

An outline of the idea of land taxation

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Abstract: There are foundations of land taxing presented in the paper in the context of modification of liberal system. The benefits of shifting taxes from labour and capital towards land are exposed, as well as the arguments against taxing of land. The argument being explored in the article is that if a society is to benefit the economic growth, a permanent and effective transfer of economic resources (including land and its resources as a priority) has to feature contemporary dynamism of economies. And, it is the economic system founded on the 'law' of land taxation that can deliver the appropriate conditions.

The examples of countries who gather taxes from land are highlighted. Post-socialism economies of Eastern Europe, undergoing shocking transformation, many of whom are the European Union members, are poverty stricken even if the statistics report significant economic growth. The concern of economic transformation of post-communist countries is evoked in the light of economic system formation.

Key words: land as the subject of taxation, social justice, economic efficiency

Investigation reveals that differences in civilization are not due to differences in individuals or races, but rather to differences in social organization. Progress is always kindled by association. And civilization always declines as inequality develops.

(Henry George, *Progress and Poverty Introduction*)

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1. Introduction

The fall of the Iron Curtain uncovered overwhelming defeat of the socialist conceptions of governance. The failure of the conception has the source in natural inability of generating economic growth, as the system was not able to adjust the structure of consumption to the structure of production. It was

associated with the lack of necessary and efficient allocation of the factors of production and the alteration of the structure of production.

Capitalists, on the other hand, at least since the crisis of the 1930s, have been searching for the remedies for deficiencies of capitalistic economic system (Lippman, 1945, p. 270). Capitalism of the 21st century is endangered since it prevails almost all over the world and is not a subject to any significant competition. And, that situation is a sort of turn-on for the research of alternative economic systems.

The last decades revealed that Keynesizm despite its renaissance lost its power in the economic debates. The opposite conceptions of Friedman's monetarism and supply economics from the 1980s also lost their significance. Liberal ideas as the theoretical foundations of socio-economic systems have been heavily criticized in literature and in debates concerning alternative socio-economic systems (Sadowski 2003, pp. 30–33).

It is worth mentioning the critics by Stiglitz of 'invisible hand of market' as the generator of high levels of productivity. He shook the basis of the paradigm of neoclassical economics together with the definition of the state of equilibrium to which he attached meaning deemed to be closer to economic reality. The new definition of equilibrium described situation which economic agents do not want to change, but the situation does not, at the same time, signify that a market is cleared (Stiglitz, 2004).

Economic effectiveness and guarantee of fundamental social values, such as social justice and freedom, require unleashed and spontaneous reaction of economic agents to be released. In addition, it is necessary to introduce the criterion of national income distribution and justice widely understood. Such perceived basis of socio-economic system ought to be interpreted as more developed/ advanced level of liberalism directed towards not only methodological and ethical individualism but also primal social value—justice as the full right of all to the fruits of their effort and the right to land and other natural resources. Those attributes of modified liberal system, in which freedom and spontaneity of economic agents as well as 'law' (rule) of land taxing, by operating towards better-being of a society, have the mission to overcome revealed today deficiencies of liberal doctrine.

Not only does the knowledge about the effectiveness of market allocation but also the understanding of the sources of market failures determine the substance of the inquiry whether moving towards higher and higher levels of competitiveness may take place when the dispersion of income and wealth is so wide (75% of the society is situated in the lowest layer of income in the advanced economies). Post-socialism economies of Eastern Europe, undergoing shocking transformation, many of whom are the European Union members, are poverty stricken even if the statistics report significant economic growth. It reflects unequal distribution of income, which releases social frustration and dissatisfaction—potential turn-on of social turmoil.

Leaving such an important factor of production like land to be allocated just by the forces of market may lead to its monopolization, especially in the times of crisis, when prices of all factors of production fall steeply or when the capital in the mostly liquidized form, i.e. money, reaches the level of saturation. It is because of the natural tendency of market economies to supersede competition and create monopolies and oligopolies (Eucken, 1990, pp. 31, 254).

According to Georgists, applying only the order of *laissez-faire* does not guarantee the effective use of production factors. It especially refers to land and through that impact directly

or indirectly impedes effective use of other factors. This sort of danger of capitalism generated by capitalists themselves is maleficent.

It was also W. Ropke who accented that it is natural for economic agents to seek economic rent actively. By doing it they make profits at the expense of those who have to bear the unavoidable loss. The situations of getting round of competition are widely observable, and consequently, monopolistic structures emerge (Ropke, 1994, p. 305).

Nowadays, world economies face complex socio-economic processes. There are challenges carried by globalization, deindustrialization, servicization that consumers, workers, employers, investors and other economic agents need to get accommodated to.

The fundament of economic system that is set on the 'law' of land taxation constructed by Henry George as the result of analysis of over 100-year history of liberal economies is put in the frames of the following postulates: 1) a man has the right to him- or herself, 2) he or she has the right to the effects of his or her work, 3) all have equal right to land and its resources.

The argument being explored in the article is that if a society is to benefit the economic growth, a permanent and effective transfer of economic resources (including land and its resources as a priority) has to feature contemporary dynamism of economies. And, it is the economic system founded on the 'law' of land taxation that delivers the appropriate conditions.

In the face of global and speedy changes, the most effective reaction of microeconomic agents is to adapt quickly. That is also what the European Union promotes in the actions such as Europe 2020.

The social and economic organization based on the system generating economic efficiency and justice delivers the opportunities for the rapid reallocation of resources as the reaction to continuous changes.

The transition of post-socialism economies is the reallocation of all factors of production driven by the socio-economic system alteration.

The chief issue of the economic problems in the long term is the effectiveness and the pace of allocation of scarce resources. The reallocation that is not enough efficient and fast is the main source of any economic crisis (Clark, 1957; Fisher, 1952; Fisher, 1945; Fisher, 1933).

Pareto criterion of efficiency employed widely in economics literature encounters its constraints. The problem became visible enough to provoke the suggestion by A. K. Sen to reject the Pareto optimality. There are a number of alternative criteria of social/ public choice delivered by A. K. Sen, R. Nozick, and J. Rawls (Acocella, 2002, p. 47).

2. The economic and ethical fundamentals of land taxation

And it was at least since the publication of the master-work by Henry George—*Progress and Poverty* (1879) that the conception of taxing value of land gained ground. It was to be the solution of the problem of persisting poverty in the midst of increasing wealth through effective use of economic factors and just distribution of national income among the members of a given society. Thus, efficiency and justice are the pivotal notion of the single tax system.

Land taxing is the result of researching the sources of the benefits of economic progress for all. Taxing land instead of other factors of production is believed to lower poverty by letting economic efficiency and justice flourish.

The foundation of land taxing is set on the ethical (on which the justice is based) and efficiency principles. Justice of land taxing is based on the premises that every person has the right to himself or herself, effects of his or her effort and that every person has equal rights to the natural resources. Taxing land is efficient because it permits to reduce other taxes, to compensate for local externalities caused by use of land, to shift land to the persons who can get higher return from it, to minimize the amount of land speculation.

Taxing according to the products of one's effort (labour) or savings is unjust and lowers the motivation to higher effectiveness (such as patent law for inventions). Introducing land taxing set by the above mentioned premises makes people use all factors of production more efficiently. Economic agents are more motivated to use labour and capital more effectively, because they receive all income from labour and capital as no tax is levied on them any more. Taxing land instead gives opportunity to equal access to the common natural good such as land. Creating incentives to boost productivity from land and other factors of production permits to assume that there would be sufficient amount of income generated in the economy to secure fundamental rights associated with realization the minimum indispensable to develop positive freedom and the full realization of privileges from negative freedom (A. K. Sen, R. Nozicki) (Acocella, 2002, pp. 84–85).

When taxes are gathered from what people earn (working or saving) or levied on spending, it generates excess burden (Figure 1). This means that incentives to work are lower than the value of what people produce and the incentives to save are lower than the productivity of investment financed by saving. Less saving means less investment. In the longer term, discouraging of investment diminishes the capital stock in an economy, and that entails lower productivity and lower wages (Tideman, 2004).

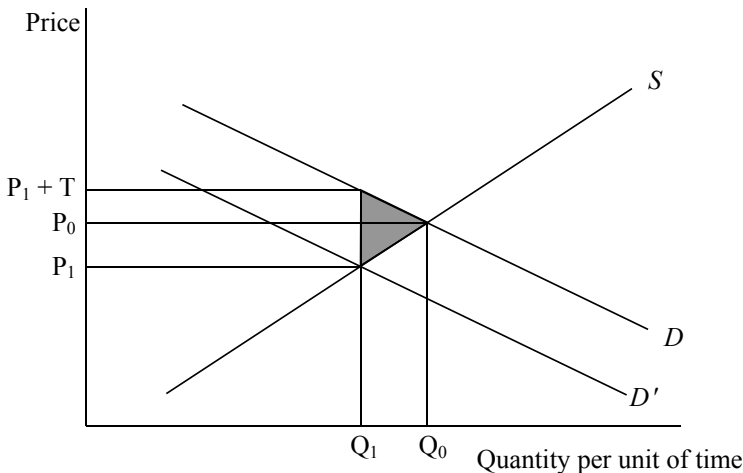


Figure 1. Supply and demand for a taxed good

Source: Tideman, 2004.

In the case of land taxing, there is no excess burden, i.e. the tax is neutral. In the land market, where the supply of land is perfectly inelastic (however, land used for accumulation of

money is characterized by elastic supply), a tax still leaves a wedge between the price for buyer and the price for seller but the quantity does not change (Figure 2). There are, however, some constraints on the analysis. Tax mustn't be of the amount higher than the rental value of land (otherwise, no one would be willing to have the land and pay tax for it), and tax cannot be increased if land is used more productively.

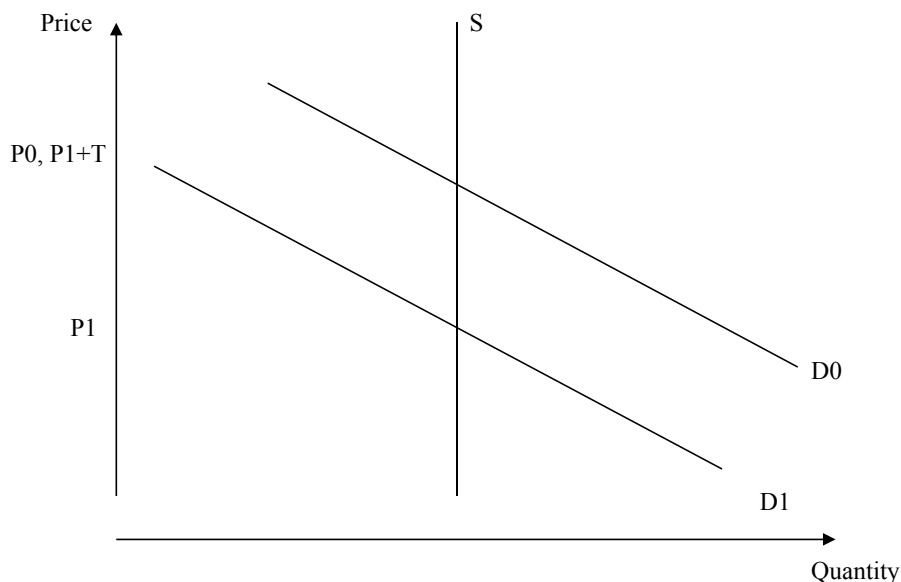


Figure 2. Effects of tax on land

Source: Tideman, 2004.

Land tax is even ‘better than neutral’. First, because, it internalizes negative and positive externalities associated with land use. Second, because it is to make lending markets function better. Third, land tax can eliminate those speculations on land that worsen economic efficiency (Tideman, 1994, pp. 103–140).

Economic gains that can be derived from concentrating tax system on land taxing instead of labour and capital taxes resolve to higher motivation to decide more effectively on how much to work and how much to save, as well as to speculate less in land (increasing the quantity of land that can be currently used) (Tideman, 2004).

The main channels of land taxation influencing economic growth is through removing taxes from labour and capital, redistribution taking place from living adults to children and unborn who acquire now the right to the land, increasing efficiency of land use.

When taxes are lowered, the earnings upsurge. Feldstein (Feldstein, 1977) estimates that the elasticity of earnings with respect to that part of income that is not taken at the margin by the state in the form of taxes is at least 1, and even more for workers with higher wages. If the action of removing labour tax is regional it has a tremendous effect in the form of attracting labour to the region. The attraction effect is even stronger for capital, which is highly responsive to the regional changes in net return.

Land taxation through redistribution to the next generations will induce adults with fewer assets to accumulate more intensively than they would otherwise do. Building such attitudes helps to intensify the accumulation of saving and capital.

Land is used more effectively when it is taxed because it is less profitable to speculate in land. Moreover, the capitalization of land taxes into the selling price of land (price of land is lower, but the cost of using it becomes higher—the annual tax) makes land more attractive for bidders with higher discount rates (more entrepreneurial) shifting it at the same time to those who will use it more efficiently. Inefficient use of land creates the income foregone now in the form of tax, which motivates to use land intensively (Tideman, 1998, pp. 263–276).

3. Some of the arguments raised against taxation of land

Taxing land would make rental value of land fall abruptly, which could eliminate lots of bank products impeding banking system function.

The explanation here is much of the virtual value and definitely difficult to proceed. A lot of mortgages would exceed the price of property if land taxes are significantly higher. That creates the need to absorb the lacking value of asset on mortgages already granted, and reform the financial system in respect to the land as collateral.

Economic efficiency could be diminished when the land value would be abated after land taxing as the consequence of reduced possibilities to use land as collateral for entrepreneurs.

Highly possible resulting effect is more attentive investment of financial resources of banks, what is desired (Tideman, 1994).

Shifting the burden of fulfilling treasury to land taxation in the way that those who do not have money to pay tax on land have to let use the land to those who can afford paying assigned amount of tax (as can be derived from above) is contrary to the saint law of private property inviolability.

The benefits and costs should be analyzed by the society as a whole and by every individual and they should have the right to vote in the form of referendum.

The privilege of monopolizing a site is associated with paying a rent for it to the community, a land tax, calculated on rental value excluding land improvements. Excluding land improvements eliminates all speculation on land.

To ensure that land is not monopolized by people who can afford paying high amount of tax it is crucial to share the rent from land equally (at least the part of rent that is not reserved for infrastructure). Then, if every person has his or her share of the rent, then everyone will be able to afford paying the rent for an equal share of the land, out of their share of the rent (suggestion made by N. Tideman).

It is perhaps the greatest impediment in implementing a full version of land value tax that current landowners are not planned to be compensated in any way.

Henry George saw the problem in the same way as compensation for slave owners. The owners of land are perceived to have no right to the ownership in the first place, and any compensation for them that would have to be done from the public money would evidently have the attributes of taxpayers robbery. Furthermore, all those who own land and use it effectively will certainly afford paying taxes on the land, all the more that all other taxes (on labour and savings) will disappear (Kyrizai, 2000, p. 73).

Are there any countries in the world that implemented the land value tax as prescribed by Georgists?

In modern systems, land value tax (tax levied on the value of land excluding the value of buildings, improvements) co-exists alongside other taxes. Land value tax as a single tax is perceived to be not sufficient to raise large enough revenues (Posner, 1986, pp. 458–459) as setting the rate too high can surpass landowner surplus and result in abandonment of property and important decline in public revenue.

The state of New South Wales levies a state land value tax over a certain threshold (farmland and a person's principal place of residence are exempt). Land tax is used by the cities of Sydney, Canberra, and others in Australia, as well as the city of Mexicali in Mexico.

In Hong Kong considerable part of government revenues are generated by high land value tax.

In the US over 20 Pennsylvania cities employ split-rate property tax, i.e. they tax the value of land at a higher rate and the value of the buildings and improvements at a lower rate. This can reflect a compromise between pure land value tax and property tax levied on real estates, as well as gradual approach of the traditional real estate property tax to a pure land value tax. Florenz Plassmann and T. Nicolaus Tideman found that higher land value tax induced higher level of construction (Plassmann and Tideman, 2000, pp. 216–247).

Taiwan, Singapore, Estonia uses land value tax as well.

Moreover, Scotland, Kenya, Namibia, China are gradually shifting towards land value taxation. In many other countries, such as Belgium, Republic of South Africa, Zimbabwe, Ethiopia, Thailand, Hungary, there is rising interest in land value tax.

4. Principle of sound economic system and land taxation

The essence of every concept of economic system is the answer of the question on effective transfer of resources and coordination of economic activity at the macroeconomic level. As Allan Fisher pointed out, if a society is to benefit the economic progress, permanent transfer of economic factors (including land and other natural resources) is essential. Every impediment of the transfer is the source of economic crisis (Fisher, 1945; Fisher, 1933). The solution of the pivotal problem resolves to the equal right of all to natural resources and to the taxation of land—efficient system of prices of land.

The effectiveness of the system of prices (informative function) of land (land taxation) is realized by signalling the scarcity of land and can take place only if market competition exists. Market competition is guaranteed by land tax, which eliminates speculation and monopolization. And, that is the only way the prices of land are objective market parameters. That is the competition that induces the adjustment of economic agents to the scarcity of land reflected in the price of land. And, the process of adjustment dictates the optimality of allocation and transfer of land within an economy. Thus, applying efficient system of prices of land constitutes the basic criterion of the evaluation of every economic system. The parameter of freely operating prices is needed to protect the system against any deformation carried by such undertakings as credit expansion, public subsidies, regulation of selling and buying land.

Lester Thurow underlined that the increase of productivity depends on the velocity of the transfer of production factors, including land, from the activities with low productivity to

the activities with high productivity (Thurow, 2001). The impediment of the process is every form of monopolization and speculation of land, which deforms the system of competitive prices.

Equal access to rent from land (income from land tax) guarantees one of the crucial conditions for market of land to function effectively. Any barriers to enter the market—barriers to market supply or demand—destroy competition and bear the threat of monopolization. Even if there is competition but market is protected to any extent, effective allocation is undermined. Closing a market represents a means of weakening competition and reducing the motivation towards boosting competitiveness.

Private property—an indispensable element of rightly functioning market economy in the conditions of strong competition leads to an equilibrated distribution of economic power among economic agents. In competition private property does not give to economic agents economic power, but it lets them manage the private factor of production for the well-being of society (Eucken, 2003). Private property in the frame of socio-economic system basing on the single land tax is to increase productivity. The mechanism of market competition deprives the right to dispose the factor of production, especially land, every economic agent who will not be able to generate at least average level of productivity.

The freedom of contracting is, on the one hand, the prerequisite of well-functioning competition; on the other hand, it has to be realized as the protection against monopolization (freedom of contracts when competition is defective can lead to fostering monopolized structures).

The freedom in managing the land according to the rule of equal access should be encumbered with responsibility. That function is realized by paying tax for the right to use the land. The land taxation induces economic agents to analyze the market precisely as the responsibility for productive use of the land is accomplished under the threat of losing the right to the land.

It is indispensable that improving rivalry towards the highest efficiency levels is completed with responsibility. That is naturally delivered by the economic system based on land value taxation. Responsibility is necessary in the process of moving towards more advanced levels of productivity and flexible eliminating all those who waste the income from production factors, here, land. Responsibility is closely connected to one of the essential conditions of the productivity advancement, i.e. the rapidity of moving from low- to highly productive activities and excluding ineffectiveness reflected in the loss (Thurow, 2001).

In the analyzes of the patterns of productivity growth, long-term investments as their determinant are very exposed. For the investment to upsurge, the stability of the economic environment is crucial. The stable knowledge on the tax rates or commercial and insurance regulation strengthen the tendency/ willingness to develop investment projects. It perhaps mostly refers to the transforming economies of Eastern Europe. Moreover, the attention should be paid particularly to the aspect of strong natural inducement of investors towards consolidation of capital in the condition of economic instability, especially in taxation policy (the phenomenon of consolidation as the means of minimizing risk of legal and institutional environment).

5. Conclusions

The debates on economic progress in advanced economies concentrated on income inequalities, unemployment, decreasing living standards are often associated with the phenomenon of deindustrialization and accompanying delocalization.

Taking into account high short-term costs of deindustrialization and delocalization, there is a need for active policy in certain areas of economy, such as industrial transformation towards modern economy, researching alternative economic systems. All those endeavors are undertaken to eliminate the short-term, negative consequences of natural processes (necessary and desired) of the evolution of market economy—deindustrialization, delocation and de-investment connected with them.

Deindustrialization and delocalization are highly desired processes if the economic progress is to lead to the transformation towards economies with high levels of productivity. The transformation (reallocation of economic factors—especially land) should be effective and rapid (economic agents should behave as if the reallocation of resources is the nature of the market, otherwise, the criterion of all economic activities and economic successes). The alternative economic system, based on land value tax, seems suitable to face successfully the eternal, economic challenge, to promote the transfer of economic factors and guarantee the well-functioning of market competition. Land tax as a single tax creates the ‘new’ comparative advantage, defined by L. Thurow as the best conditions to localize economic activity and to move it to higher and higher levels of productivity (Thurow, 2004).

Structural alterations, no matter how theoretically positive or negative they are, should be analyzed precisely and separately on each economic ground.

Each reallocation, including those taking place in post-socialism Eastern Europe, which does not catch enough pace, is very often encumbered with such undesired social phenomenon as unemployment, inequalities, lower life standards, decreased level of social protection. The slow structural adjustments are frequently intensified with negative supply shocks (as the example of advanced market economies in the 1970s and the 1980s shows) or negative demand shocks (as can be observed nowadays in the European economies). Thus, driven by deindustrialization, ability to respond flexibly to rapid changes which exposes the potential of economy to adjust structurally, is the most important feature of European economies.

The main barrier in introducing land tax in the economies of Eastern Europe is the lack of awareness of the wide parts of society concerning the advantages and disadvantages of land taxation, as well as comprehension of the ideas which are pivotal for the reform, such as market mechanism, economic freedom, economic justice.

Furthermore, the important barrier of setting tax system on land tax is the value of great part of land that is unknown what makes the reform very costly. The lobbying of minority that would become victims of the tax reform which is powerful prevents it from realization.

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Zarys koncepcji opodatkowania gruntów

Abstrakt: Treści artykułu obejmują podstawy opodatkowania ziemi w kontekście modyfikacji systemu liberalnego. Podkreśla się w nim korzyści z opodatkowania ziemi zamiast z pracy i kapitału, ale również argumenty przemawiające przeciwko opieraniu systemu podatkowego i ekonomicznego na podatku od ziemi. Twierdzi się,

że jeśli społeczeństwo ma korzystać ze wzrostu gospodarczego, musi się w nim odbywać ciągła realokacja czynników wytwórczych, w tym ziemi. Podkreśla się, że propozycja opodatkowania ziemi jest wykorzystywana w wielu krajach oraz że może ona stanowić element tworzenia systemu gospodarczego w krajach postkomunistycznych.

Słowa kluczowe: ziemia jako przedmiot opodatkowania, sprawiedliwość społeczna, efektywność ekonomiczna
