landlord sits still....To not one of those improvements does the land monopolist as a land monopolist contribute, and yet by every one of them the value of his land is sensibly enhanced....[T]he land may be unoccupied, undeveloped, it may be what is called ‘ripening’—ripening at the expense of the whole city, of the whole country, for the unearned increment of its owner.

(Churchill 1970 [1909]: 118–19)

However, the People’s Budget was defeated in the House of Lords and its land tax provisions were never implemented. The long switch from indirect to direct taxation, to be discussed in section 10.2, has obscured the importance of the insights of all the land-taxers from Adam Smith to Winston Churchill. Only recently have they emerged blinking into the limelight. The case made by Smith, Paine, and Ricardo has never been effectively contradicted. Section 10.4 explains what has happened to the political case.

10.2 The Switch from Indirect to Direct and from Opaque to Transparent

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In Adam Smith’s time, the main taxes in Europe were nominally land taxes, although they were very far from being taxes on Ricardian rent. There were also tithes or teinds (church taxes paid as a proportion of the produce of the land) and excises and customs duties, which it became Smith’s job as Commissioner of Customs for Scotland to oversee. One of his subordinates for a time was Robert Burns, author of *The de’il’s awa’ wi’th’exciseman* and exciseman in Dumfries (McLean 2006: 21, 39–40). These are all indirect taxes, as is any other tax on purchases (e.g. value added tax in the EU). Ultimately, the burden of all tax is borne by the consumer (Kay and King 1990; Mirrlees et al. 2011; Institute for Fiscal Studies 2016). An indirect tax is one where the ultimate consumer pays indirectly, because an input has been taxed and the producer of that input gets the money back from the ultimate consumer. By contrast, direct taxes are levied on each consumer’s income, property, or profits. Indirect taxes are generally less transparent than direct taxes, because they are rolled into the prices that consumers ultimately pay.

War brought change to the UK tax system. Prime Minister Pitt the Younger, a devotee of Smith (McLean 2006: 22–3), first introduced income tax in his budget speech of 1798, as a device to pay for the Napoleonic wars. He commended the ‘equality of the tax, and the general efficacy of the measure’—language that suggests he had his mentor’s maxims in mind. As William Hague summarizes it:

Income tax would thus be fair, collectable, and would provide for the more rapid repayment of the greater debts now being incurred. It would be applied on a sliding scale, zero on incomes below £60 a year, and then one twentieth on those over £60, rising to one tenth on incomes over £200.

(Hague 2004: 434)

The foundation for a progressive neutral tax system had been laid. Pitt’s income tax was obviously progressive. It was also neutral in that it was intended to apply to all sources of income, with a separate schedule and separate collectors for each. (The schedules remained until the 2000s; separate collection did not.) However, it expired at the end of the war. It was revived by Pitt’s disciple Sir Robert Peel, as announced in one of the great Budget speeches:

[Y]ou must so adapt and adjust your measures as not to bear on the comforts of the labouring classes of society. My conviction further is, that it would not be expedient, with reference to the

narrow interests of property, that that should be done. Well then, Sir, I must, with my sense of public duty, abandon the hope of realising in the present year any revenue from the post-office. Shall I revive the taxes which were laid upon great articles of consumption, and which were very productive? Shall I revive the taxes upon salt, upon leather, and upon beer?...Shall I increase the taxes on railways? I confess nothing but a hard necessity would induce me to derive revenue from locomotion in the present state of this country, when it is a great object to facilitate the transfer of labour, and to enable those to whom labour is capital to bring it to the best market....[T]o those who in small communities turn their attention to financial affairs, and who fancy they have made some discovery that pretty nearly puts them on a level with Archimedes; when finding that pianofortes, umbrellas, or such articles are not subject of taxation, they immediately suggest them to the Chancellor of the Exchequer, accompanied with a claim for a very large percentage on the ground of the novelty of their discovery and the certain success of its application,—I shall take this opportunity, of discouraging all such suggestions....I propose, that for a time to be limited, the income of this country should be called on to contribute a certain sum for the purpose of remedying this mighty and growing evil. I propose, that the income of this country should bear a charge not exceeding 7d. in the pound....I shall propose, that from the income-tax I now recommend all incomes under 150l. shall be exempt.

(Hansard 11 March 1842, from http://hansard.millbanksystems.com/commons/1842/mar/11/financial-statement-ways-and-means#S3V0061P0_18420311_HOC_23, consulted 28.09.11)

Peel's income tax was to be levied under the five schedules previously defined by Pitt, of which the financially significant ones were Schedule A, 'the property which was derived from land', and schedule D, 'income derived from the profits of trades and professions'. Schedule E, then defined as 'the income of all public officers' was insignificant, although it came to cover the vast majority of income subject to income tax, which is deducted at source on the pay as you earn (PAYE) system. Like its predecessor, therefore, Peel's income tax was progressive and neutral. Despite all efforts by that great Peelite and Pittite Chancellor of the Exchequer, W. E. Gladstone, it never proved possible to abolish income tax.

In the worlds of Pitt and Peel, the tax-and-expenditure regime was progressive on the tax side, but not on the expenditure side. What would now be called social protection and was then called the Poor Law was financed out of local taxation. This might be locally progressive but it was globally regressive after the Industrial Revolution. As every commentator from Charlotte Brontë to Dickens to Disraeli to Engels noted, unemployment in industrial areas could be both cyclical (in trade depressions) and structural (among trades like handloom weaving that were made obsolete by innovation). A consequence of this is that local support for local social protection could not work. The areas that had most expenditure needs had least tax capacity, and vice versa. One of the first, and curiously overlooked, great UK finance ministers to understand this was George (Viscount) Goschen, Chancellor of the Exchequer in the Unionist government of 1886–92. The Unionists hated the idea of devolution (Home Rule) to Ireland. Faced with a phalanx of Irish Party MPs determined to achieve just that, they resorted to what one of them, Gerald Balfour, described as killing Home Rule with kindness: i.e. by redistributive expenditure on social protection and public works in Ireland. Goschen's Budget of 1888 initiated formula funding for Ireland and Scotland. The following year, he initiated estate duty, which his Liberal successor Sir William Harcourt made more progressive in 1894 to the fury of landowners.

The next Liberal government (1905–10) was the most redistributive in British history to that date. Successive chancellors H. H. Asquith and David Lloyd George expanded social protection with non-contributory and nationally uniform old age pensions (1908) and a contributory National Insurance scheme against inability to work through sickness or unemployment (1911) (Braithwaite 1957).

p. 192 However, the government's fiscal programme was overturned by the House of Lords, who defeated the 1909 Budget by 350 votes to 75:

[A]s is so often the case when the House of Lords is engaged in reaching a peculiarly silly decision, there were many comments on the high level of debate and on the enhancement it gave to the deliberative quality of the chamber.

(Jenkins 1968: 100–1)

It was peculiarly silly because the counter-revolutionary action of voting down supply, which had been reserved to the Commons since the English Civil Wars ended in 1648, led to the Parliament Act 1911 and a substantial restriction on the Lords' veto power. Nevertheless, in defending the material interest of the landed class, it proved effective. The Lords' ire was directed not at progressive income tax, nor at increases in excise, but at the trivially yielding land tax structure in the 1909 Budget. Although the Liberals were re-elected in both of the 1910 elections forced on them by lordly and royal veto plays (McLean 2012; McLean and Nou 2012 [2010]), they lost their overall majority. They now depended on the Irish Party, which was in a position to insist first on the Parliament Bill and then on Home Rule. Because the Parliament Act required a Commons bill to be passed three times before it could be enacted without Lords' consent, Home Rule (and the similarly placed Welsh disestablishment) occupied most of the sessions of 1912, 1913, and 1914. The only (though not trivial) social protection legislation of the Liberals' third term was the enactment of National Insurance in 1911. Lloyd George returned to land tax in 1914, but his plans were defeated by a backbench revolt of landed Liberals just before the First World War broke out.

The subsequent history of land value taxation in the UK is equally negative. When the Attlee Labour government (1945–51) introduced a regime of land-use planning (Town and Country Planning Act 1947 c. 51), they recognized that by increasing the scarcity of what young Winston had called 'ripening' land, government was increasing its price relative to that of unripe land, and that it was legitimate for the public to reclaim in tax some of the betterment in value that they had granted in planning permission. However, both then and in later iterations, property developers simply waited for a change of government, successfully betting that a Conservative administration would repeal betterment taxes. The ghost of a betterment tax lingered on in "Section 106 Agreements" (the reference is to Town and Country Planning Act 1990 s.106), by which a developer could be required to spend money on infrastructure as a condition of being granted planning permission. Section 106 Agreements were an interesting example of a tax that demonstrably violates all four of Adam Smith's maxims, although they satisfy Colbert's.

In a Colbertian move noticed only by tax specialists and backbench Conservatives, the Macmillan Conservative administration (1957–63) abolished Schedule A of income tax in 1963. Schedule A was, by Peel's calculations, the highest-yielding of the five schedules in 1842 (from

p. 193 http://hansard.millbanksystems.com/commons/1842/mar/11/financial-statement-ways-and-means#S3V0061Po_18420311_HOC_23, ↪ table in text at col. 444: Schedule A was expected to contribute £1.6 million (42 per cent) of the £3.771million total yield). The campaign to abolish it came from Conservative backbenchers such as the newly elected Margaret Thatcher. In 1960 she was reported to be

in favour of the abolition of Schedule "A" and said a number of people in Parliament had been campaigning for its abolition. It dated back to 1842, when one could not get at individual incomes and the assessment of property was the only way.

The campaign against Schedule "A" was now getting very strong and if nothing was done about it in the Budget speech, she thought an amendment would be put down to deal with the matter.

(*Finchley Times*, 19 February 1960 at <http://www.margaretthatcher.org/document/100947>)

By 1960, Schedule A had become a tax on the imputed income from owner-occupation of houses. It led to much hissing, not only in Finchley, because the income stream that it taxed was invisible but the tax chargeable was visible. However, its abolition violated the principle of tax neutrality. One form of investment (owner-occupation of houses) was then favoured in the tax system twice over compared to others: by the non-existence of Schedule A and by tax relief on mortgage interest payments (another favourite cause of Mrs Thatcher, who vetoed its removal). The latter anomaly has been removed; the former has not.

Thus in 200 years the UK tax system has become more transparent and relies more on direct taxation than formerly. However, transparency is not all to the good from the point of view of designing a fair tax regime. Taxes on domestic property and on bequests are transparent. Those liable to pay know that they are liable. This has consequences, to be explored now.

10.3 Special Properties of Land

As a tax base, land has some desirable properties. It doesn't move. They aren't making it any more. As Smith and Ricardo both noted, a tax on the unimproved value of land is the least distorting of all taxes. This is because, with any other tax, the taxpayer may adjust her activities so as to pay less. The tax authority receives less than it expected, and economic activity is distorted. In addition, any land tax may be philosophically justified (Young Winston again) while the landlord sits still.

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In fact, Young Winston, together with Lloyd George and Attlee's ministers, was primarily making a different point to Ricardo's, a point that is independently valid. Much of the value of land derives from the uses to which it can be put. Land which would otherwise be useful only for agriculture, or not even for that, becomes useful as the electric trams and the far-off water are brought to it. These utilities are nowadays mostly supplied by the public sector, which gets none of the consequent revenue stream from the improved value of the land. Where they are introduced by the private sector, it makes a smaller return than it otherwise would, unless it gets hold of the land into which it develops. The only conspicuous UK example of coordinated development of transport and housing by the same company is Metroland, the area in north-west London and beyond served by the Metropolitan Line from Baker Street, and immortalized by Sir John Betjeman. It is no surprise that one of the leading Georgeites in contemporary UK politics is Dave Wetzel, a Labour politician who helped to run Transport for London when Ken Livingstone was mayor.

Therefore there are good philosophical (Smithian and/or Ricardian) arguments for not one, but two, land value taxes. One (call it the Ricardo tax) is a tax on the value of the 'original and indestructible power' of land before improvement. The other (call it the Churchill tax) is a tax on the proportion of the improved value of land that has been brought about by public investment. This could also be prospective: a tax on the increment of value that will accrue once permission for a high-value development is granted. It is this last version of the Churchill tax that Section 106 agreements palely shadow.

10.4 The Practical Politics of Land Tax

10.4.1 Land tax on domestic property

However, as the first review of the Mirrlees report ruefully states, 'those who lose from tax reforms tend to be vengeful while those who gain from them tend to be ungrateful' (Johnson and Myles 2011: 323). The rest of this chapter descends from Olympia (District Line and Overground) into the subterranean world of practicality and trade-offs.

As in the UK in 1909, tax reform can be blocked by vested interests. The House of Lords was then, by construction, a landed house, which blocked the reforms to land tax (and only those). This cannot recur, because the character of that house has changed and because the Parliament Act 1911 restores the Commons' monopoly of supply. Why then have all subsequent attempts at land taxation also failed, and what could philosophers and policymakers combine to do about it? The favoured treatment of owner-occupation of housing over other asset classes arises because the median voter is an owner-occupier or aspires to be, but does not know that she owns any other assets. (On the Colbert principle, the taxation of pension funds, where voters' unknown assets reside, fluctuates violently.) Of the two gross distortions favoured by Baroness Thatcher, one has gone (mortgage interest relief). The other remains (non-taxation of the income stream from owner-occupation). There are two other taxes on housing, both bad: Council Tax, and Stamp Duty Land Tax (which is also levied on transfers of commercial property).

p. 195 Council Tax, which pays for some local government services, was introduced in a hurry after politicians discovered that the Community Charge (poll tax) introduced in 1986–8 was the disaster that every informed commentator, including Chancellor Nigel Lawson, had predicted (Butler, Adonis, and Travers 1994). It marks a partial ↪ return to the pre-poll tax system of domestic rates. But, presentationally, it had to be called something different and work differently. It is therefore a worse tax than its predecessor-but-one. Rates still exist in Northern Ireland, whose citizens, consistently with Johnson and Myles 2011, show no gratitude for that.

Under Council Tax, each house is in a band determined by its value in 1991. Yes, 1991; that is not a typing error. (In Wales the reference date is 2005.) The bands are coarse and the tax is regressive. House values correlate very closely with household income (I deal with the apparent “Devon widow” exception later). Every house is taxed, so that there is no zero rate; and the tax per pound of 1991 valuation goes down jerkily from the lowest 1991 valuation to the highest.

Not every tax need be progressive, so long as the system as a whole is (Kay and King 1990; Mirrlees et al. 2011). But when a tax is regressive, there needs to be some independent reason for levying it, as each regressive tax makes the aim of achieving a progressive system that much harder. For example, some ‘sin taxes’ such as those on beer, spirits, and tobacco, are regressive because poor people tend to consume more of those sinful goods than rich people—perhaps absolutely more, and certainly more as a proportion of their incomes. For another example, the scope of VAT in the UK is unusually narrow by international standards, with zero-rating of food and children’s clothing, and reduced rating of domestic fuel. These exemptions are perverse. They are an inefficient way of protecting the poor, because they depend on people’s tastes. Poor people who like VAT-free foie gras do better than poor people who like VAT-able takeaway burgers. The reduced rating of domestic fuel flatly contradicts the rest of the UK’s carbon taxes. A broader base for VAT would increase welfare, but the losers would have to be compensated in the progressive part of the system by a reduction in their direct taxes and/or an increase in benefit rates. The regressiveness of Council Tax is as perverse as the reduced rate of VAT on domestic fuel. Neither serves any policy goal except helping to win the next election. Brave politicians have allowed a revaluation (as in Wales in 2005). Less brave ones have promised not to revalue (as in Wales for 2015) or frozen rates (as in Scotland in 2011).

How then could a brave government make Land Value Tax (LVT) for housing acceptable to the median voter? I suggest four answers, which are not mutually exclusive.

- Abandon stamp duty land tax (SDLT) on house sales. Taxes on transactions are inherently bad, as they discourage economic activity. The yield of SDLT, which is chargeable on both domestic and commercial transactions, is currently 1.8 per cent of the UK tax yield; Council Tax and business rates yield about 4 per cent each (Institute for Fiscal Studies 2016: Table 1). It would therefore be trivial to recoup the yield from SDLT in redesigned land taxes on houses and businesses.

- Set a zero rate of LVT for the first, say, £100,000 of house values, and then set an annual rate of, say, 0.5 per cent of each house's sale value. (This is approximately the rate that would recoup the existing yield of Council Tax and domestic SDLT.) This not only makes LVT progressive, but is nicely Ricardian. In an old industrial town or former mining village, one might pick up a house in good physical condition for about the limit of the zero rate of SDLT, £125,000. This house is an analogue of the most marginal farming land in Ricardo's model. The land it is on has effectively a zero value, so that it should bear zero tax. The same argument applies to countries such as Ireland and Spain where there were vast speculative developments of now-unsaleable apartments on land that, therefore, likewise has zero value. Since the price of building or repairing a house in Tow Law is little different from the price of doing the same thing in Chelsea, almost all the difference between the prices of similar houses in Tow Law and Chelsea is simply the difference in the Ricardian rent of the land they stand on. It is appropriate that this difference should bear a Ricardian tax.
- Make local zoning authorities less afraid of NIMBYs (Not in My Back Yard protesters). In the UK, the zoning authorities, except in National Parks, are elected local authorities ('councils'). For elected members, the decision whether or not to allow a development is unbalanced. A council will get into no trouble for refusing a development; it may get NIMBY trouble for permitting it. The extra Council Tax an authority would gain from permitting new houses tends to get lost in the elaborate block grant formula which pays for most of local authorities' expenditure. A robust LVT on houses would allow councils to keep all their domestic LVT; align the incentives facing them more appropriately; and enable the grant system to be simplified.
- Make an offer to Devon widows. Much of the opposition to domestic LVT focuses on the plight of the asset rich/cash poor household: stereotypically, a widow who continues to live alone in the former family home in Devon. A householder who is unable to pay her LVT after all relevant benefits have been taken into account may, therefore, defer her tax liability until she dies or her house is sold. This idea reaches back to Tom Paine's insight that the easiest point at which to collect the tax is at a transaction. Note that this is conceptually quite distinct from saying that the transaction itself will be taxed. Deferred LVT would not be the same as either SDLT or Inheritance Tax. Those who would do less well under such arrangements are not Devon widows but the sons and daughters, nephews and nieces, of Devon widows, a less generically deserving class.

10.4.2 Land tax on commercial property

The present property taxes on commercial and industrial property in the UK are SDLT, Section 106 Agreements, and Business Rates (officially National Non-Domestic Rates). Business Rates yield about the same as Council Tax in each year. Although collected by local authorities, the proceeds are pooled and redistributed as part of grant arrangements. This is done for equity reasons: the capacity of councils to attract business varies even more than their capacity to attract housing. But it means that the incentives to face down NIMBYs are even weaker than for domestic developments. The reward for facing them down is extra business rates, which, since 1990, have been immediately equalized away. UK governments have recognized this problem, and in 2015 Chancellor George Osborne announced that by 2020 the proceeds of business rates would be returned to the council that raised them. This solves the NIMBY problem but worsens the equity problem, as the councils with a robust Business Rate base are all in London. An equalization scheme, the details of which are not yet known, will certainly be needed as the complement of localization.

Mirrlees et al. (2011: Chapter 20) argue that the structure of business rates is inefficient, as they tax an intermediate input (business premises).

[T]here is a strong case for levying a land value tax, which is a tax on pure rent—if the practical difficulty of valuing land separately from the buildings on it can be overcome.

(Mirrlees et al. 2011: 477)

Can it be overcome? That difficulty was a sufficient reason for the failure of Lloyd George's land tax in 1914 (Offer 1981; McLean and Nou 2012 [2010]). It is admittedly not easy. There are some purchases and sales of bare land: for example, forest land, farmland with no structures on it except dirt-cheap barns, or empty brownfield sites. But none of these is exactly Ricardo's 'original and indestructible powers of the soil'. Planted forests have had money spent on them; both they and natural woods may attract future subsidy (which is capitalized into sale prices), and need year-to-year management. Farmland has been ploughed, drained, and fenced. Empty brownfield sites have been cleared, and have infrastructure (utilities, sewage, transport) on site or at their edges. LVT for non-domestic land would certainly require a beefed-up valuation agency. But the task would not be as intimidating as in Lloyd George's time. Satellite mapping of all the land in developed countries is now available. Valuation in principle requires less work on the ground than it did. There is an existing UK government valuation agency which could be expanded and, perhaps, integrated with the Ordnance Survey.

An important step, which could be taken before the national valuation register was ready, would be to remove the anomalies and exemptions in the present structure. Farmland is exempt, as are empty buildings and empty brownfield land. These exemptions result from lobbying, not from first principles. There is no reason why farming should be taxed more lightly than other ways of making money, and the existing exemption gives rise to multiple opportunities for tax avoidance. As to unoccupied land, owners should be given an incentive to develop or to sell it; and councils should be given an incentive to help its development or sale.

p. 198 A further point, which applies to both domestic and business LVT, is that it is the best tax to fund local and subnational government, for the very simple reason that land does not move, and therefore there is no scope to avoid tax by moving to a lower-tax jurisdiction. LVT could revive local government in England by giving it more fiscal responsibility, aligning taxing and spending decisions better. There would still need to be an equalization regime, but it urgently needs (in any case) to become less baroquely non-transparent. LVT could help here.

Scotland, Wales, and Northern Ireland are gaining more devolution within the UK. Scotland has had Scottish National Party (SNP) governments since 2007. The SNP is committed at least in the long term to Scottish independence and in the interim to what the SNP calls "devolution max", which would entail devolution of all taxation and most spending to Scotland. The Calman Commission of 2009 (Independent Expert Group 2008, 2009; Calman 2009) proposed a much more limited degree of tax devolution (its terms of reference prevented it from going further). But based on the principle that land does not move, it proposed a range of small land and quasi-land taxes (landfill tax, aggregates duty, airport passenger duty) for devolution; gently reminded the Scottish Parliament that it already controlled Council Tax and Business Rates; and encouraged policymakers to think anew about land taxation. The depressing immediate response was an auction among the parties in the 2011 Scottish Parliament election as to how totally and for long they would freeze Council Tax.

This situation changed as a result of the Scottish independence referendum of 2014. In the last week, when the pro-independence side was surging in the polls, the anti-independence parties joined in a so-called 'Vow' that they would greatly increase Scotland's tax powers in the event of a 'No' vote to independence. The No side won by a margin of 10 percentage points, and accordingly the Smith Commission was set up (Smith of Kelvin 2014). Reporting at great speed, this recommended the devolution of almost the whole of income tax, and the assignment of half of VAT revenue in Scotland to the Scottish Parliament. The effect on

land taxes has been indirect. Because the Scottish Parliament is closer than before to being fiscally responsible—that is, responsible for raising what it spends—it has to look in a grown-up way, for the first time, at all of its tax powers. The freeze on Council Tax has ended, and SDLT in Scotland has been replaced by a Land and Buildings Transaction Tax. In fact, SDLT has been amended in the rest of the UK to be more like the Scottish tax, and some of its most objectionable features have disappeared.

In Wales, politicians were deafened by the hissing when Council Tax values were updated in 2005, and an extra Council Tax band was added for very high-value properties. But the number of properties falling into the new Welsh Band I is tiny, and those who do not live in Castell Coch may not notice Council Tax as being any more progressive there than in Scotland or England.

p. 199 Nevertheless, it is fair to say that both the Scottish and Welsh governments have taken some baby steps towards a more proportionate system of property taxes. ↪ Northern Ireland never abandoned rates, and therefore starts from a better place, or would do if its politicians could focus their attention away from sectarian issues.

10.5 Property, Theft, and Inheritance

There is one more property tax to consider—estate tax, known misleadingly in the UK as inheritance tax. The philosophical issues surrounding it have not changed since Paine. The politics have.

In every developed economy, the main component of the estate of those who die is their land and property. ‘Property is theft’ was the self-contradictory slogan of the French anarchist Pierre-Joseph Proudhon (1809–1865). In the steps of Rousseau, Proudhon wished to counter the idea that property owners had a legal and moral right to keep all their property free of tax, and to hand it on intact to their heirs at death. Proudhon, and some of his followers, wished to see an estate duty of 100 per cent. A non-contradictory version of Proudhon’s slogan is that land values are socially constructed. As the thinkers reviewed in this chapter all knew, land is valuable only because human beings do things with it. Some of what they do could exist without government: Ricardian rent would arise even in an anarchist society because some land is naturally more productive than other land. But even the most laissez-faire country needs a system of property rights before agriculture can get going, as otherwise a strong man need only wait until someone else’s crops have ripened and then help himself. Smith discussed the co-evolution of agricultural and legal property codes at considerable lengths in his Glasgow law lectures. These were intended to become a book which would have filled in the territory between *Theory of Moral Sentiments* and *Wealth of Nations*. But the project was unfinished at Smith’s death. On his deathbed he asked his executors to destroy his manuscripts, which they did. However, almost 200 years later, two versions of the law lectures turned up in lecture notes taken by two students in successive years (Smith 1982). So Smith’s arguments about the evolution of property have now become well known to scholars. All this lies behind Smith’s innocent-looking half sentence in Maxim I: *that is, in proportion to the revenue which they respectively enjoy under the protection of the state*. Even the most minimal state maintains courts and police officers, which have to be paid for. A non-minimal state provides other public goods, including utilities, and private or semi-private goods such as education and social protection. These are financed out of tax; and they contribute to the socially constructed value of land.

p. 200 The twentieth-century addition to this edifice was zoning (planning permission). The right to refuse planning permission confers extra value on land that has it. It creates a scarcity of land available for high-yield uses. No politician since, and including, the young Winston Churchill has found out how to tax the betterment value of land that is either serviced by publicly funded utilities, or has planning ↪ permission for a high-yield activity, or both. Therefore land owners have capitalized their untaxed gains into the price of their assets.

For most householders, their home is their only real asset of any consequence. Furthermore, most homeowners paid the recently inflated prices that have characterized the housing market in most developed economies in recent decades. Not they, but previous owners, capitalized their untaxed capital gain into the price of houses.

This explains why the politics of estate duty (known as Inheritance Tax—IHT—in the UK) is so toxic. Any politician who proposes to raise, or even to maintain, it is immediately assailed by slogans such as “inheritance tax is a death tax” and “inheritance tax is double taxation”. A promise by the Conservatives to raise the threshold for IHT in 2007 knocked Labour Prime Minister Gordon Brown off balance, a balance he never recovered. He scrambled to put a “me too” threshold increase into his budget, but this did not restore his credibility. And yet, IHT is only paid on a tiny proportion of estates, depending on the ratio of house prices to tax thresholds. In the UK since 1993, the proportion of estates liable for IHT has varied from 2.5 per cent to 6.8 per cent (Institute for Fiscal Studies 2016: Table 14). In the USA, where the politics of protest against so-called ‘death tax’ has been even more acute, the proportion of estates liable for federal estate tax dropped to 0.2 per cent (Tax Policy Center 2016).

Two things are necessary to break this impasse. One is to look at tax and transfers from a whole-of-life basis. The other is to dispel myths about “death taxes” and “double taxation”, and at the same time to allay the reasonable fears of householders who think that their only real asset may be needed in old age to pay for their care.

As all tax specialists including the Mirrlees team insist, tax and benefits should be studied over the taxpayer’s life cycle. As an accounting identity, my lifetime income and expenditure must be equal, plus bequests received, minus bequests given. At some stages in my life I earn more than I spend; at others, vice versa. For most people, at some stages in life they pay more in tax than they receive in benefits; at others vice versa. Household saving to meet the needs of old age and dependent children is very important, and it needs to be done in a stable framework (another reason why changing taxes, even bad taxes, can be difficult). Rapidly increasing longevity means that the burden (on somebody) of health and social care for those no longer able to live independently is highly likely to increase. As owner-occupiers get older, they come to see more and more that their house is the main asset which could defray whatever part of these costs is not met by the state. The value of their house has been raised by past public investment and public policy, especially restrictions on planning permission for new housing. How is this vicious circle to be broken?

First, by tax reformers winning a battle of rhetoric. Inheritance taxes are not death taxes. Dead people do not do much. One thing they do not do is pay taxes. The real incidence of all inheritance, bequest, and estate tax is on those who receive the proceeds. Therefore also, IHT is not double taxation. Those who pay the tax have not already paid tax on the bequest. For the inheritors, the bequest is a windfall that stands outside the accounting identity *lifetime income = lifetime expenditure*.

p. 201 An ageing person has a reasonable interest in what Paine eloquently called ‘liv[ing] in Old Age without Wretchedness, and go[ing] decently out of the World’. Paine proposed to fund this by a cash transfer. Nowadays, it is funded by a mixture of tax-financed and private provision for health and social care. Although the tax system should include a land tax which both reduces the value of the ageing person’s house, and requires payment from a cash income stream that she may not have, the remedy can be adapted from one that also occurred to Paine: viz. that the tax liability may accrue until the person dies or the house is sold. In a well-designed tax system it should accrue at zero real interest.

Of course this arrangement leaves losers compared to the present situation. But those losers are not the elderly, but their heirs. If, at the extreme, the tax liability on their mother’s house, plus the money she has spent on social care, completely eat up the inheritance they were expecting, that is sad. But at least they will

have no IHT to pay. And no *moral* issues arise: there can be no moral right to demand, or expect, an untaxed inheritance.

Property is not theft. But it could be taxed in a more rational way than at present. In the long run, everybody would gain.

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