THE CASE FOR A NEW PEOPLE'S BUDGET

Foreword by Sir Vince Cable

In 1909, “The People’s Budget” made a ground-breaking attack on poverty. But one reform was never implemented. Over 100 years later, a tax on land values is needed more than ever.

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WHAT IS LAND VALUE TAXATION?

In a modern society, the value of land is created in three ways: by natural qualities, like fertility or mineral wealth; by the presence of human population; and by the availability of public services. All of these are more or less a matter of location. None of them are contributed by the owner or tenant of the land. Hence it is only fair that the community which, together with natural endowments, creates this value should receive the benefit of it. On the other hand, all that is produced by work and the use of capital is rightfully the property of the producer. It follows that taxation should draw principally upon the value of land, and avoid, as far as possible, any charge upon property rightfully earned. This is the rationale of a land value tax, and is as valid today as it was a century ago.

“A variable land tax would, of its own accord, and without any attention of government, readily suit itself to the actual situation of things, and would be equally just and equitable.....”

Adam Smith, *The Wealth of Nations*, Everyman, p.315

“A tax on rent would affect rent only; it would fall wholly on landlords, and could not be shifted to any class of consumers.”

David Ricardo, *The Principles of Political Economy and Taxation*, Everyman, p.110

“Taxes on the value of land not only do not check production as do most other taxes, but they tend to increase production by destroying speculative rent.”

Henry George, *Progress and Poverty*, Hogarth Press, p.134

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Foreword

by Vince Cable

The centenary of the 1909 Liberal Government's attempts to introduce the taxation of land values always meant that the Party would be taking a special interest in LVT this year. As things have turned out we are doing so in the middle of an economic crisis which is bringing our whole financial management into focus and raising the possibility that government, of whatever party, will have to consider a significant increase in the level of general taxation. So this collection of essays on different aspects of LVT is particularly appropriate.

The booklet demonstrates that LVT is not just another property tax, important though it is that property should not go untaxed. The writers argue that LVT has far-reaching effects on breaking down monopoly land-holdings, on encouraging new enterprises and raising the levels of earnings, on recovering the cost of major and minor public works, on supporting small-scale farming and the cultivation of marginal land, on stabilising house prices and, perhaps most importantly, reducing the disparity between the rich and the poor. These are large claims but they spring from a fundamental view that the wealth produced over the centuries by the efforts of the community is reflected in land values and is therefore a proper target for taxation.

ALTER has done us a service by assembling these arguments at this time. The introduction of LVT is already part of our taxation policy. As a first step we want to see commercial rates replaced by site value taxation. But this is only a first step towards a wider system for taxing land values. Lloyd George could not be faulted for his enthusiasm for the cause but in the end he failed to deliver. Successive Labour governments have also failed to produce practical schemes which commanded cross-party support. A hundred years later, we need to be clear what our objective is and better prepared to achieve it.

House of Commons
August 2009

The People's Budget

by Geoffrey Lee

Without Henry George there would have been no People's Budget. The American economist's best-selling book, *Progress and Poverty*, had aroused worldwide interest in land value taxation. The fact that he came to England was due to a fortunate change in his circumstances. For once he was being paid to write and give talks. In October 1881 he went to Ireland under the auspices of the *Irish World* to act as correspondent and to lecture. In 1885 he was to make one of his most powerful speeches in London. Addressing a great crowd outside the Royal Exchange (now a shopping mall) he pointed up to the letters which are written across the front of the building: "The Earth is the Lord's". A man in the crowd cried out, "The Landlords'." George responded, "Aye, the landlords. They have substituted the landlords for the Lord above all; and the want of employment, the misery which encircles society wherever civilisation goes, is caused by the sin of the denial of justice."

Lloyd George had long been a champion of his namesake's ideas for taxing land values. As early as 1891 in a speech at Bangor he had refined his own ideas and was producing practical suggestions which would bear fruit in the 1909 budget. The land monopoly was his prime target. He pointed out that in London alone the land was worth £500,000,000, more than all the municipal debt in the country. That debt had been caused by local government expenditure on such things as waterworks, sanitation, lighting, tramways and roads; an expenditure which created in large measure the wealth the landlords enjoyed. The rest of that wealth was a result of the work, the energy and the enterprise of the people who dwelt in London. He went on to point out that if the great towns had not expended money on public works then this land value would not exist. The landlords had not contributed a penny towards this expenditure but were reaping the rewards.

In a speech in Newcastle he gave examples of the landlords' unearned increments:

> They laid down in Glasgow a system of tramlines and a magnificent system it is; but what is the result? Simply that all the land in the suburbs is going up in value by leaps and bounds. Land worth £500 two or three years ago is worth £5,000 or more this year. The land of Glasgow and its suburbs is going up in value to the extent of £2,000,000, and yet towards all the municipal expenditure entailed the great landlords have not contributed a single penny....

> I was given other figures for Liverpool. I was told that the Lords of Derby and Sefton and Salisbury – that these three noble Lords are in receipt of the sum of £345,000 a year from ground rents in the city. Out of that enormous revenue they do not contribute one penny to the public expenditure on the place.

There was a groundswell of feeling against the landlords that predated Henry George's visit to this country. Ernest Jones, the Chartist, expressed it in a famous speech in 1850:

> I will recite to you a creed. I believe that God gave the land to Adam and his children as an inheritance for ever .... He did not create one Adam, the progenitor of the rich, with a title deed graven on his breast, and another, the father of the poor, with a spade chained to his arm, but he did give a title to the land in these words: "He that will not work, neither shall he eat." And by that title I claim the land for every working man, and by that title I am determined to obtain it.

Asquith, the prime minister, was under pressure to introduce land value taxation. A memorial signed by 250 MPs in November 1908 urged that it should appear in the next budget. A similar petition had been put to Campbell-Bannerman (signed by 400 MPs) in 1906, and in 1907 the United Committee for the Taxation of Land Values was formed and issued some 50,000,000 leaflets during the next three or four years.

It was clear, however, that the Lords would throw out a Bill which sought to value land, which was the sensible way to proceed before taxing it. If the valuation was included in the budget the government stood a chance that the Lords would hesitate to break the convention and not pass a Finance Bill. In the end Lloyd George proposed a modified and somewhat muddled land-taxing proposal which would not have brought in a great deal of revenue.

It alienated the ardent land-taxers who could see that it came nowhere near to Henry George's ideal of a single tax, and it infuriated the landowners who saw it as the thin end of a very nasty wedge.

Budget day was on April 29 and Lloyd George was not on good form. He had laboured long and hard over his preparations and was exhausted. He spoke badly and, having throat trouble, rather quietly. Members shouted to him to speak up and after two hours his voice gave out altogether. At five o'clock an adjournment was called so that he could have a half-hour break to recover.

It was an unfortunate performance, especially in front of a crowded House, with the Peers' gallery, not unnaturally, packed to the brim. He came back and spoke until eight o'clock when he sat down utterly depleted. In all, allowing for the interval, he had been on his feet for four and a half hours.

The fatigue did not last, and the next day he was playing golf at Walton Heath – health fully restored – and doing the first hole in "bogey".

Most of the extra money required was to come from increases in income tax (from 1s to 1s 2d) and on death duties, spirits, tobacco, vehicles and petrol. But, as expected, it was the land taxes that created the uproar although the political economist, Pigou, pointed out they were rather more "taxes on windfalls" than taxes on land.

First, there was a 20% tax on the increment value of land when sold. It would only apply to future appreciation from present-day valuation, which the Chancellor proposed would be made on all land. This valuation was his prime objective for a future, more substantial and coherent tax.

Second was an annual duty of 1/2d in the pound on the capital value of undeveloped land. Agricultural land and parkland to which the public had access was exempted. Third was a mineral duty of 1/2d in the pound. This was subsequently changed to 1s in the pound on the rental value of all rights to work minerals. Fourth was a reversion duty of 10% on any benefit accruing to a lessor from the determination of a lease.

Lloyd George concluded his budget speech with these words:

> This is a War Budget. It is for raising money to wage implacable warfare against poverty and squalidness. I cannot help hoping and believing that before this generation has passed away we shall have advanced a great step towards that good time when poverty, and the wretchedness and human degradation which always follows in its camp, will be as remote to the people of this country as the wolves which once infested its forests.

He could not foresee the Great War that was to make a mockery of all his plans. Nor that when he was Prime Minister after the war he would stand by while his Chancellor of the Exchequer (Austen Chamberlain) repealed his so passionately-fought-for land taxes.

Although it is true that he believed deeply in these new forms of taxes, it is also true that he had a not-very-well-hidden agenda in introducing them. He wanted a fight with the landlords, especially those in the House of Lords. He wanted to break their power.

Before the government had to contend with the Lords it had to get the budget through the Commons. This proved to be a monumental task with 70 parliamentary days of debate spread over six months. The days often turned into nights with sittings going on until six or seven o'clock in the morning. On one occasion Winston Churchill was accused by the Conservatives of attending wearing his pyjamas under other clothing in order to sleep more easily between divisions. This seemed unlikely as he claimed never to wear pyjamas.

There were 554 divisions upon specific points of principle and difference. The opposition used every delaying trick that they could think of, including time-wasting debates on whether or not to continue the debate on late-night sittings. Asquith was forced to drop part of his legislative programme and extend the session into the late summer.

A Budget Protest League was formed, and to counter it a Budget League, with Churchill as its president, was set up to tell the people its advantages. Churchill barnstormed the country making speech after speech in brilliant style. These were hastily compiled and printed in a book, *The People's Rights*, in the last weeks of 1909. It was designed as a guide and armoury for the general election campaign that followed the rejection of the budget in the House of Lords. Most of the speeches in the book were delivered in Lancashire where Churchill made known his views on land in a clear and unequivocal fashion:

> Land differs from all other forms of property. It is quite true that the land monopoly is not the only monopoly which exists, but it is by the far the greatest of monopolies. It is a perpetual monopoly, and is the mother of all other forms of monopoly. It is quite true that unearned increments in land are not the only form of unearned or undeserved profit which individuals are able to secure; but which are not merely not beneficial, but which are positively detrimental to the general public. Land, which is a necessity of human existence, which is the original source of all wealth, which is strictly limited in extent, which is fixed in geographical position – land, I say, differs from all other forms of property in these primary and fundamental conditions.

Mr Balfour opened his attack on the budget in the Commons on May 3. It is obvious from his first remarks that he completely misunderstood, as many others have before

and since, what Henry George was suggesting. The political correspondent of *Punch* describes the scene:

> Prince Arthur [as *Punch* liked to call him] evidently bestowed exceptional pains on the preparation of his speech. Magnificently scornful of what he calls "the electioneering manifesto" that prefaced delivery of Budget speech. To the delight of Opposition drags in Henry George. At first there was a shocked feeling of breach of Order, doubtless inadvertently committed, accompanied by accidental miscalling of Christian names. The name of the Chancellor of the Exchequer just now in everyone's mouth. Had Prince Arthur, not especially notable for accuracy of detail, made a slip and called him Henry? This takes much longer to explain than it did to flash through the minds of Members. The point suggested with studied innocence was quickly seized and greeted with shouts of boisterous laughter.
>
> "Mr Henry George," he continued when silence was restored, "held that the possession of all land was intrinsically robbery, and that it ought to be taken away without compensation to existing owners. That is a fairly coherent system; but what on earth lies at the bottom of the system of Mr Henry George's great namesake?"

If Arthur Balfour could not understand Henry George then he was not going to understand Lloyd George. Punch clearly thought that the Commons were not taking the Budget seriously. Their reporter noted the following day:

> "This is not an ordinary debate," remarked Mr Pretyman, rising to resume discussion in Committee on Budget scheme. "It is one of the most momentous issues ever presented for the consideration of Parliament." Whereupon Members on both sides with one accord strolled out to gossip on the terrace, write letters or read the evening papers. 'Twas ever thus....

Nevertheless, there was considerable opposition in the country from those most affected by the land taxes. The Duke of Beaufort went so far as to suggest that he would "like to see Winston Churchill and Lloyd George in the middle of twenty couples of dog hounds".

Churchill, who was less tied to the House of Commons, made more public speeches than Lloyd George, who was needed to shepherd his budget through Parliament. But the speeches the chancellor made were effective and, indeed, often more virulent

than Churchill's. His vendetta against the landlords was personal, whereas Churchill, who came from an aristocratic background, took a more detached line in his attacks.

One of Lloyd George's most savage speeches was to 4,000 Londoners at the Edinburgh Castle in Limehouse. The Limehouse speech has gone down in history as a masterpiece of invective and set the government on its collision course with the Upper Chamber.

"Slimehouse" was the name the Tories gave it. Delivered on a sweltering hot July evening in 1909 to a rowdy Cockney crowd, who responded with cheers to every other sentence, it attacked the aristocracy in a way that caused the King to complain that Lloyd George was "setting class against class and stirring up the worst passions of his audience."

Lloyd George gave examples to illustrate the need for the new land taxes:

> Take cases like Golders Green and others of a similar kind where the value of land has gone up in the course, perhaps, of a couple of years through a new tramway or a new railway being opened. Golders Green to begin with. A few years ago there was a plot of land there which was sold at £160. Last year I went and opened a tube railway there. What was the result? This year that very piece of land has been sold for £2,100 now – £160 before the railway was opened – before I went there – £2,100 now. My Budget demands 20 per cent of that.

More examples followed and he concluded with a scathing attack on landlords: "Their day of reckoning is at hand." As was to be expected, the speech infuriated the Tories. Sir Edward Carson in a letter to *The Times* said that Lloyd George at Limehouse had "taken off the mask and openly preached a war of the classes, insults to individuals, the satiation of greed, and the excitement of all the passions which rendered possible a momentary triumph of the unscrupulous demagogue."

Undeterred, Lloyd George continued to make fiery speeches. In October at Newcastle he rounded on a favourite enemy – the dukes: "a fully equipped duke costs as much to keep up as two Dreadnoughts, and they are just as great a terror, and they last longer".

Punch had charted the progress of the budget through the Commons in some detail, although at times it summarised affairs in brief notes that echoed the public's weariness with the long-drawn-out affair:

May 10	1909 Committee sat up late with Budget Resolutions.
May 11	Commons sitting till a quarter past two this morning, again pegging away at the Budget.
June 8	Still droning round the Budget.
June 21	In a rage and Committee on Finance Bill.
June 29	Worry away at Budget Bill.
June 30	Clause 1 of Budget Bill passed with trifling amendments.
July 12	Commons still harping on Clause 2 of Budget Bill.
July 19	Up all night with Budget Bill.
August 19	Sitting eighteen hours, Committee nearly finished Part 1 of Budget Bill dealing with Taxation of Land.
September 27	Thirty-fifth sitting in Committee on Budget Bill. Members in almost comatose state.
October 5	In Committee on Budget Bill. Land in sight.

By November it was all over. As expected, the Lords then rejected the budget by 350 to 75. The "Peers versus the People" general election followed in short order.

The peers, since their very existence was under threat, took part in the 1910 general election with some gusto. It was the first time that they had been allowed to do so, and then only by virtue of an amendment of the House of Commons' Standing Orders on Privilege.

Lansdowne took the line that the Liberals were stirring up class hatred while Curzon defended the hereditary principle using the French historian Ernest Renan's observation that all civilisations had been the work of aristocracies.

Churchill, in opposing, went tub-thumping round the country in his usual sparkling style. Often he would lead the singing of the Land Song, thousands of sheets of which had been distributed in a mass demonstration in Parliament Square by a Captain Hemphill. It was sung to the rousing tune of *Marching Through Georgia*:

The Land! The Land! 'Twas God who gave the Land!
The Land! The Land! The ground on which we stand!
Why should we be beggars, with the ballot in our hand!
God gave the Land to the People!

Punch came up with its own version which it suggested should be sung to the air *Marching through Lloyd-Georgia*:

The land! The land! 'Twas Lloyd that pinched the Land!
The land! The land! – Don't get behind the band!
With the Ballot in his eye and the Budget in his hand.
Lloyd pinched the land for the People!

As ever, the press were more enthusiastic, not to say hysterical, about events than either politicians or public, as *Punch* pointed out in a little guide to the actual meaning of some of the more dramatic headlines:

Phrase	*Exactitude*
The Lords Declare Civil War	The Peers prefer to let the nation decide on a measure
The Enemy	Fellow-subjects who don't happen to agree with you politically
The People	Fellow-subjects who do, to the exclusion of all others
Forcing a Revolution	Spoiling the Christmas holidays with a General Election

The Liberals won the election with a reduced majority but were still outgunned by the House of Lords. However, the rejected People's Budget was reintroduced to the Commons, passed and returned to the Upper Chamber. The Lords let it through without a division and it passed through all its stages within a few hours. On April 29 it received the Royal Assent, one year to the day after it had first been introduced.

The land taxes, badly drafted and never fully implemented because of the start of the First World War, were repealed in the 1920s. What is needed now is a new land value taxation budget and a government with the will to put it through.

Fiscal and Banking Policy: A Double Dilemma

by Brian Hodgkinson

The problems that confront the British economy threaten a greater disaster than even the prolonged depression of the 1930s. For who can say that Britain will improve on the sad performance of Japan in the twenty years since 1990? Like Japan, we have suffered primarily not from a nebulous "global crisis" – as the Labour government so frequently told us – but from a grossly excessive asset price bubble, consisting principally of enormously inflated land values to which great volumes of debt were attached. It does not change the analysis to add that some of this debt was imported from the USA.

We face a double dilemma. The first is fiscal and therefore governmental; the second is monetary and mainly concerns the private financial sector, especially banks. Much political debate continues to focus on the fiscal dilemma. In short, it consists of an apparent choice between recession on one hand, and a sovereign debt crisis on the other. Political conservatives and free marketers favour taking a risk with recession, whilst left-wing and social democratic critics prefer to defy the bond market and risk a Greek-style collapse of British government securities. It is a horrible choice. Are we to see unemployment rise to over three million in order to satisfy the international bond market, or are we to fall into the draconian hands of the IMF when our government debt becomes B-rated or lower?

Those who are prepared to risk a double dip recession – which more or less includes George Osborne and the Coalition government in general – will have welcomed the emergency budget presented in June 2010 which was based on a policy of drastic cuts in expenditure and modest increases in taxes. After ring-fencing health expenditure, other departments were told to find 25% reductions within five years. Even the figure of 40% was mooted by the Treasury. Total public expenditure would fall from about 47% of GDP to below 41%. This was expected to involve large falls in public employment, which would especially hit areas like the North and Wales where the government is a relatively large employer. Welfare cuts would have a similarly differential regional impact. There would also be a large knock-on effect on the private sector, as government orders were cancelled.

Liberal Democrats were, of course, unhappy about this. The most significant tax rises were a 20% rate of VAT from January 2011, a capital gains tax rate of 28% on higher incomes and a bank levy of £2bn. Corporation tax would be reduced and personal

allowances raised by £1,000. Some relief was given on national insurance to firms in the regions. The total deficit reduction by 2014-15 was expected to be £113bn.

Anyone who still gives some credence to Keynes and his famous multiplier effect must believe that such a massive and rapid reduction in the government's impact on the economy will be detrimental. Public capital expenditure will be cut by over 50%, which amounts to 1.5% of GDP. Jobs, public procurement, local services, education, welfare and so on will all feel the effects. But, say the optimists, the private sector will revive to take up the slack created. Entrepreneurs will appear, even in the economic war-zones of the regional fringes, to provide growth, exports and, above all, employment. The question is: "Why should they?" What will make them believe that they have expanding markets and lower costs? Export markets are going to be subjected to fierce competition from other countries with similar problems, many of which – including those in the Eurozone – may allow their exchange rates to fall dramatically. Only the miserable prospect of growing unemployment forcing wages down may console British entrepreneurs! The tax and national insurance concessions are minimal. Is all this pain really being inflicted to buy off a handful of dealers in government bonds, many of whom are the very banks that were largely responsible for the crisis in the first place?

The other side of the dilemma is simpler. If the fiscal deficit is allowed to continue anywhere near its present rate of £180bn a year, or about 11% of GDP, total public debt will become unmanageable – both because the service charge would be enormous and, more strikingly, because buyers of government bonds would surely cease to be interested. The credit rating would collapse, and perhaps very soon the British economy would be taken to the pawnbroker of the IMF. It would be 1931 all over again on a much bigger scale.

In principle, there is only one long-lasting solution to this awful dilemma. Somehow the fiscal deficit has to be greatly reduced without massive cuts in expenditure or greater deleterious taxation. Logically, this leaves only one course open – to raise revenue in some way that does not hit production. Virtually all existing taxes – VAT, income tax, corporations tax, capital gains tax, excise duties, national insurance and so on – all deter producers, especially at the margin. And the margin consists of both producers in unfavourable locations and the last workers and resources taken on by a firm, i.e. the marginal output of any firm. Taxes on output, whether levied on labour, capital or sales, deter firms from producing more. At the margin they cannot bear the taxation. This is elementary economics.

There is, of course, one form of tax that has no such impact, namely a tax on economic rent or the annual value of land. Economic rent is the surplus that arises on any site

owing to its location and natural resources. This value is created in three ways: by natural endowment, such as fertility or mineral wealth; by the presence of the surrounding community that provides markets, labour and much else; and by the effect of public services and utilities that enhance the land value by providing transport, water, power, education, law and order, refuse collection and the rest. The moral case for collecting economic rent rests largely upon recognition that these three causes are in no way provided by the occupant or owner of the site concerned. Thus there is no case at all for appropriation of the economic rent by the tenant or freeholder.

Here we are more concerned with the economic case. There are very strong pragmatic reasons for advocating the taxation of economic rent. The tax cannot be avoided. It also helps to redistribute income and wealth. The supply of land is not diminished; indeed it is enhanced by stimulating landowners to put land to its best use. But at the present time of crisis the greatest emphasis should be put on the dire necessity to find government revenue that does not adversely impact on production. A tax on the annual land value does not affect a firm's decision to produce and invest by one iota. For the land value remains the same whatever output and investment takes place. It is determined solely by the three external factors mentioned above.

The introduction of a land value tax would enable other taxes to be reduced. Perhaps at the present time the reduction would have to be gradual, but productive resources would be released with every pound of existing taxes that were cut. Ask any genuine entrepreneur what he would do if taxes on labour, capital and so on were reduced without any corresponding rise in taxes on his output! Only the unproductive holder of land would bear the new tax. He could not move the land to avoid the tax; nor could he close the site down without having to bear the tax on the unused land.

What Michael Hudson has written about eastern Europe could be applied word for word to the condition of the British economy:

> The main issue in eastern Europe and beyond over the coming years will be whether economies can free themselves from the twin burdens of heavily taxed wages and inflated housing prices, while avoiding an overdose of needless austerity. The clear alternative is a reformed system that focuses on taxing the rising land values created by general prosperity, or economic rent. It is worth remembering that taxing the 'free lunch' of rising land values was part of the original liberalism of Adam Smith, John Stuart Mill and the Progressive Era reformers in the US, all of whom sought to make their economies more competitive. Today, tax reform is

> again the best option to help countries around the world regain their competitiveness.
>
> *Financial Times*, 7 July, 2010

Such a solution has the extra merit of dealing with the regional problem created by the present fiscal policy. Marginal areas of Britain, and marginal sites within all areas, would pay much less tax. Areas and sites of high economic rent, like central London or opulent high streets, would pay more – but not on their production, which could continue to be very profitable. At last there would be a natural balance of employment and investment around the country. This would not be a case of taxing the more efficient firms and industries. Efficiency is a matter of the best use of land, labour, capital and technology. Taxing the surplus – the economic rent – has no impact on efficiency whatsoever. Indeed it encourages it by rewarding efficient producers with the full untaxed value of their contribution.

Unlikely support for this policy of dealing with the fiscal deficit comes from a recent editorial in the *Financial Times* about the Australian mining industry: "The purpose of resource taxation is to capture for the nation the 'economic rent' of its natural resources". It does not go on to say that all land constitutes every nation's natural resource, but it does take the vital step of distinguishing between the value of output produced by labour and capital and the value created by the land itself, i.e. its rent. Where better to implement this principle than in the British economy at this time of need? A recent estimate of the total capital value of land in Britain is £5 trillion. Tax should not be levied on the capital value, since the latter would diminish with every increase in the tax. Taxing the annual value or rent, however, leaves the capital value intact. Clearly there is a huge potential revenue resource immediately available.

What then of the second dilemma? On the one hand, banks are berated for having lent excessively and without discrimination. On the other hand, they are being told to lend more to get the economy moving again. Should they risk a similar crisis in a few years' time, or should they stifle the economy by withholding funds? The problem appears to be about banking reform. Much has been said about institutional changes: the setting up of new regulatory regimes, reinstating control by the Bank of England, abolishing or strengthening the Financial Services Authority, and so on. Why is regulation – previously shunned by those who wanted to make a bonfire of all controls on the so-called "free market" – now welcomed on all sides? The reason, of course, is that the banks grossly abused their freedom by lending to all and sundry wherever they thought that asset appreciation would carry on without limit.

When the inevitable crisis came, the banks went into reverse and stopped lending, even to each other. Quantitative easing to the extent of £200bn has given them a new liquidity. Their capital requirements have been strengthened. Yet they are still not lending sufficiently to industry. Perhaps nothing short of full nationalisation will make them do so.

All this, however, fails to get to the root of the banking problem. One simple fact gets overlooked. The banks create money. Bankers themselves seem to think that they merely re-lend money. Textbooks assert that banks "borrow short and lend long". Where do they think the money comes from in the first place? All agree that almost all money – about 97% – consists of bank deposits. Cash in the form of coins and notes are the small change of the system, although it may become critical in a banking crisis. So who generates the 97%? Obviously the banks create it when they give overdrafts or loans. Someone gets a facility to draw cheques without having a positive balance to draw against. When the cheques are honoured the payees deposit them in a bank, thus creating bank deposits – which are bank money. Hence the whole process begins with the granting by a bank of the right to draw cheques.

The reason for the ubiquitous and dangerous myth that banks simply re-lend money is that a prudent bank relates the extension of its overdrafts and loans to the amount of its deposits. If it gives too many overdrafts, for example, it may become heavily indebted to other banks at the bank clearing, because its deposits may be inadequate. But the fact that all banks may be prudent, and that as a result bank lending is always kept in line with deposits, does not change the brute fact that the money is created by the banks. If it were not, where would the deposits, i.e. bank money, come from?

From this forgotten but fundamental point arises the key to solving the banking crisis. For if the banks can create money at will, then they have freedom of choice as to whom they lend. The question becomes, not just what regulation should be placed on total bank lending, but which lending should be regulated – or even prohibited – and which lending should the banks be free to extend? The answer is equally simple. Productive lending should be allowed; non-productive lending should be controlled. Why? Because productive lending yields output that matches the money created. It would include short-term loans for working capital and longer-term loans for capital investment in equipment, machinery, technology, etc.

Non-productive lending, on the other hand, yields no output at all. All that it does is to push up the price of the assets that are purchased with the money created. For example, lending for the purchase of buying bonds or shares simply raises their price, for there is no greater supply of the assets. There is just greater demand for the existing

supply. Similarly, lending to finance consumer spending raises demand for consumer goods without creating any more productive capacity. In the short term it may stimulate output if there is unemployment or spare capacity, but in the long term it leads to a consumer debt crisis of the type we have witnessed recently. But the most virulent form of non-productive bank lending is that which finances the purchase of land. For land is in fixed supply. Some land, of course, is withheld from the market, and may be sold if demand rises. This, however, only modifies the general tendency for land prices to rise if money is created for its purchase.

Excessive lending for the purchase of land has not been ignored by financial analysts, such as Conrad Voldstrad:

> Have we addressed what actually happened in the financial crisis? Or have we left the real culprit lurking, ready to resurface and create more instability in the financial system? It is clear today – and it was clear three years ago – that the culprit is real estate exposure … the investment bank industry was feeding at the trough of the real estate lending boom.

Financial Times, 7 July, 2010

Some banks, like RBS, are shedding their property debt on a large scale at the present time. But are they truly repentant? When the land market starts to revive, as it will whenever the economy shows any real sign of growth prospects, they will revert to their old ways of "seizing the day".

Yet to get rid of all non-productive bank lending in the British economy at the present time is a hopeless ideal. Lending for stock market speculation could perhaps be reduced, but there is clearly no sharp line between that and genuine investment in risky projects. Consumers will need time to change their habit of buying first and earning later. And, above all, the purchase of land underlies the markets for both business investment and private house purchase.

Yet there are solutions. Banks can be given guidelines on lending. These could be enforced, if necessary, by re-introducing Bank of England or FSA controls on liquidity, capital requirements and so on. Building societies could be resurrected to take over all lending for private mortgages. Unlike banks, they did not have the power to create money. Their lending was entirely financed by deposits; hence it came out of saving, and did not have the same impact on land prices.

These proposals together would have a substantial effect on cutting non-productive lending. But there remains one vital piece in the double dilemma scenario. The two dilemmas are crucially interrelated. The rise in land prices that fuelled the so-called "global crisis" was caused primarily by uncontrolled creation of money by the banks for the purchase of commercial and housing land. ("House" prices, of course, include land prices.) A tax on the annual value of land not only helps to solve the fiscal dilemma; at the same time, it brings down the capital value of land. Provided that such a tax were introduced gradually, it would eliminate much of the speculative element in land purchases, and put an end to asset bubbles based on land values. As Philippe Legrain wrote in *The Times* recently:

> The notion that we can all get rich by swapping more or less the same stock of houses at ever more inflated prices is a dangerous delusion. Property speculation diverts funds from productive investment in promising companies – and when the bubble bursts, the economy plunges into recession, home-owners are stranded with huge debts and banks laid low by bad loans seek bailouts from taxpayers.

The Times, 16 June, 2010

Land value bubbles are the mother of all asset bubbles, since other assets are limited to narrow markets (like dot-com shares), whereas all business and housing enterprise is literally built on land. Hence a secular policy of permanently reducing land values would put the whole economy on a sound basis.

So the bad news that the British economy faces a double dilemma may be turned into the good news that there is one fundamental solution to both dilemmas! Policy to implement it would require very careful timing, and the accompaniment of sound measures on bank regulation. Moreover, statesmanship would be needed to ensure that short-term fears about, for example, negative equity in the housing market or a fall in consumer demand did not outweigh a long-term view of what is essential. At least the Coalition government offers the opportunity for wise advice from the Liberal Democrats!

LVT and Transport

by John Howell

Effect of transport links on land value

In East London, as the new rail link from Dalston Junction to West Croydon nears completion, house prices along the route are already rising. In March 2010, *The Times* reported a Croydon estate agent as saying:

> People are already talking about the extension [from Dalston] because it will have an impact on prices. It will make a psychological difference for the 300,000 residents of Croydon to be on the Tube map. There could be a migration of City workers to West Croydon … and a new development of 330 apartments has sold right away.

In April, the "High Speed 2" rail network, planned for 2026 and intended to link London and Birmingham in a mere 49 minutes, was announced. Again, *The Times* commented:

> Homeowners along the route have cause to celebrate. Research by Savills shows that a one-minute reduction to a commuter rail journey adds £1,000 to the price of an average home.

Time and again, locations are seen to become more valuable as a direct result of improvements in transport infrastructure. Farmers and manufacturers benefit from quicker and wider access to markets, and commuters gain from reduced journey-to-work times. Improved transport increases the total of goods and services available to a location and this always feeds through to an increase in its site value. Were these increases tapped into by LVT, existing and new transport links would become more or less self-financing.

The income of any transport system will come from its fares or tolls. At best these will only cover running costs. So where to find the immense capital outlay for tunnels, track, bridges, motorway intersections, land purchase, etc? There have been past instances of transport schemes which were paid for, at least initially, out of the land value that they had helped to enhance. These days this does not happen and, in spite of the indispensable role transport plays in the health of the economy, most of the transport infrastructure is said to be unprofitable, only kept alive by grudging subsidies from public funds, and rarely sufficient to meet the demands placed on it.

Lessons from London's Underground system

In 1900 the tube network under central London was gradually being built. But despite the obvious relief it would bring to the overcrowded streets above, most schemes were in financial straits. The partly-constructed Bakerloo Line had gone bust, the District Line was in difficulties, and a proposed line to Hampstead had no investors.

The problem then, as now, was that the revenue from fares was mostly absorbed by running costs, and left little to cover the immense initial capital outlay on tunnels, rolling stock and stations. Fortunately, a rather shady financier from Chicago – one Charles Yerkes – managed to persuade American investors there was money to be made out of London's commuters, and by 1907 the lines were completed.

American transport promoters like Yerkes had become adept at making their schemes pay by building well out beyond city boundaries so as to make a killing on increased land prices when housing sprang up around the passenger stops. Yerkes, spotting the potential for this in the undeveloped fields north of Hampstead, extended his North London Line out to them, and doubtless it was the ensuing land deals that enabled him to succeed where previous English tube entrepreneurs had not.

The idea of raising the otherwise daunting initial capital cost of urban railways by tapping into the increased land values they created was clearly recognised by Frank Pick, vice-chairman of London Passenger Transport Board – the public monopoly that had taken over the running of London's tubes, trams and buses in the 1930s. In evidence to the Barlow Commission (1939) he stated:

> The moment an underground extension is projected, the value of the land is at least doubled. When the railway is built and the stations opened the land adjacent is at least quadrupled in value. In view of the difficulty of maintaining a public utility like the London Passenger Transport Board in a satisfactory condition from (only) the receipts of fares, there is every reason, in the interests of the public, why the Board should receive its appropriate share of the land values it helps to create. The earnings of a tube railway (from fares alone), even under favourable circumstances, are not sufficient to provide the interest and the sinking fund upon the capital invested.

Quoted in *Underground to Everywhere*, S. Halliday, 2001

The only other early instance of increased land values being systematically recaptured to finance capital costs was the Metropolitan Line in northwest London. Before 1900, because it used steam trains, it had been forced to buy far more land than it needed for the tracks, and sometimes made useful profits by selling this land later.

By the 1920s it was financing new line-building by deliberately buying agricultural land to the north of London, and capitalising on its increased value when the lines were finished. Consequently, the Metropolitan Line was regarded by many as the best in London. Sadly, Pick's hope that this model would be applied to the rest of the network was not to be fulfilled. His evidence to the Barlow Commission continued:

> This potentially valuable source of railway finance was again not taken up. Profits from property development would only go to property developers. The benefit to railways would be confined to the extra journeys of those who travelled from the properties.

[*Ibid*]

Lessons from London's Jubilee Line Extension (JLE)

In 1989, the Jubilee Line needed extending to East London where developers hoped to build Canary Wharf – a new financial centre to rival the City of London. Meanwhile, the idea of tapping enhanced land values to pay for new transport links had resurfaced, and Paul Channon, transport minister to Mrs Thatcher, declared:

> If there is to be new transport investment in London, the passengers who benefit from it should meet its cost through the fares they pay, rather than be subsidised by taxpayers in the rest of the country … and contributions should also be forthcoming from property owners and developers who stand to gain from the transport improvements.

Consultants advising the government agreed:

> …any new line should be paid for by those who benefit including passengers, property developers, and landowners … In the case of the Jubilee Line Extension, we understand that the Department of Transport has been advised the benefits which the line would bring to the property developers are likely to exceed by a considerable margin the cost of the line, and that a Government contribution to funding would appear not to be needed.

Halcrow Fox & Associates, *East London Rail Study Report*, 1989

Canary Wharf's developers knew that the accessibility provided by a proper tube line would earn them an extra £320 million a year in rents. They therefore willingly contributed £100 million to the line's building costs, and as part of the deal insisted that other developers whose sites benefited from the line were also charged one-off "planning gain" payments of about £20 per square foot when their developments went ahead.

Nevertheless, the bulk of the JLE's £3.4 billion cost fell, as usual, on taxpayers throughout the United Kingdom who felt no benefit. To the Treasury and London Transport it appeared that the JLE was adding to an existing large network, and that benefits to landowners were not concentrated in such a way as to form "an easily identifiable tax base." Of course LVT would have done just that.

Just supposing the mechanism of LVT had been available to fund the JLE, would its revenue have been sufficient? In *Taken for a Ride* (2001), Don Riley, a Southwark property owner, used his extensive local knowledge to document the scale of property rent and capital value increases that occurred once the JLE was up and running by 1999.

He conservatively estimated that, within a 1,000-yard radius of each new station on the line, values rose by £1.3 billion, so for the ten stations along the line the overall gain was of the order of £13 billion – nearly four times the total construction cost. Riley suggested that if that gain were annualised into a 10% return, and taxed at 25%, it would yield £325 million a year to the exchequer and pay off the line cost in 10 years.

In March 2004, a report commissioned by Transport for London estimated the "JLE uplift" of land values was £2 billion around Canary Wharf station, and £800 million round Southwark station – figures of similar magnitude to Riley's, who commented:

> I was impressed by the magnitude of the increase in land values. It seemed obvious that the Jubilee Line [Extension] could have been constructed without the aid of subsidies from taxpayers who live in the deprived regions of Humberside and Merseyside. I was particularly annoyed that rich financial institutions in the City – 20% of which were foreign owned – would benefit from similar investment. The City was calling upon taxpayers, to an important extent, to improve the transport infrastructure for their benefit.

Applying LVT properly

However, even in the Hampstead, Metropolitan and JLE examples, the LVT principle was only partially followed. Effectively, in these cases, site value increases were tapped on a "once-only" basis, which contributed only to the initial construction costs. There was no provision for the major recapitalisations that would sooner or later be needed to adapt to new technologies or changed patterns of demand. Unless contributions from site values are ongoing, a lack of capital funding will haunt future generations.

Also flawed is the developer's "planning gain" payments system, instituted when the JLE was built, because it misses the vital fact that new lines enhance values of all sites with development potential, even if they are not developed. Site owners who choose not to develop still benefit from a transport upgrade without having to contribute to it.

Perhaps this explains why, even after the boost from the JLE, Southwark and Bermondsey still have many underdeveloped sites. By applying to sites, rather than the improvements on them, LVT stimulates development and discourages inactivity.

Finally, it cannot be repeated too often that LVT is meant to replace other taxes, not supplement them. LVT stops the land value created by local transport improvements leaking away to those who have not paid for them. With revenue from this new source, taxes on labour and expertise could be phased out, allowing more jobs to be created, and the general level of earnings to rise. This would also reduce capital and running costs of transport networks and many more schemes would appear to offer "value for money" than at present. Ventures such as London's Crossrail, the East Coast high speed link, and efficient freight services to take pressure off roads and cut pollution would all become viable.

LVT and funding roads

As road technology improves, so does access within and between urban areas, giving sites new potential and greater value. As with railways, the funding of road building is mostly based on flawed principles. Why should motorists in remote areas, far from any motorway or at the farthest extremity of their local road network, pay the same road fund tax as those conveniently placed near crucial motorway junctions?

Again, is it sensible for remote producers, who use more fuel in reaching their markets, to pay the same rates of fuel tax as everyone else? Won't such taxes encourage the undesirable overconcentration of production and people in core areas?

Road developments benefit users, but also site owners. Both need to contribute in proportion to either their level of use or site benefit. Generally, benefits accruing to site owners are not tapped, and the main burden falls on users.

How roads affect site value

As any major urban area grew, faster means of transport (cars, lorries, trams and buses) reduced the time and cost of travel for commuters or freight and increased the distances they could travel. This improved the residential/commercial potential and site value of land at the urban fringe because access to employment or markets in the central zones was improved. Similarly, along motorways between conurbations, land values along the route, especially near access points, would rise sharply because of shorter journeys to hubs of employment or business opportunity. In his *Economic Analysis for Highways* (1960), R. Winfrey states:

> …because of travel time reduction, and because of a reduction in motor vehicle running cost ... landowners (i.e. developers) can afford and do pay higher prices for the land than the current price of land before the construction of the new highway. Thus this higher price reflects the greater productivity of the land in its new use.

Site value usually ignored

Winfrey estimated that the net benefits accruing as a result of a new highway could lead to land prices increasing between 100 and 1,000 percent, but also noted this was ignored in the cost/benefits analysis of new schemes:

> …landowners may reap sizeable windfalls from selling their land at these high prices brought on by the highway improvement. To such landowners their gains are unearned. [However] land-value changes are not part of the … economic evaluation … of highway improvements.

[*Ibid*]

Failure to tap site values means that road improvements are underfunded. A particular irony in suburban areas was that road widening was often penalised by having to acquire land at prices enhanced by the very improvements of access they had created. The notion of tapping into site value did occasionally appear, sometimes a little distorted, as the following passage from the Liberal MP Hilaire Belloc shows:

> The grant of new roads should include the purchase, if not of a continuous belt along each side, at least of blocks of land, especially in the neighbourhood of existing communications, near railway stations, near villages or other centres to be established, etc. the price to be determined by … the old price basis before the scheme of the road was developed. If this were done … the [enhanced value] of … these sites would accrue to the public purse and would gradually relieve the cost of construction … Without such a funding model, the nation would make a direct and immediate present of millions to chance owners of land upon their trajectory.

H. Belloc, *The Road*, 1923

Belloc's idea of road builders buying open land at pre-road development prices and recouping enhanced values later by selling the land for housing, has the same "one-off payment" weakness of the planning gain charges mentioned earlier.

Funding roads from users

The other natural source of road funding would be users – motorists, haulage firms, bus companies, etc. One might expect them to bear the "running costs" of roads – lighting, signage, repairs, policing, etc – while the capital cost of construction and periodic major improvements was charged to LVT. But the proportions in which road costs should be split between users and LVT really needs further study. Should the capital and running costs of a motorway be borne by a proportion of LVT in the towns it serves, or from tolls levied on users? There is obviously a case for both.

Tolls are fairly easy to collect manually in limited access situations like motorways, bridges and tunnels. In the more complex urban and suburban networks one would need sophisticated electronic road pricing schemes, with different zones charging different rates according to demand or the need to limit congestion. Although road pricing suffers a bad press because of its "Big Brother" image, it would in fact replace other taxes which already require much prying by the state into our lives.

Moreover, if users are not charged effectively for the road space they use, the savings they make will be transferred to site values. Although this could be recouped, site-taxing would not regulate problems like congestion as directly as road pricing.

LVT applied to airports and aviation

In order to land or take off from airports, airlines buy "landing slots" from the airport owners, such as the British Airport Authority. Being relatively limited in number, the value of these slots has surged with increases in air traffic. Like land, the skies are a public asset, so the charges for landing slots which give access to them might reasonably be regarded as public income.

Unfortunately, ownership of the landing slots has fallen mainly into the hands of the airlines, so privatising this valuable public resource, and distorting the natural funding of aviation.

Through being unable to charge full market rents for the right to use their runways, airports can only be profitable by building shopping malls and renting out retail space. The lack of a proper auction market for the valuable landing slots leads to constant lobbying and intrigue for them by airlines. Sometimes, they will fly near-empty planes to keep control of slots, leading to overcapacity. The lack of real competition allows inefficiencies and inflated costs to develop – ultimately passed to passengers, the environment, or the taxpayer.

There is growing agreement in political circles that landing slots represent a valuable, justifiable and sustainable source of public revenue. Landing slots at Heathrow alone are said to be worth £5bn a year. A free market in slots should be established by periodic auctions. Revenue from them needs to be shared between (i) the airport authority – to develop new runways, etc, (ii) local authorities – to mitigate the effects of noise and air pollution, and maintain neighbouring transport infrastructure, and (iii) government – to pay for air safety, immigration and customs. With landing slots valued by regular auctions, and airlines charged accordingly, the users of overcrowded airports like Heathrow would become more aware of their real environmental impact and seek alternatives. Meanwhile, the capital costs of new airports could be properly funded.

Conclusion

In the Industrial Revolution, big landowners wanting to develop their resources or tap into markets used their rents to construct turnpike roads, canals and sometimes railways, and covered running costs by tolls or fares from users. It was a sustainable model. It required no state funding, yet produced and maintained transport facilities when and where required.

What went wrong? Most of the early schemes always looked profitable, so landlords were tempted to sell them on to investors who failed to notice that from then on the scheme would no longer be funded by the landowner's rents, but the savings from ordinary people's earnings. It was also not noticed that benefits the scheme brought to any area would leak away as rents to landowners rather than profit the scheme and its shareholders.

This was not a sustainable model, because it was hard to build the reserves needed when major upgrading and re-investment of schemes became necessary. These now had to be met by taking on debt repaid from future earnings, and the effects of that are today all too evident.

LVT offers a way of bringing the sustainable model up to date. At present, there is chronic underinvestment in the UK's transport infrastructure, and the economy suffers as a result. By LVT funding, our railways could be made cheap and fast enough to attract long-distance passengers and freight from the motorways, which would also reduce pollution. Economic life in outlying parts of the country would revive because of their improved accessibility. Population could then decentralise from the major conurbations to smaller settlements where wasteful and polluting journey-to-work travel was reduced.

At present, transport is funded partly by fares and freight charges and partly by taxation levied on labour, enterprise and production. Taxes raised in this way discourage employment. They also make many marginal locations uneconomic. These two factors combine to make the cost/benefit assessment of many new transport projects seem unfavourable. The project's cost is increased by the damage that taxes to fund it will cause to the rest of the economy, and its benefits seem limited by the apparent lack of potential in outlying areas. Hence government is reluctant to invest, and expects users to meet an unfair proportion of transport costs.

Under LVT, transport funding would fall precisely on those who benefited, and it would be easy to raise the capital sums for construction and long-term upgrading that projects need.

Business and Enterprise

by Catherine & Brian Hodgkinson

Structure of industry and commerce

The structure of industry and commerce has changed enormously over the last one hundred years. In 1909, Britain was still the greatest manufacturing nation in the world, and yet, unlike today when "size" is regarded as the leading indicator of a company's efficiency and ability to compete in global markets, companies were much smaller and often owned and run by individual entrepreneurs with some expertise in the production process. Today, most of our largest enterprises are owned by absentee shareholders and run by "management experts" who know little of the production process and are thought to be able to manage factories, shops and banks equally well.

There has, of course, also been a huge transformation in the UK economy, as it has moved – especially since World War Two – from manufacturing to service industries. Over the years many economists have argued that this transition was almost inevitable because we were unable to compete internationally in manufacturing (except in a very limited number of fields such as defence equipment and pharmaceuticals). The theory that the UK's role is in the service industries, especially financial services with our international reputation through the City and Lloyds of London (with our central position in the international time zones also viewed as a favourable factor), has gained much credence. Successive governments, particularly from the Thatcher era onwards, have looked increasingly to the financial services sector to generate the UK's wealth, and have done little to prevent the resulting imbalances in the overall national economy or the disparities in regional wealth.

The emphasis on services has brought enormous changes to both the structure of our economy and to land use. Many of the old industrial heartlands, which were the power house of the UK a century ago, have seen their "raisons d'etre" disappear. The coal mines have gone from the Rhondda and Barnsley, the steelworks from Sheffield and Ebbw Vale (where the site of the ironworks is now – you've guessed it! – a shopping centre), the shipyards from Tyneside and Clydeside, the cotton mills from Bury and Rochdale, and the woollen mills from Huddersfield and Halifax. Many workers, both skilled and unskilled, found themselves without the jobs that had been frequently inherited from fathers and grandfathers. Governments have sought to ameliorate the conditions in these depressed areas by giving investment incentives to "light" industry,

often bringing in overseas investors – a dispiriting reflection on our own inability to finance industry.

The changes wrought over the last fifty years to the old heavy industrial areas of the UK are poignantly summed up by former South Wales miner Max Boyce in his song "Duw, It's Hard":

> In our little valley
> They closed the colliery down,
> And the pithead baths is a supermarket now...
> They came down here from England
> Because our output's low.
> Briefcases full of bank clerks
> That had never been below…

And the solution? The beginning of the final verse says it all:

> But I know the local magistrate,
> She's got a job for me,
> Though it's only counting buttons
> In a local factory.

Why has manufacturing declined?

The decline in our manufacturing base has not occurred just in the traditional regions of heavy industry a long way from London. It has happened all over the Midlands and the South East and in a very wide range of industries. Need it have been like this? Are the reasons for the decline to be attributed to international competition and to pricing ourselves out of world markets because our wages were too high and our productivity too low?

There is an alternative explanation. Failure to address the problem of rising land costs in the UK over many years has been a major factor in our industrial decline. Land costs in the UK are among the highest in the world, because we have a relatively small land area and heavy concentrations of urban population. This strongly affects manufacturing industry in places like London, the West Midlands and the North West.

What are the consequences? Firstly, manufacturers pay high rents under leases or high interest charges if they have purchased a freehold site. These costs must be recouped in higher prices for final products. Secondly, employees incur high housing

costs in urban areas, which force up their wages and thus also enter into final prices. If workers react by commuting long distances, this also becomes a cost, both directly in wage bills, or indirectly in terms of workers' dissatisfaction and lower productivity.

In addition to these high land costs, British manufacturers face an equally damaging condition in a taxation system that strikes at the crucial margin of production. This margin has two forms, as David Ricardo clearly explained two centuries ago. On the one hand, there is the extensive margin, consisting of the firms – usually small and often with the potential for growth – that operate on inferior sites and hence have lower labour and capital productivity. On the other hand, all firms – including the largest and best-located – employ labour and capital up to the point where their marginal output falls off and becomes uneconomic. This is the intensive margin. Taxes such as income tax, national insurance and corporation tax hit both kinds of margin, since they are levied equally on all employment, regardless of whether it is marginal or not.

The higher output of non-marginal labour and capital is not due to efficiency. It is due to superior location. In short, the value of the higher output is rent. Our present tax system ignores this crucial differential. The nearest we have come to recognising it was the crude regional employment tax of Harold Wilson, which could not deal with differentials of rent within regions.

So manufacturing industry has declined in the UK primarily for two reasons: high land costs and inequitable taxation. Evidence of these causes of decline has been graphic. In the Midlands, manufacturing firms closed down and sold their sites to property developers. Sometimes valuable sites have simply been left vacant, whilst the owners – untroubled by any taxation on empty and unproductive sites – have waited for the land price to rise to make a speculative profit. A striking example occurred in Reading, which in 1909 was known as "biscuit town" – the home of Huntley and Palmers, the largest biscuit manufacturer in the world and truly a global supplier. Production ended there in 1976 and the town's economy is now largely based on insurance and other financial services. Huntley and Palmers had a central site, and no doubt its price soared to such a level that the case for redeveloping the site for other seemingly more productive purposes was compelling.

Monopoly and oligopoly

Since 1909 there has been an increasing concentration of industry and commerce in a small number of hands, some of it obvious as in the supermarket brands of Tesco and Sainsbury, some well hidden from the public by the use of a variety of brand

names owned by one corporation. For many years, for example, shoe shops in the UK's high streets traded under a variety of names but were almost all owned by The British Shoe Corporation. Today, a woman can walk through any shopping centre and purchase clothing from Top Shop, Wallis and Evans, Dorothy Perkins and Miss Selfridge without being aware that she is buying from the same company – the Arcadia Group, owned by Philip Green (who lives, of course, in Monaco).

Monopoly and oligopoly are almost always unjustifiable. Only in the cases of natural monopoly and the rare instances of much greater efficiency residing in one or in a few firms can it be defended. Usually it is the consequence, like the developments referred to above, of the UK systems of land tenure and taxation. As Winston Churchill said in 1909, land monopoly is the mother of all monopolies. It still is today. A retailer owning a central site makes large "profits". These in reality are rent – not profits of work, capital or enterprise, but of location. If this is doubted, let all such retailers pay a full economic rent for their site and see what "profits" remain!

Whilst High Street retailers grow fat on rents, those on inferior sites suffer the same level of tax. Such marginal producers are forced to pay income tax and other taxes levied on production – i.e. on labour, capital and enterprise – even though the productivity of these factors of production is relatively low at their locations. The result is that the "fat cats", gorged on rent, get fatter and the others starve. In time, whole industries – not just retailing but IT, oil, chemicals and many others – become dominated by a few large firms. Under the misnomer of "competition" this monopoly or oligopoly set-up is regarded as efficient, and even as a model for capitalist economies. From it flow the evils of inefficiency, huge inequalities of wealth and income, and a gross imbalance in the structure of industry, where "services" – including unproductive firms like property companies and tax experts – account for 70% of GNP.

The effects of a tax shift

Company taxation is fiendishly complicated, with companies bearing employment taxes, VAT, corporation tax (and all the allowances that accompany it), and business rates. Even small family businesses spend a disproportionate amount of time and money paid to accountants trying to reduce their tax burden – time which would be much better spent seeking to improve their products and services. The introduction of LVT would be accompanied by a simplification of the corporate tax structure. It would also mean that those companies which organise their UK business activities so that they pay little or no tax in the UK would either have to pay LVT or quit the UK, for a tax levied on the annual value of land cannot be avoided.

Were taxes that strike at labour, capital and enterprise to be removed in favour of land value taxation, UK industry would in the course of time be transformed. Rent-seeking firms would be eliminated as the tax on rent rose to complete the tax shift. Productive firms would be relieved of taxes on their inputs, and at the same time they would face diminishing land costs as LVT brought land prices down. Manufacturing would revive, albeit in new forms consonant with technological developments. Retailing would become truly competitive as small firms entered the industry on marginal sites released from heavy rent and tax burdens.

Other industries would experience profound and beneficial changes. Extractive industries (like oil, coal and other minerals) would pay taxes proportionately to the value of the sites they occupied, with their productive inputs of labour and capital free of tax. Deep or difficult seams would bear less tax than those with easy access. All kinds of industrial empires of monopolists and oligopolists would be revealed for what most of them are: collections of businesses held together by the glue of privately appropriated land rents.

Consumer choice would no longer be a response to the whims of advertising agencies; it would become the genuine expression of buyers confronted with a range of firms in every industry, except those that are natural monopolies. The charade of brand names owned by a few oligopolists with the semblance of competition would be no more. The counterpart of this really competitive market would be the free entry of producers into industries of their choice. Individuals or groups of workers could set up in business without the crushing costs of expensive land and heavy taxes. Workers' co-operatives might become a realistic possibility when both land and capital were available cheaply, and when the shadow of monopoly power was removed.

This would not be a return to 1909. World markets, technology, needs and tastes have changed significantly. But an economy built upon a land taxation system in which rent bears the taxes and productive forces are free to operate would be flexible and energetic. New conditions would be met by genuine enterprise. A truly liberal economy – enabling workers to fulfil their talents, entrepreneurs to become creative and consumers to exercise their free choices – could look forward to a century of economic progress far more rewarding than that experienced since the rejection of the 1909 Liberal budget.

Food Scarcity and Farming

by Duncan Pickard

We have been repeatedly warned that human starvation is inevitable because the capacity of humans to reproduce exceeds their capacity to produce sufficient food. The most famous doomsayer was Thomas Malthus, writing at the end of the 18th century, but the same message is repeated with increasing frequency in the present century. This is because of the popular acceptance of the theory of global warming, which has led to the almost universal belief that the area of land available for food production will be greatly reduced as a result of desertification, the rise in sea levels and the need to reduce greenhouse gases by using more land for growing biofuels.

Food scarcity is an everyday experience for millions of people in many countries; death from starvation is not uncommon today. It is estimated by the United Nations that there are about 850 million people currently existing on less than one dollar per day. Poverty and lack of food are closely associated. In the United Kingdom, the ability to produce sufficient food for our needs is also the subject of debate – especially in the farming press, where leaders of the farmers' unions repeatedly claim that they need more government help (i.e. money) to enable them to increase food production. The reason for wanting to increase self-sufficiency is the claim that the security of food supplies is undermined by greater reliance on imports.

Since the industrial revolution we have relied heavily on food imports. Self-sufficiency declined from 60% at the end of the 19th century to about 40% one hundred years ago. Self-sufficiency in total food supplies has not been much more than 50% since the end of food rationing after the Second World War. Even for food which can be grown in temperate climates, our self-sufficiency has seldom exceeded 65%. In recent years, supplies of beef, lamb and pork have continued to decline, making us more dependent on imports; self-sufficiency is currently around 60%.

Increasing our own production

There is no doubt more of our food could be grown in the UK. During the years 1939-1945 imports of food were halved, yet supplies were sufficient to avoid under-nutrition by increased home production and rationing. The general health of the population improved under these wartime conditions. Indicators of health such as the incidence of coronary heart disease showed significant improvements.

Within Europe, the ability of farmers to increase the supply of food in response to political and economic stimuli has also been clearly demonstrated. The Common Agricultural Policy – although it has always been more of a social welfare policy than an agricultural policy – succeeded in stimulating food production on a massive scale. The combination of production-linked subsidies, capital grants for buildings, and equipment and intervention in markets to maintain minimum prices gave rise to huge surpluses of most food commodities. These surpluses became such a political embarrassment that quotas were introduced, beginning with milk in 1984, and intervention in markets has been phased out. Such were the mountains of grain in stores throughout Europe that compulsory set-aside was introduced to reduce output.

The potential to increase food production is not in doubt. New plant varieties, improved pesticides and better cultivation techniques are being introduced which continue to increase output. If farmers improved their technical ability such that all could match the top twenty-five percent in terms of output and efficiency, total food production could be considerably increased. Constraints to agricultural output are economic and political. The effect of economics on production has been evident in recent years. In 2007-2008 the increase in the price of fertiliser and fuel, coupled with the decrease in the price of wheat because of good harvests in all the major grain-growing countries, meant that large areas of land remained uncultivated in 2009. Costs of production were estimated at sowing time to exceed the likely value of outputs, and so some farmers decided not to take the risk, and many fields were left fallow. Increases in the price of oil – which result in higher fuel, fertiliser and pesticide costs – would reduce food production unless the price of produce also increased.

Livestock production has declined throughout Europe in the last few years. The main reason for this was the political decision to change the Common Agricultural Policy from one where subsidy payments were linked to production, to de-coupled income support payments based on the area of land available to be farmed. In Scotland, large areas of the hills and uplands now have no sheep or cattle, because a farmer has no obligation to farm his land to produce anything in order to receive the area payment. If a farmer can obtain sufficient income from his land without keeping livestock or growing crops, it is reasonable for him to do so. It is a basic tenet of human behaviour for people not to work when they can satisfy their needs whilst not working.

Livestock farming has declined more than arable farming because animal husbandry is more labour-intensive than arable farming, which is more easily mechanised. A fact which is often overlooked in the debate about food production is that our political system relies predominantly on obtaining the necessary funds for public expenditure from the taxation of earnings (income tax and national insurance contributions) and

enterprise (value-added tax, capital gains tax and corporation tax). The costs of employing labour are much higher than they would be if government adopted the Liberal taxation policy which Lloyd George tried to implement one hundred years ago.

When deciding whether to retain a flock of sheep or a herd of cattle, a farmer has to be aware that he has to send a cheque to Her Majesty's Revenue and Customs in addition to the wages his herdsmen need to meet their own living expenses. For every two herdsmen he employs, the farmer has to pay to HMRC a sum approximately equal to the take-home pay of a third man. Should a farmer decide to invest in a bigger tractor for his arable land so that he can do more of the cultivation himself, he is allowed to offset some of the cost of depreciation of the tractor against taxable profit. This means that farmers (and other employers) are encouraged by our antiquated, disincentive and complicated tax system to make their employees redundant and invest in machinery instead. Because organic food production is more labour-intensive than conventional production, organic food is made much more expensive by the burden of employment taxes.

A change in taxation to land value taxation would change the economic balance between the use of labour and machinery on farms and allow more people to be employed. There would also be an increase in the opportunities for newcomers to enter farming. Under the current tax system, which taxes the ownership of property very lightly relative to the taxation of labour, those of us who own land find it easy to increase our personal wealth by maximising the area of land we own. This means that agricultural land prices are much higher than can be justified by the profit to be gained from farming the land. High land prices have a large negative impact on young people without money to gain access to land for farming, but those of us who own high-priced land find it easy to borrow money to buy more land because banks are happy to lend against the collateral value of the land we already own. A tax based on the value of the land we own would lead us to minimise our farms to the optimum size so as to maximise profitability per unit area. We would release land which is least profitable, for example those fields which are most remote from the farm steading and incur the highest costs to cultivate or to tend livestock. Land so released would be available for would-be farmers to use.

Food waste

It would be wrong to discuss food scarcity and the perceived inability to feed a growing world population without reference to the incidence of obesity and the amount of food which is wasted. In 2005 the WHO published statistics showing that there were 400 million adults classified as obese, and 1.6 billion more were overweight. The WHO

forecast for 2015 is for 2.3 billion to be overweight and 700 million obese. Apart from the huge medical health cost associated with these numbers, the amount of food consumed in excess of nutritional requirements must be enormous.

It has been estimated that about one third of all food purchased for home consumption in the UK is wasted, and the amounts of farm produce lost in developing countries through inadequate storage and consumption by vermin and other pests are huge. Before we become alarmed about our inability to avoid starvation on a global scale, there is much that can be done to make sure that existing food supplies are better stored, distributed and utilised.

Politics and food

That there are untold millions in the world who are undernourished is undeniable; but it is politics and economics which prevent most of these people from feeding themselves from their own land. Even where natural disasters such as severe drought result in the need to import food, it should be possible to obtain it from countries where food is produced in such abundance that millions are in danger of eating themselves into an early grave. In large parts of Africa, people are starving – not because their land is too infertile through climate or soil conditions, but because of conflict. Zimbabwe is an excellent example: when farmers had security of tenure on their land and were allowed to benefit from their labour and investment of capital, they produced sufficient food for the native population and also an exportable surplus. Now Zimbabweans are starving and need food aid.

In India and China, many are undernourished because of fundamental flaws in the systems of land tenure. In India the private ownership of land and the retention by landowners of the rental income produced by their tenants means that those who work the land have no incentive to increase output above that needed for their subsistence. Whenever a surplus income is produced, the landlord increases the rent and so takes the surplus from the tenant. In China the command economy denies the tillers of the land the opportunity to reap the benefits of their labour, should they seek to increase production. The common failing of all command economies is the tendency for workers to do the minimum necessary to meet the quotas they have been set.

Wherever we look in the world we find that there is the potential to increase food production when necessary. The common feature of areas where people are short of food is the denial of access to land to hungry people. Conflict, whether within or between countries, often results in starvation; but in many cases conflict has its roots in disputes over access to land and other natural resources. Unless and until non-

governmental organisations such as the World Bank, the International Monetary Fund and the agencies of the United Nations accept that the "Land Question" needs to be answered because it is central to understanding the causes of poverty and starvation wherever they exist, the search for a solution will be in vain.

The "Land Question"

A major handicap in confronting the land question lies with the teaching of economics in colleges and universities throughout the world. Most economists who teach the subject were themselves taught that "land" is "capital" and insist that their students also accept this to be true before they can be accepted as graduates. Instead of receiving a thorough grounding in the history of economics by studying the works of such political economists as Adam Smith, David Ricardo and Henry George, students are taught the contorted jargon associated with "business studies", and in fact know very little about economics in the true meaning of that word.

There is another handicap in facing up to the "Land Question". Whenever the leaders of the world's biggest economies meet to discuss "the end of poverty", were they to admit that there was an issue of access to land and the fair distribution of resource rents in some developing country, they would have to admit that there was also a "Land Question" to be answered in their own countries.

There is nothing wrong *per se* with the private ownership of land; on the contrary, security of tenure on land is essential for anyone investing in labour and capital to have the confidence that they might earn a suitable return on their investment. It is the private acquisition of the *rental* value of land (and other natural resources) which results in social and economic injustice. Because most governments in the world fail to collect economic rent from all who are privileged to occupy land, their citizens suffer from injustice. Firstly, those who benefit from acquiring economic rent from land are unfairly doing so because they did not create the land, nor did they themselves give it value. Secondly, because governments need money to fund their necessary functions and allow the private collection of resource rents, they resort to the taxation of labour and capital. This means that the goods and services which people produce by their own efforts have to be taxed. The disincentive effects of such a fiscal system are obvious. Such are the disincentive and unjust effects of our current fiscal system that it is difficult to imagine one which could be worse.

Food scarcity is a grim reality for many people and there is widespread anxiety about our ability to produce sufficient food for the projected increase in world population. However, most of those who have given careful and thorough consideration to this

subject have concluded that there are sufficient physical resources and technical expertise necessary to produce food in quantity and quality to meet current and projected demand for food. Whether or not this may be achieved is a social and political question. Its answer depends on our willingness to face the issues raised by Lloyd George in his "People's Budget" one hundred years ago.

An Equitable Tax Regime for Utility Companies

by Brian Hodgkinson

Many questions about economic policy look quite different and easier of solution once the introduction of a tax on land values is considered. In the case of the utilities of energy, water and telecommunications this is undoubtedly so. In particular, the fundamental question of public or private ownership and the related problems of pricing, investment and subsidy become much simpler.

Land, in the economist's sense of "the factor of production that nature supplies" (D. Begg), enters into the output of utilities in two ways: firstly, as the source of the raw materials of the industry, e.g. oil, water or radio waves; and secondly, as the location of individual sites or plants, e.g. power stations, reservoirs or cable lines. Given that suitable land is available as regards both source and location, then the factors of labour, capital and enterprise can co-operate to produce services of energy, water and telecommunications. Or, in a little more detail: to produce energy requires land in the form of fossil fuel fields, running water, wind, tide or solar rays, in addition to sites for power generating stations and land for pipelines and electricity pylons. To produce usable water requires land for reservoirs, purification plants and pipelines. To produce telecommunications services requires land for pylons, satellites, landlines and radio waves.

No two sites are the same, since natural resources are randomly distributed and each location is, by definition, unique. The quantity and quality of the resource varies greatly: for example, fossil fuel seams differ in richness and depth; wind and tides vary in strength; sites for transmissions depend upon topography. Hence the ubiquitous principle of the Ricardian rent of land reappears in modern guise. Every site, whether of a natural resource or of a unique location, attracts a rent, precisely determined by its relative advantage over marginal sites, which in theory have zero rent. The simple proof of this is that sites of any value have a capital price if put on a free market. Such a price is more or less the capitalised value of the annual Ricardian rent.

What is the relevance of all this to the utility industries? The oil industry alone demonstrates that this is probably the central issue. For who receives this rent? The answer, of course, is the owner of the oil field, usually an oil company that has prospected and exploited the field. But there is another potent question to be asked. Who is really entitled to receive this rent? Who or what creates the rent? The work of exploration, mining and distributing the oil is undoubtedly done by the oil company's

employees, capital and enterprise. So the company is clearly fully entitled to the proceeds of the productive work. But the value of this productive work does not include the rent. Why not? Because the rent is the return from the natural advantages of the site, i.e. the oil under the seabed. That was put there by nature. No individual person or company played any part in the matter at all. Hence the question of entitlement can only be answered by saying that the whole community has the right to the rent. It is the gift of nature for the community that can make good use of it. In practice, then, it must be a national resource available to the whole people.

Such a principle may sound far removed from the tough competitive world of modern capitalism, where the "free market" seems to extend to natural resources as much as to produced goods and services. Yet consider the consequences of ignoring the principle that the rent of land is created by nature and not by work, capital or enterprise. If it is wrongly assumed to be the product of these latter factors, then it falls into the possession of giant corporations as super-profits or of grasping individuals like the Russian billionaires who seem to have appropriated most of the natural resources of the ex-Soviet Union. Moreover, the true efficiency of the productive aspect of utility companies is grossly obscured. For example, how can anyone tell whether energy, water and telecommunications companies are efficient, if their so-called profits include huge elements of rent? Only if the rent is clearly identified can the residual surpluses or deficits become a measure of the efficiency of the factors that are actively engaged in production, i.e. labour etc.

What better and fairer way to identify this rent than by taxation? An annual land value tax would precisely measure it, for it is levied on the rent that natural resources and location yield. Thus it discriminates between a rich central field of fossil fuels and a marginal field, between a large reservoir near an urban centre and a small remote one, or between telecommunication sites of different capacities. A rare case of recognition of this principle by the government occurred for the oil industry. The Treasury proposed a tax allowance that would reduce the tax burden on marginal oil fields:

> A universal tax relief would be a 'blunt instrument' that would not target help on the oil and gas fields that most need it . . . The (proposed) value allowance would cut the tax rate for some projects, which should be the 'fields at the margin that are most in need of assistance'.

Financial Times, 25 January 2009

Oddly enough, a report on wind farms implicitly acknowledged the same principle. The proposal for a huge wind farm in the Thames Estuary elicited the fact that the Crown Estate owns the offshore seabed, and can charge firms investing in the wind farm for licences to build there. Such licences could vary in price according to the relative advantages of location of the windmills. There is no reason why these two examples of tax allowances on marginal oil fields and licences for building wind farms could not be generalised to bring under the benign umbrella of land value taxation all the cases of land use by utilities.

If we set aside moral and political reservations about nuclear power, an interesting further example of how this might work is offered by the industry. The previous Labour government approved a substantial increase in nuclear power. Our existing nuclear reactors are all but extinct. The French nuclear giant EDF obtained contracts to build new capacity in the UK in the form of either four or six new reactors. Where should they be located? This is a very serious question in view of public fears of pollution or accidents on the one hand and prospects for employment and technology on the other. The answer turns out to be very simple:

> British Energy has a unique advantage: its land. The easiest place to build new reactors is next to existing ones: locals (who often work at the plant) tend to be enthusiastic, and there is easy access to grid connections and less risk of protracted planning battles.

The Economist, 22 March 2008

So the best sites on purely economic grounds are adjacent to existing sites. At these places the local population is inured to the risks and welcomes the employment. The transport facilities are in place. Planning permission would not be such a problem. In addition to the sites that EDF is targeting, Wyfla in Wales and Oldbury in Gloucestershire have been selected by the German companies Eon and RWE in a joint bid. Far the best way for the government to recover the rent of these sites would be by means of an annual land tax, rather than by a once-and-for-all sale. An annual tax can be revised. Any future rise in rent from the likely rise in energy prices would be captured for the taxpayer, instead of going as a windfall to the French or German companies. This was dramatically illustrated when the price of the site at Bradwell, Essex, jumped from a reserve price of £40 million to a bid of £160 million. What falls to the operating companies should be the reward of efficient and safe power production, not gains merely from the future occupation of UK land.

Any introduction of a land tax needs to be offset by an equivalent reduction in other taxes. Since these all fall largely on production in one way or another rather than on rent, which is a pure surplus, this reduction would be a stimulus to productive firms, whether UK or foreign. Moreover, existing taxes hit marginal producers more heavily than others. The reason for this is that taxes like income tax, national insurance and VAT are charged at a uniform rate on labour and sales, despite the disadvantages of a marginal site. Firms in poor locations have heavier costs and a smaller market for their products, yet bear the same tax burden as those on central sites. The government seems to grasp this in relation to North Sea oil, but shows no understanding of the general principle. A tax on land values would give relief to marginal firms throughout the economy, not just a handful of oil companies on marginal sites in the North Sea.

Were all sites used by utility firms subject to a land tax of sufficient magnitude while being relieved of other taxes, the perennial question of public or private ownership would be much easier to answer. The utilities' profits (or losses) would no longer be distorted by large receipts of rent; hence their accounts would show the true operating situation. If they continued to record exceptional profits, this would be a sure indicator of monopoly power, assuming that efficiency was fairly evenly spread throughout the industry. In some cases, such as control of regional water supplies, monopoly is evident in any case. There is a natural monopoly whenever the duplication of capital, such as pylons or pipelines, would be pointless.

Oligopoly is also not difficult to identify when an industry only contains a handful of firms, as is the case for many utilities. The scale of the technology required perhaps makes this inevitable. Yet identifying the rent makes it easier to see which firms are more efficient. At present much so-called competition, for example between energy suppliers, is bogus. Stripped of rent by a land tax, their relative efficiencies as producers would be more obvious.

Public ownership is always preferable to absolute private monopoly, but of course regulation may be a better alternative when there is some degree of competition, as perhaps in the energy market. The whole issue of public versus private monopoly, however, goes beyond the terms of this article. Suffice it to repeat that a clear view of the presence of rent, and the case for taxing it, eliminates a major cause of confusion about the issue.

Questions on the pricing and investment policies of utilities also appear in a new light once the rent of land is brought into the calculation. As Ricardo demonstrated, rent does not enter into price, since price is set by the costs of the marginal producers. However, when the margin is closed down by taxation – as at present – the price is

set higher because supply is restricted. A tax on land value in place of existing taxes would release marginal producers; for example, in the North Sea, on less accessible coal fields, and at remoter resources of water – thus bringing prices down. Particularly important could be the effect on renewable energy, where wind farms, hydroelectricity and even tidal power might all develop faster if marginal sites were zero-taxed.

There could also be a substantial benefit to micro-producers. The green credentials of a land tax need to be fully examined. Micro-production – using individual windmills, solar panels or watermills, for example – is by its very nature marginal. Instead of complicated exemptions from tax or the granting of State subsidies, a land value tax would automatically relieve such projects of tax – provided, of course, there was a corresponding reduction in present taxes on production. The development of new sources of energy and water would be stimulated.

Biomass energy is an interesting example. The technology of boilers for burning willow or hazel to provide energy has improved noticeably. These woods can grow effectively on marginal land, e.g. on areas liable to flooding, but at present the land costs rise with the demand for the biofuel as landowners take advantage of the new market. A land tax would prevent the land price from rising whilst collecting the extra rent as public revenue. In effect, the use of previously unused marginal land would be a net gain to the economy.

Not only micro-projects but investment generally in utility industries would benefit. Taxes on labour, capital and enterprise raise the cost of productive investment, e.g. the building of utility plant and equipment. The present system of capital allowances against tax only gives partial relief to investment in productive assets. Even a 100% immediate write-off on new capital does nothing to reduce the cost of the assets themselves, for they are produced under a tax regime that raises costs of production by taxing labour and other inputs heavily. A tax on land lays no charge at all upon these factors, since it falls entirely on annual land value.

Investment would gain also from the fall in land prices consequent upon the imposition of an annual land tax. The capital price of land falls more or less proportionately to the level of the tax. A 50% tax would halve the price of land – although a gradual increase to 50% would be advisable to avoid difficult adjustments. Cheaper land would leave expanding utilities with more finance for productive investment in capital and new technology, instead of paying private landlords large subventions which contribute nothing to the economy. At present much of what is called "investment" amounts to no more than paying landlords to make suitable land available. Who produced the land? Who gave it the natural and acquired advantages that make it suitable?

Finally, what of the question of government subsidies to utility industries, whether public or private? Once more a land tax reveals a hidden aspect. Utilities like energy, water and telecommunications create very considerable external economies, i.e. benefits or cost reductions for firms and individuals outside the utility company concerned. These external economies are indicated by a rise in land values in the area affected. For example, when natural gas becomes available to a region, the price of both commercial and housing land rises. When telecommunications are extended in type or range, there is a similar benefit for landowners. A general land tax captures this benefit, which is fair on the grounds that it is a windfall gain in no way due to the efforts of the beneficiaries. Were this gain collected by taxation, there would be a strong case for making a subsidy available to the utility company that was responsible for creating it. In particular, such a tax could finance the necessary capital expenditure. There could be no more equitable way of financing a new power line, water reservoir or broadband extension than by collecting the value of the new facility from the chief beneficiaries. Indeed, why should anyone else pay for it?

This final point emphasises that in reality a land value tax cannot work well if isolated to one sector or area of the economy. Such a tax imposed on utilities alone would lead to distortion rather than equity. How could other taxes such as income tax and corporation tax be relieved only for utility companies, for example? Land use would also be inefficient were some land taxed and not the rest. The whole principle rests on the equitable taxing of rent, and rent exists throughout the whole economy. Only on the margins of production is it absent. Hence it must be taxed pro rata everywhere. Since it is created by nature and by the presence of population and public services, it is right that its collection as public revenue should be a cornerstone of an economic policy that looks to justice rather than to expediency.

Land, Location and Luck: Housing and the Land Tax

by Jock Coats

> You cannot build houses without land; you cannot lay down trams for the purpose of spreading the population over a wider area without land. As long as the landlords are allowed to charge prohibitive prices for a bit of land, even land, without contributing anything to local resources, so long will this terrible congestion remain in our towns . . . It is all very well to produce Housing of the Working Classes Bills. They will never be effective until you tackle the taxation of land-values.

David Lloyd George, at Newcastle, 4 March 1903

Shelter is one of our most basic human needs. From squatting in caves, through sheltering under animal hides stretched between trees, to the most luxurious twenty-first century super-yacht, we have yet to find a solution to our dependence on land – even if, in this last example, simply as a temporary mooring or supply point. For most of us, however, in the contemporary developed world, shelter means a home in a building of some kind on a piece of land somewhere.

Here in the United Kingdom, using our entire land mass there would be approximately one acre available for every adult and child if only we all budged up a little until we occupied an equal space each, and of course assuming it was free for the taking. But we don't. Not only is it not at all free for the taking, but it would be extremely inconvenient. We need access to other people, markets, jobs and social interactions. So we jostle with each other to be able to live in a place as convenient as possible for our individual combination of such needs.

This creates a market in the value of sites for us to live on. Those sites that are the most conveniently located in relation to the places more people wish to get to, for work, for trade, or for play and socialising, will be attractive to more people and so, using simple supply and demand, will have the highest value.

At some point, at a particular travelling distance (or, more likely, time) from those places we all have to get to, it no longer becomes practical or possible to travel to those places. Unless there are other similar centres nearby, the value of the sites beyond that point will be, to all intents and purposes, zero.

We can see this effect at work in the housing market in our towns and cities. At the height of the recent property price peak the lowest quartile average property in the London Borough of Kensington and Chelsea was worth twice as much as the lowest quartile property in the London Borough of Sutton. Would we believe that the buildings cost twice as much to build in Kensington as in Sutton? It's unlikely. We can only conclude that the factor that makes the Kensington properties worth so much more is their site values, that is to say their advantageous locations in relation to the centres of commerce, trade and social life compared with those in Sutton.

As another illustration of land values, in early 2008, the Chelsea Barracks 12.8 acre site in Kensington and Chelsea was bought for a record £959 million – which even at Kensington and Chelsea's average (and nationally high) population density would be £1.4 million per resident in the new development.

The changing "land valuescape"

There are many factors that can change the relative value of locations. One of these is the improvement of transport systems. We see this happening all the time. When the Metropolitan Railway was built out to Amersham in Buckinghamshire between 1868 and 1904, the company was able to finance the entire project by developing homes around the stations it was building, so-called "Metro-land". More recently, we have seen City of London workers making use of ever more efficient rail services to counties outside London – even as distant as Northampton, York and beyond. Site values in these areas have risen to compete with the London market, allowing for the additional commuting costs.

We can also observe other infrastructure, public and private, which alters site values. We often read how parents will try to get their children into "good schools" by buying up property in the right catchment areas. The state schooling system may well be equally free to all at the point of delivery, but the wealthy can afford to take up the places in better-performing schools because they can afford the property.

Similarly, private investment could bring employment opportunities or up-rate the jobs available in an area, say from manual to higher skilled (and paid) professional. The nearby housing that was once affordable for the manual workers needed by the factories is now priced out of their reach by the incoming accountants.

Some will say, "so what?" – you don't have to live in a particular location. If you are priced out of an area, go somewhere you can afford. What this objection misses, however, is that in a well-functioning economic area, those people now priced out are

likely to be just as necessary to the smooth functioning of that economy as everyone else. The new offices will still need their low-paid cleaners, the shops their low-paid workers. In fact, the very functioning of the things that will attract wealthy purchasers to the Chelsea Barracks apartments will rely on less-well-paid workers still being able to live a practical distance from their work.

The affordability gap

The asset type that has experienced the greatest rise in value in the past decade is of course housing, and much research has been done in measuring supply, demand, prices and the relative affordability of housing for various groups of people.

Looking at relative land values, for example, between 1997 and 2007 in the English regions, we find that on average in that decade land with outline planning consent for housing increased in cost by an average of 415%:

Percentage increase in land cost in English regions, 1997-2007

Region	Increase
North East	494%
North West	516%
Yorkshire and the Humber	455%
East Midlands	443%
West Midlands	352%
East of England	429%
South East	397%
London	387%
South West	402%
England average	**415%**

Over the same period, average house prices (including Scotland, Wales and Northern Ireland, which are based on Council for Mortgage Lenders figures) increased by an average of 294%:

Percentage increase in average house prices by UK region, 1997-2007

Region	Increase
North East	268%
North West	290%
Yorkshire and the Humber	284%
East Midlands	285%
West Midlands	273%
East Anglia	296%
Rest of South East	293%
Greater London	323%
South West	316%
Wales	291%
Scotland	274%
Northern Ireland	431%
United Kingdom average	**294%**

In this period, nationally, average household incomes increased by just 151%, whereas the average income of households entering the home-ownership market as first-time buyers grew by over 200%. Housing has thus become unaffordable to an increasing number of households. This disparity between incomes and housing costs has been reflected in a massive increase in household debt over the same period with a marked change in the structure of the entire economy. In 1995, mortgage debt was the equivalent of 54% of national GDP, whilst in 2006 it accounted for 84%. The total value of owner-occupied housing stock increased from 142% of GDP in 1995 to a whopping 268% of GDP in 2006. Put simply, our national stock of wealth increased by over 100% based solely on the debt-fuelled rise in nothing more productive than land values.

A century of change

In 1909, when Lloyd George proposed land taxes, housing tenure was very different from today. Just 10% of the housing stock was owner-occupied; the remaining 90% of households rented, all but 1% from private landlords. As a tax on ownership rather

than occupancy, his land taxes would have impacted most directly on that small proportion of the super-rich who owned real estate. By the early 1970s, half of all households were owner-occupied, and this figure continued to rise until recent years, when owner-occupancy peaked at just over 70% of all households, with only 10% or so privately rented and the remainder "public sector" rented (either local authority or housing association).

One of the most common objections to land value tax for residential property is that its impact on owner-occupiers would involve a far higher proportion of households than in Lloyd George's day. However, there are compelling counter-arguments to this objection.

There is a correlation between the proportion of the population who own houses and those who pay substantial amounts of income tax. Replacing taxes on incomes with taxes on land values, in other words, would not really alter the number of households subject to tax, but simply change the basis on which it is raised.

Some will further object that today's homeowners have built up a substantial financial investment in their property and that the tax will reduce its value. However, capital value (as we have seen above) is generated now, as it was in Lloyd George's day, by the efforts of others. It cannot be said to have been "earned" by the homeowner.

In any case, as long as we are living in it, the value of our house is little more than a paper value. House prices change all the time and our current "investment" is only really worth what it will buy in the form of our next house. The only point at which it can be liquidated as cash is when we trade down to something cheaper, or when we cease to need it and it is sold (often at death, by inheritors).

Paying the mortgage

What is it that we are doing when we decide to move from renting to buying our home? Usually we are calculating that it is better to be paying off a mortgage and acquiring a property than continuing to pay rent. Even though we may not think of it in these terms, real estate is valued, like any other investment, as the current value of a series of future income returns on the capital invested – in the case of owner-occupied housing these "returns" are not having to pay rent. We are also hoping that the capital value will grow.

Land taxes would reduce the initial capital outlay we need to buy a house by, roughly speaking, the amount of mortgage the annual tax would pay for. This is because the

capital land value would fall proportionately to the rate of the tax. Assuming we also reduce other taxes by the equivalent amount, this would result in a net increase in disposable income after housing costs. For example, if you are paying £10,000 a year in mortgage now and your property is half land value and half building value (and in expensive locations land will be even more of the total value than this), you would end up paying around £5,000 to finance your property and £5,000 in land tax, but you would also be benefiting from a roughly equivalent £5,000 reduction in your household's other taxes.

More land brought into housing use

The major benefit that a tax on land values would bring to the housing scene is that it would release unused or underused land for building. LVT penalises those who hold land out of use, so it would encourage owners of these sites to develop them or release them into the market to save on their taxes.

As an example local to me, a recent Freedom of Information Act request to Oxford City Council revealed that there are empty commercial properties worth around £100 million in site values in this small city alone. As long as the site is unused the owner pays no rates. Switching non-domestic rates to site value taxes would give a great incentive to release this land, probably for housing use. In the example of Oxford, this could produce sites for an increase of nearly ten per cent in the number of homes in the city, without touching any existing housing land or using virgin greenbelt land. It is likely that in other cities with less pressure on the housing market and more former industrial land, this could yield significantly more, further reducing the cost of housing for everyone.

There are some frequently raised common concerns in relation to LVT and housing that we should consider:

Negative equity

"Land taxes would lead to large-scale negative equity problems for those with current mortgages". It is true that if you had just taken out a mortgage for that £200,000 property only to find that suddenly land taxes halve the value of your property, you would have a negative equity problem. But that is not what is proposed. The tax would start at a very low level – under 5% – and would not reach these higher levels until some years after it had been in force.

If we look at the total value of outstanding debt on housing compared with the total housing market value, we find that only 31% of that value is outstanding mortgage borrowing, Land values, and so house prices, have risen so rapidly that only those who have taken out first-time mortgages in the past four years or who have remortgaged in "equity release" schemes would actually find themselves owing more than their property was worth even after land taxes were fully implemented.

Furthermore, in the current economic crisis as of 2009, those who borrowed in the past few years to buy at the peak of the market are already facing many of these problems. Reducing their outgoings by lowering other taxes would leave them with enough to continue paying their current mortgage. The long-term benefits of the structural change in taxation – which would serve to reduce and stabilise housing costs – would still be advantageous even to them.

Asset rich, income poor

"What about asset-rich, income-poor households like pensioners?" There is a current generation of people who paid off their mortgages while they were earning and are now subsisting on low pensions, free of most housing costs, and paying little direct taxation on their low incomes. They might find themselves with a new tax liability and little with which to pay it. Little, that is, except for the land values locked up in their current housing that, as we have seen, they have not really earned. The extent of this problem is much overestimated. The majority of the poorest pensioners are still tenants, whilst those in the most valuable properties are, by definition, amongst the wealthiest people in the land and with pensions to match. For those who genuinely would fall into this trap, many possible solutions have been offered, such as allowing them to defer the tax entirely until death – to be paid for out of the sale proceeds of their house – or until they sell to trade down.

According to research by Help the Aged, a significant proportion of those approaching retirement would actually like to downsize but cannot find suitably-sized property in the community in which they wish to remain. A more flexible land market would help to address this. At present once we have paid for our home we have little incentive to re-evaluate our need for that particular home in relation to others' needs. Once its size was reflected in the tax bill there would be an increased demand for more modest housing. Developers would start responding to the needs of different types of households at different stages in their lives instead of – as at present – waiting until mature neighbourhoods start to die off and then wreaking sudden, often very disruptive larger-scale redevelopments on the remaining residents.

Within a generation, however, we would have shifted to a culture where, by paying tax on what we use rather than on what we earn, we would have more money to invest in genuinely economically productive assets, through our real savings, and be better provided for when our main source of income ends. We can then make a more considered choice about what we want to spend our increased savings on: continuing to pay higher taxes on a home we may strictly no longer need, or reducing our tax bills and enjoying other benefits of retirement.

Garden grabbing

"Concreting over the countryside or suburban gardens." Once again we need to look at the problems associated with releasing land for more housing, and the efficiency, or lack thereof, with which we utilise our existing housing stock.

We currently have more empty homes than households on waiting lists. Patently there will not be a complete coincidence between where the empty homes are and where the demand is, but since land taxes are due whether or not a property is occupied they will create an incentive for owners of empty properties to bring them back into use and so receive rent from which to pay those taxes, or to release them for sale into the market.

Other contributors have shown that one result of LVT is to invigorate the economic life of marginal areas. As depressed regions of the UK get the benefit of this effect, many houses at present standing empty and unwanted will once again be attracting buyers, and the pressure on housing in the South East will slacken.

But in the final analysis, we may have to face the reality that if we wish everyone to have a decent home they can afford, some new land will need to become housing land. In such an eventuality, however, it is worth remembering that building 2 million additional new homes on unused land at significantly lower densities than currently recommended would use up just 200,000 acres, much less than half a per cent of non-urban land in the UK. Under LVT even this would be substantially less expensive than at present, when developers are free to buy up land and profit from speculative increases in its value during the landbanking, planning and development process.

In the end it will be for the planning process to make a judgement as to how to balance the need for houses against the need for green space. If a planning authority has a clear policy that it will not permit development in back gardens, or on other valued green spaces, then that will be reflected in the level of tax and there will be little inducement for the householder or landowner to sell, even if anyone wanted to

buy. If, on the other hand, the planning authority had a more permissive policy, the tax would follow the increased land value and the houses would soon appear.

Conclusion

As Lloyd George's quote at the start of this chapter rightly says, until we tackle the taxation of land values properly, government housing programmes will not succeed but will continue to cost taxpayers a lot of money. Meanwhile, owners of vacant land are free to do precisely nothing while they wait to pick up their windfall gains as land values increase.

Poverty and the Welfare State

by Margaret Godden

In 2008 we celebrated the centenary of the introduction of Old Age Pensions and the sixtieth anniversary of the founding of the National Health Service. It should have been a good year for the Welfare State. But was it? Controversy rages about the basic tenets of what had seemed to be the holy grail of British social policy.

The Welfare State, we are told, is producing a dependency culture; its cost is outstripping the available resources, and the standards of its various services are falling. Our hospitals are infected with MRSA, cancer patients are denied life-saving drugs, students are emerging from our schools unable to read, and there have been much-publicised failures in child protection and old people having to choose between food and warmth. Both Conservative and Labour governments have experimented with involving the private sector, but the results are both unpopular and unconvincing.

So this is a good time to review both what we can expect the state to provide and how it should be funded and managed.

There are certain functions which have always been seen as the responsibility of the state such as defence, policing, the coinage, and the maintenance of public spaces. They have not always included health care, education, financial support for the poor or the welfare of young, old and other "vulnerable" people. Through much of history these were the concern – insofar as they were anybody's concern – of family, friends, the wider community and charitable foundations. It is only in the last century that Britain, along with other advanced countries, has come to see them as primarily an obligation of government, and that electorates have been willing to pay large amounts of tax to fund them.

Pensions

Lloyd George's Old Age Pensions Act 1908 is usually seen as the true start of what has become known as the Welfare State. It provided for a non-contributory pension of 5 shillings per week to all citizens over the age of 70 whose income was less than 12 shillings. There is no doubt that it was a landmark piece of legislation; even then, though, the pension was being criticised by reformers for being (a) too low and (b) means-tested.

The Pensions Act was followed in 1911 by the first National Insurance Act, providing for those who were unemployed or unable to work through sickness. Contributions were compulsory and its application was extended until by 1920 it covered two-thirds of the employed workforce. State-funded relief had come to stay.

It was far from being an entirely new concept. The Elizabethan Poor Laws and their successors had responded to the increasing numbers of destitute beggars following the twin disasters of the destruction of the monasteries and the implementation of land enclosures. Monasteries were no longer there to extend charity to the hungry and homeless at the very time when villagers were being turned off the land. Poor Law relief was administered locally. The regulations changed from time to time, veering between the very harsh (with the workhouses more of a threat than a place of refuge) to the comparatively lax, which were then criticised as discouraging the idle from seeking employment. Today we see the same tension between the need to provide adequate support to the needy and the danger of encouraging a dependency culture.

Charitable giving peaked in the Victorian period. By the end of that century the average middle-class household gave 10% of its income to charity. Today we give only a tenth of that but charitable organisations still provide a raft of support for the needy – lunch clubs for the elderly, support groups for the disabled, drop-in centres and shelters for the homeless. Social Services Departments value their contribution, often with financial support. Larger organisations such as Age Concern may be contracted to provide services on behalf of the Council because it is recognised that they simply do some things better. Voluntary charity and self-help projects, as well as family and neighbours, still have a place alongside state provision.

In 1909 the 5 shillings per week pension represented 18% of average earnings. Lloyd George responded to criticism that it was too low by claiming, "It is only a beginning, but a real beginning". William Beveridge wanted to create a system which would pay a pension adequate to live on in the 1940s but had to settle for a level well below that, supplemented by a means-tested assistance scheme. Today the basic State Pension is a mere 16% of average earnings – below the 1908 level. Pensioners with no other source of income have to apply for supplementary means-tested support, though many fail to do so through pride or ignorance of their rights.

Over a century of sincere attempts to secure a reasonable level of income for all our citizens at the end of their working lives has spectacularly failed. Our Liberal Democrat constitution commits us to ensuring that no-one shall be enslaved by poverty. It is unacceptable that those who work throughout their lives cannot save enough to see them through their retirement. Rather than responding to this by paying inadequate

pensions out of taxation, is it not time for us to concentrate instead on preventing the poverty from occurring in the first place?

Health

If the majority of people had a high enough income during their working lives to provide for their own old age, they might also be expected to be able to look after their own health needs. However, even if possible, is this what most of us would want?

The National Health Service is without doubt the most highly valued institution of the 1940s Welfare State. The knowledge that if you fall ill you will be entitled to complete care – free at the point of delivery and based on up-to-date knowledge and treatments – is a comfort to us all. Of course there are some limitations on this promise which are a source of friction. If you are not young, old, suffering from a chronic disease or claiming some other special entitlement, you will be charged for your prescriptions; the availability of care is not uniform across the country; dental treatment (if you can find an NHS dentist) is expensive; NICE is accused of delaying approval of new drugs; and the intrusion of private provision raises many hackles. However, these are all seen as failures of the service to live up to its own high standards. The principle of a universal high-quality medical service available to all is something Britain is not going to abandon readily, even if the reality falls short.

Sadly, the reality does fall short too often. In 2009 newspapers reported the scandal of some 400 deaths in Stafford Hospital – the result of "appalling" emergency care, according to the Health Commission. At the same time, information obtained by a Conservative parliamentary question revealed 242 deaths of old people while in hospital through malnutrition (or, more precisely, starvation). Recently released figures for cancer survival rates show us coming 16th out of 19 European countries, with only Poland, the Czech Republic and Slovenia doing worse. Our poor nursing standards have resulted in the frightening spread of MRSA through hospital wards. Procedures and drugs which are routinely available in other European countries may be refused as too expensive – as in the case of the breast cancer drug Perceptin. In other words, the NHS is failing to provide top-quality medical care.

Some of this can be laid at the door of the micromanaging, target-driven Department of Health under the previous Labour government. There were well-attested cases of patient care being driven by managers' determination to reach a target rather than by medical good practice, e.g. patients being left in ambulances rather than admitted to A&E in order to delay the start of their waiting time. In the case of Stafford Hospital, it was alleged that managers pursued targets to the detriment of patient care, including

using receptionists instead of medical staff to carry out initial checks on patients coming into A&E. Liberal Democrats advocate a more locally managed health service with few if any national targets, and the Coalition government's early proposals for health reform seem to be going in that direction. However, as long as the NHS is "National" and as long as health policy ranks so highly as a matter of public concern, it is hard to see how any government will have the courage to stand back and really let the professionals get on with the job.

The NHS was never intended by its inventor to be the only source of care available to patients. It was the socialist Nye Bevan who set the template for the NHS such that patients who wished to supplement their treatment by paying for expensive drugs would be told that if they did so their NHS treatment would be withdrawn. Liberal William Beveridge would never have supported that. Speaking in 1946 he said, "The national minimum [of health care] means that no one is to fall below a certain standard – it will leave everyone free to spend his income above that standard as he will."

There are different patterns of health care in the European Union which appear to offer greater flexibility and choice to patients, and produce better health results, than our own system. Could it be that we are fixated with two beliefs: first, that the NHS is "the envy of the world", and second, that the only alternative to it is the US model of outrageously expensive medical care for the haves and very poor care (or none) for the have-nots?

As long as we have an underclass which gets the worst deal all round – the worst housing, worst schooling, worst job prospects and worst health – then it behoves the rest of us to stay part of a monolithic NHS, so that the more articulate and demanding will ensure reasonable standards for everybody. That, at least, is the hope.

However, if we could move to a more equal society, where real poverty was so rare that it could be accommodated generously either through state provision or charity or a combination of both, then perhaps we could find a way to dismantle the unhelpful aspects of a centrally-controlled NHS while still retaining its core values of universal access to high-quality health care.

Education

Whereas for every patient with the same condition, be it a twisted ankle or a stroke, there is a uniform procedure and a limited number of options, that is not the case for children. Every child is different; every child has special needs, though some are more

special than others. Increasingly, schools have been subject to control from central government, and the ability of teachers (let alone parents) to influence what goes on in them has been reduced. Families fight to get their children into the "best" schools, which they can judge only on league tables of SATS and GCSE results, since in terms of curriculum they are pretty much indistinguishable.

Central government judges educational success almost exclusively by examination success, and in particular success in a narrow range of subjects: literacy, maths and science. History, geography, modern languages (never mind dead ones), craft, art, music and sport do not figure in the SATS tables. This concentration on narrow targets has unintended consequences. The literacy hour is accused of making it harder to develop a love of reading in pupils. When ministers had a bout of concern about childhood obesity they found that schools, with their encouragement, had got rid of their kitchens and sports fields. Now that the collapse of financial services is drawing attention to our loss of manufacturing capacity, they bemoan the lack of students studying engineering, but it's too late. Technical subjects were downgraded long ago.

Just as children are different, so are parents. Some welcome a school that emphasises examination success. Others want to see a more relaxed view with the emphasis on character development and social interaction. Some want a strong religious element while others want the opposite. Some look for single-sex schools while others want co-education. Then there are the parents who think they recognise a special talent in their child and want a school that will develop it. Some parents dislike the very large secondary schools on offer and would prefer something smaller and more personal.

Even if you live in London or a large city you may have little chance of finding the ideal school for your child within the state system, unless you are in tune with the prevailing emphasis on examination success. If that is the case, all you have to do is to move into the catchment area of a high-achieving school (i.e. a school with high-achieving pupils). If you live in a rural area you probably have one secondary school within convenient reach of your home and that is that.

For too long, teachers have had to cope with an over-regulated national curriculum and the strain of "teaching to the test" in order to secure a good place for their school in the infamous league tables. Of course a lot of good work goes on in our state schools, with dedicated teachers and happy children, but this is more in spite of the system than because of it.

Meanwhile, whenever the government is faced with a problem relating to children or the family, the schools are expected to deal with it. In this respect, state schools are

seen as a tool of government rather than a service to the family and child. As teenage pregnancies rise we expect schools to provide better sex education; as bad behaviour in public places increases, schools must inculcate better values in their pupils; the country generally has a poor diet so do something about it in schools; we need to raise the recycling rate or reduce smoking, so deal with the subject in school and then the children will take the message home to their parents; working parents do not have time to look after their children, so schools should provide breakfast in the morning and after-school clubs to fill the gap. The state schools are lumbered with it all.

Much of this is due, once again, to an overly controlling government. The Coalition government is promising change, giving schools more independence and parents more power. However, it is hard to see how a state system of education could ever provide the wide variety of schools available outside the state sector. These are not confined to the obvious public and independent schools that cater for a largely privileged group. They include non-Christian faith schools, specialist schools such as the Yehudi Menuhin school for young musicians, international schools, experimental schools such as Summerhill, and "small" schools that deliberately keep pupil numbers low to give a highly personalised experience to each child.

It is surely amazing that as parents we are willing to entrust our children's schooling to a system over which we have so little choice or control. No child should be denied education through the poverty of his or her parents, so free and assisted places will always be needed. But what sort of a society is it in which over 90% of families cannot afford to pay for their own children's education? It is one which is suffering a bad case of the ill distribution of wealth.

An end to poverty?

It is the belief of the authors of this book that it is not enough to seek to relieve poverty. We should be striving to end it. The money that is spent every year in the UK on what we call the Welfare State is produced, one way or another, by its citizens. We need to ensure that more of it remains in their hands, rather than being recycled to them by the state. Lloyd George's other project, the taxation of land values, would have a major effect in achieving just that.

Why are average earnings so low? One reason is that it is hard to earn oneself a living in self-employment. The difficulties are not entirely related to land. The legislative requirements of health and safety, equal opportunities, planning and so forth, while desirable in themselves, often weigh disproportionately on small firms; and then there is the burden of dealing with those two bad taxes, VAT and income tax. Large firms

have whole departments managing them, a cost transferred from government to business which is rarely commented on. Small businesses must find the expertise to manage these systems when they should be concentrating on running the business. But the biggest problem they have is often finding premises to work from.

As long as landowners can afford to keep their land out of use until they get the highest possible rent for it, it is difficult for small businesses to start up. Even when the site is very marginal and the rent therefore low, the landlord may well think it is not worth the hassle of letting it. If a tenant does make a success of a new enterprise he will find his rent goes up accordingly as soon as the lease is due. Under a system of LVT the landowner would have to pay the tax whether the land was used or not – he would need to have a tenant. More sites would become available, rents would be stabilised, and self-employment would be a realistic possibility.

This is important because the level of wages is largely set by what a person can earn by other means. This is why if unemployment benefits are set "too high" people may choose not to work. We have seen people working for half-pay or even no pay at all when companies were threatened with collapse due to the credit crunch and staff knew there were no jobs out there waiting for them if they lost this one.

Large companies see wages as just another cost to the business, along with rent, bank interest, taxes, equipment, raw materials, etc. In small co-operatives, earnings are seen as the object of the enterprise. They exist to make a collective living for their members. (Why have the Liberal Democrats forgotten about co-ownership?) After two centuries of trade unionism, workers have become "human resources" – just a commodity to be purchased at the lowest price possible. Wages have become so depressed that we have had to introduce a minimum wage; even then, some employers will avoid it if they can by importing foreign workers and cheating the system. At £5.80 per hour it is barely enough to live on, but even so it is taxed.

Our present taxation system seems designed to keep the poor poor and the rich rich. The top earners cannot be effectively taxed because they will first hire an accountant to find a loophole; and if that fails, they will use their access to accumulated wealth to pay themselves a compensating increase. Meanwhile, the low-to-middle earners are mostly tied into a PAYE system which cannot be avoided. In addition, they have to pay VAT on their purchases and council tax on their home and all the other extras like stamp duty and road tax that come their way. No wonder the "hard-working families" that politicians admire so much have to turn to the state to supply basic needs.

Land value tax does not penalise you for working hard or spending money – or saving it. It simply collects from those who claim ownership of land the accumulated value which has accrued to that site through the efforts of generations of citizens past and present. Its effect is to encourage enterprise and to make it impossible for individuals to claim gross amounts of wealth which they have done nothing to create. It would reduce the disparities of income that we see today and make it possible to provide generous support for those few who really needed it.

Banking and Finance

by Christopher Glover

The credit crunch and financial crisis of 2007-2008, which brought the banking system to the point of collapse, is by general consent the most serious economic crisis since the Great Depression of the 1930s. Lax monetary policy and imprudent bank lending fuelled an unrealistic and unsustainable boom in residential and commercial property (i.e. land) prices. Over-reliance on the interbank market and the use of financially innovative "products", particularly in the repackaging and worldwide distribution of sub-prime lending in the United States, also had a lethal effect.

It would be churlish and unfair to lay all the blame for this situation on the banks. In an attempt to prove that it was finance-friendly, the Labour Government under Tony Blair set about ingratiating itself with the City. Ministers were taken in by the vast profits the banks were making and failed to see any danger in the financial engineering/innovation on which it was based. Mesmerised by the success of the City, they turned a blind eye to the grotesque compensation packages granted to the manipulators of money. There were policy mistakes too. The transfer of bank regulation from the Bank of England to a new untried body, the Financial Services Authority, was a serious error. Appointing a professional economist as Governor of the Bank of England rather than an experienced banker was also unfortunate. Nevertheless, the banks have much to answer for.

Historical background

British – and particularly Scottish – banks have traditionally had an enviable reputation for financial probity, integrity of dealing and reliability. True, they were not regarded as the most imaginative or adventurous of institutions, but they were solid and dependable. That reputation has taken a battering in recent times. How has this come about?

Historically it would seem that the passing of the Competition and Credit Control Act 1971 was a turning point. Until then the Government kept a strict control on bank lending and consumer credit. The banks operated an interest rate cartel and worked within government-imposed quantitative and qualitative controls on lending. In consumer credit there were controls on the length of hire-purchase contracts and the percentage deposit required. The bank manager was a conservative individual conscious of the fact that he was lending depositors' money. It was not easy to borrow money.

The 1971 Act abolished most of this and allowed the chill winds of competition to blow through the banking industry. The results were dramatic. In the two years following the introduction of CCC there was a rapid expansion in bank lending, the money supply and wholesale (i.e. interbank and non-bank) money markets. In this new world, unregulated "fringe" banks – licensed deposit-takers authorised by the Department of Trade rather than the Bank of England – began to flourish, obtaining much of their funding from the wholesale markets. These fringe banks lent to property companies, often by way of second mortgages. The clearing banks were big lenders to the fringe banks via the wholesale money markets.

In November 1973 a fringe bank, London and County Securities, ran into liquidity difficulties, being unable to renew deposits in the wholesale markets. The property boom was coming to an end and the clearers were increasingly reluctant to lend to the fringe banks. The resultant loss of confidence in the fringe banks threatened to spread to the banking system proper. The Bank of England responded quickly by organising a support operation known as the "lifeboat" in co-operation with the London and Scottish clearing banks. This support operation was organised – very successfully – behind closed doors. Some thirty fringe banks were bailed out. It is widely believed, too, that one of the big clearing banks and a prominent life assurance company were also in the "lifeboat".

The secondary banking crisis of 1973-1974 occurred well over 30 years ago, and yet its salient features – slack monetary policy, imprudent lending, a boom in property prices, and over-reliance on the wholesale money markets – are depressingly familiar today. It illustrates all too clearly the consequences of obliging the banks to operate in the "laissez-faire" open market. Prudence and the protection of depositors' money took a back seat in the banks' pursuit of profit. The secondary banking crisis did, of course, lead to a considerable tightening up of prudential supervision, and eventually the passing of the Banking Act 1979. Nevertheless, the philosophy behind CCC remained intact: banks were to compete in the marketplace.

The consequences of this philosophy are evident in the recurrent economic crises to which this country has been subject. Although each crisis has its distinguishing aspects they all exhibit familiar common features: (1) there is an unsustainable boom in property prices; (2) banks engage in imprudent lending; (3) credit institutions become unduly reliant on short-term funding from the interbank market; and (4) a new feature in the current crisis – the banks use complicated financial devices ("products") to circumvent regulatory capital requirements.

These distinguishing features are each discussed in turn.

The boom in property prices

Every property has two elements: the building itself and the land on which it rests. As the building deteriorates over time and is in constant need of maintenance, it is the land or site which causes the property to rise in value – in real terms, at least. The classic justification in economic theory for a rise in the price of a thing is that it brings forth increased supply. However, this cannot happen with land; it is fixed in supply.

A rise in land prices therefore serves no useful economic purpose. On the contrary, rising house prices raise the bar for young couples trying to buy their first home. At the same time, those of the older generation who bought their houses years ago find themselves living in houses which they could not afford to buy at today's prices. In effect, rising house prices represent a transfer of wealth from the younger to the older generation.

Rising land values also push up the rents for shops, offices and industrial premises. When times are good, this means only the most profitable shops can afford high street rents. The sole trader, small shopkeeper or restaurateur is progressively squeezed out and replaced by identikit chain stores and multiples. In a downturn, high rents push traders out of business altogether. As a result, properties lie empty when they could be used at a lower rent. Factory and warehouse premises lie idle for the same reason. High land values thus bring in their train rising unemployment and lower output.

The reason why rising land values have this pernicious effect is not difficult to find. Because property (i.e. land) is expected to rise in value with economic growth, there tends to creep into property values a speculative element. Where this happens, the rent demanded (or the purchase price) reflects not just the current benefit of the site but some of the future benefit. In times of economic expansion this speculative element in the price of land and buildings becomes dangerously high. Homeowners then find they cannot meet the mortgage payments, retailers can no longer afford the rent and businesses look for cheaper offices.

Rising property prices are therefore socially divisive and economically disruptive. Government policy should aim to nip any nascent property boom in the bud. An annual land value tax would give government some control over the level of property prices. Such a tax would not be a disincentive to work or production since the rise in property (i.e. land) values does not arise from the efforts of the owner but from the community. Government infrastructure expenditure is a good example of this.

Imprudent bank lending

Over the years, and particularly since the Thatcher "revolution", the profit motive has increasingly become the central focus for the banks, and as a consequence prudence has suffered. In former times, when prudence reigned, a bank would rarely advance more than 70 per cent against the value of a property. But in recent times, mortgages of 100 per cent and even 125 per cent have been common. Income multiples, too, have risen. It was not that long ago when a mortgage income multiple of three was considered the maximum. At the height of the recent boom, income multiples of five and six were not unusual.

Prudence dictates that a bank should not borrow short and lend long. Yet this is precisely what Northern Rock (and others) did on a large scale. Building societies have been encouraged to abandon their mutual status and become limited companies listed on the Stock Exchange, thus giving them access to additional sources of finance and increasing their lending – and hence profit – capacity.

Although imprudent bank lending doubtless affected all loan categories, it was particularly important, and highly evident, with regard to property loans. As far as the typical bank or building society officer is concerned, the loan he authorises is conceptually distinct from the property on which it is secured. Yet collectively, bank and building society credit is the largest single factor determining property prices. Imprudent bank lending policies were instrumental in causing the property boom.

As argued earlier, rising property (i.e. land) prices serve no useful economic purpose. On the contrary, they are highly damaging. The mountain of bank and building society credit supporting excessive property prices has been misdirected. It should have been channelled into financing the production of goods and services.

The interbank market

Over-reliance on the interbank market precipitated the collapse of Northern Rock. The availability of funds in this market suddenly dried up when it became clear that heavy losses were being incurred on sub-prime property lending in the United States.

The freezing up of the interbank market did not only affect Northern Rock. Its effect was reportedly such that normal bank lending could not be resumed until the interbank market was brought to life again. But why is it that banks cannot function properly without the interbank market, i.e. without lending to each other?

Banks have two main functions: they operate a payments system for depositors and they extend loans to individuals and organisations. From experience, the banks know approximately what percentage of their assets they need to keep in liquid form to satisfy the cash requirements of their depositors. The remainder is lent out at interest. There is nothing in this simple description of the basic function of a bank to indicate the necessity for the banks to lend to each other on a massive scale.

The interbank market can be viewed from another angle. Assume, for example, that all the banks in this country were owned by a single holding company but in every other respect were unchanged. The consolidated balance sheet of that bank holding company would show the banks' sources of funds on the left-hand side – deposits plus shareholders' capital – and the uses of those funds on the other side – loans at interest, liquid assets and the banks' fixed assets (bank offices, equipment, etc). There would be no interbank lending. It would all have been cancelled out on consolidation – one bank's loan asset being offset by a corresponding liability to repay it on the part of another bank.

There is no obvious reason why banks need to borrow from each other – apart, that is, from the traditional overnight borrowing which banks engage in to suit their changing day-to-day liquidity requirements. To lend depositors' money to another bank is to delegate to that other bank the responsibility reposed in it by the lending bank's depositors. Why should a bank do this?

Financial engineering by the banks

The regulatory authorities insist that banks maintain a minimum level of shareholders' capital. This capital adequacy requirement is to provide a cushion to absorb any loan losses. It is an assurance to depositors that their money is safe. Typically, the capital-to-assets ratio is around 5%. Thus for every £100 of loans the bank must have £5 of its own capital. The capital adequacy requirements distinguish between assets which have little or no risk and those which carry risk. Normal bank lending entails risk and attracts a capital adequacy requirement. A bank which is up against its capital adequacy limit may not engage in further lending.

Economic conditions in the ten years preceding the present crisis were generally benign, both at home and abroad. This was a sustained period of uninterrupted economic growth. It was a good time for banks. However, as lending rose, capital adequacy was in danger of becoming a constraint. To circumvent this difficulty, the banks devised various credit-shifting "products", the effect of which was to remove

the credit risk from the originating bank's loans, thus allowing that bank to increase its lending without the constraint of the capital adequacy requirements.

A detailed description of these financially engineered "products" is not possible here. They were highly complex artificial constructions and the mathematics used in devising them was often unintelligible, even to insiders. In essence, they consisted of bundling up a portfolio of loans, transferring it into a specially created vehicle and selling tranches of this vehicle to investors. Each tranche had different investment characteristics. The credit risk of these loans was no longer on the originating bank's books.

The creation of these structured investment vehicles and the sale of interests in them was highly profitable, both for the investment banks which devised them and for the originating banks. It was through "products" such as these that banks around the world were induced to invest in US sub-prime mortgages. Those that did so were often investing in triple A-rated securities, and yet the underlying loans on which they were based were anything but triple A-rated. The ingenious mathematical structure of the vehicle – which few apparently could comprehend – was supposed to ensure this benign outcome.

The notion that risk can disappear by means of financial prestidigitation is not entirely new. Modern portfolio theory holds that by combining securities in a portfolio their aggregate risk is reduced (as opposed to being merely averaged). In other words, some of the risk disappears by the very act of combining securities in a portfolio and it reappears again if the portfolio is broken up. This, of course, is arrant nonsense, yet it continues to be the received wisdom in academia and is the basic premise of much investment management activity in the City. The problem is mathematics. No one likes rejecting a theory or a "product" because they cannot grasp the impenetrable and abstruse mathematics in which it is expressed. Such a person only shows his ignorance. And, of course, these financially engineered "products" were most convenient.

The simple fact remains, however, that no amount of financial wizardry can produce something out of nothing. The benefits or advantages for investors in these specially created vehicles (such as CDOs – collateralised debt obligations) could not exceed those in the underlying portfolio of loans. Why should the originating bank give up these benefits through the mechanism of a CDO? The obvious answer is that, with the credit risk removed, the bank's capital adequacy requirement was reduced, leaving it in a position to make further loans. The bank would also make a profit from charging fees to the CDO and by retaining an interest in equity.

The banks would no doubt hotly deny that the main purpose of these structured investment vehicles was to circumvent the capital adequacy requirements. While acknowledging the benefits of what is euphemistically termed "regulatory capital relief", they point to other advantages such as spread arbitrage opportunities, funding and economic risk transfer. But these are self-serving and do not bear examination. The banks' evolving loan-to-deposit ratio tells it all. This rose from almost 100 per cent to 150 per cent between 2000 and 2008.

Traditionally when a bank makes a loan, it monitors it carefully to ensure the timely and correct payment of interest and repayment of capital. However, if the bank plans to transfer the loan (or the credit risk in it) into a specially created vehicle for onward disposal, its attitude to the loan itself will be sensibly altered. It will not need to be so concerned about the quality of the loan. So these structured investment products subvert the traditional banking approach and could well lead to lower loan quality.

These clever products of financial engineering proved very attractive in the benign economic conditions from 2000 onward. But once the sub-prime lending crisis broke they collapsed like a pack of cards. The losses occasioned by these instruments were huge, almost wiping out the capital base of some banks.

Conclusion

Banks cannot be allowed to fail. This is because the failure of a bank, if the authorities do not handle it properly, can easily lead to a lack of confidence in the banking system, with depositors rushing to withdraw their money. Economic activity would soon grind to a halt. This circumstance puts banks in an entirely different category to ordinary businesses.

The security of depositors' money should be of paramount concern. Yet if the bank's management know that all its deposits are guaranteed by the State, the temptation to take undue risks with the bank's assets, thereby boosting executive pay and shareholders' return, will be difficult to avoid. It is therefore necessary to treat deposit-taking institutions as public utilities. Their profits must be capped. This may be done by means of a regulatory body, as it is with other utilities. Alternatively, the Government could introduce an excess profits tax applicable solely to banks.

It is clear from the present, as well as past, economic crises that other measures are also required if the banking industry is to be put on a sound footing and another disastrous financial crash is to be avoided. First, there must be an end to financial engineering/innovation and grossly excessive executive remuneration. Banks must

return to their traditional way of operating. In making a loan, the bank concerned is best placed to understand the risk entailed and to ensure that the customer makes timely payment of interest and repayment of principal. Banks must keep the loans they make on their books, together with the associated credit risk. The practice of "originate and distribute" must be outlawed. It should be illegal for banks to transfer their loan risks to structured investment vehicles such as CDOs.

As the discussion above shows, it is by no means obvious why the interbank market should be so crucial to the operation of banks. The role of the banks is to lend to others, not themselves. Yet the freezing up of the interbank market precipitated the current financial crash. All this points to the need for a comprehensive enquiry into the workings and role of the interbank market.

There is also the question of bank regulation. It is tempting to see in the failure of the regulatory authorities to anticipate the crisis the need for a thorough overhaul of the current system. Yet it would be wrong to smother the banking industry with yet more layers of rules-based, box-ticking regulation. It would be infinitely preferable – and more in line with the traditional approach in this country – for the authorities to lay down general principles or guidelines for banks. These could be accompanied by a more "hands-on" approach in monitoring compliance.

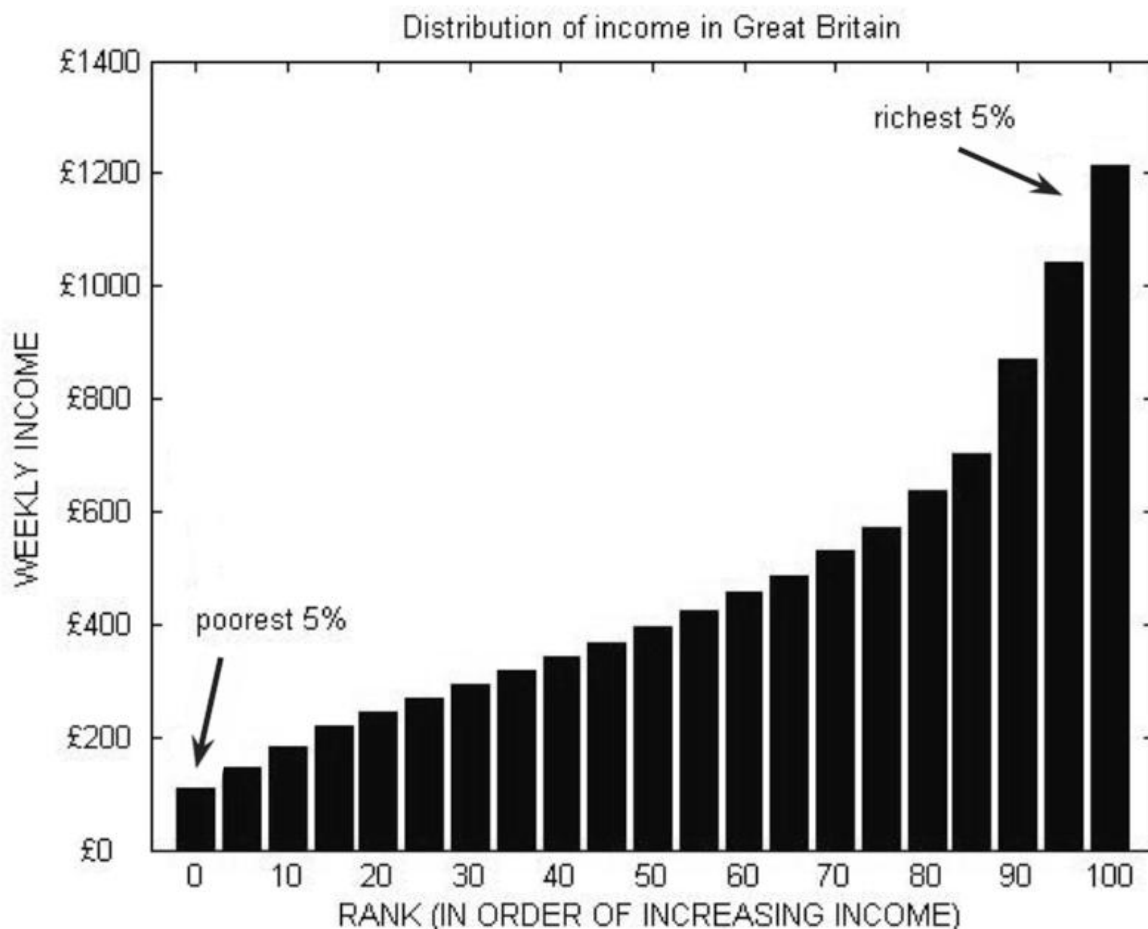
Effective measures to curb imprudent bank lending are difficult to devise. The authorities could impose quantitative and qualitative controls on property lending, i.e. restrict the amount banks can lend for this purpose and stipulate minimum loan-to-value ratios. But this would be a clumsy measure with arbitrary and potentially unfair consequences for individual banks. A neater and more efficacious solution would be to introduce a national tax on land values. This would give the government some control over property prices and reduce the speculative appeal of property. Another advantage is that a huge amount of unproductive bank credit would thereby be released and become available for financing worthwhile investment in the production of goods and services.

Land Value Tax: The Social Justice Argument

by David Cooper

The advantages of land value tax have been explained elsewhere in terms of economic efficiency. However, there is another advantage that is often overlooked: without a significant element of tax on property holdings, income tax is unfair.

In Britain, income is unevenly distributed. If you took a representative sample of 100 people and formed them into a procession from lowest paid to highest, you would find that each of the five lowest paid earn only about £100 per week. The next five would each be on about £150 a week. The wage would rise quite slowly as you moved along the procession, so people near the middle of the procession – the 50th person and the few after – would be earning on average just over £400 a week. After this, incomes would increase faster, and the fortunate five or so people at the end of the procession would be earning a very comfortable £1,200 per week.

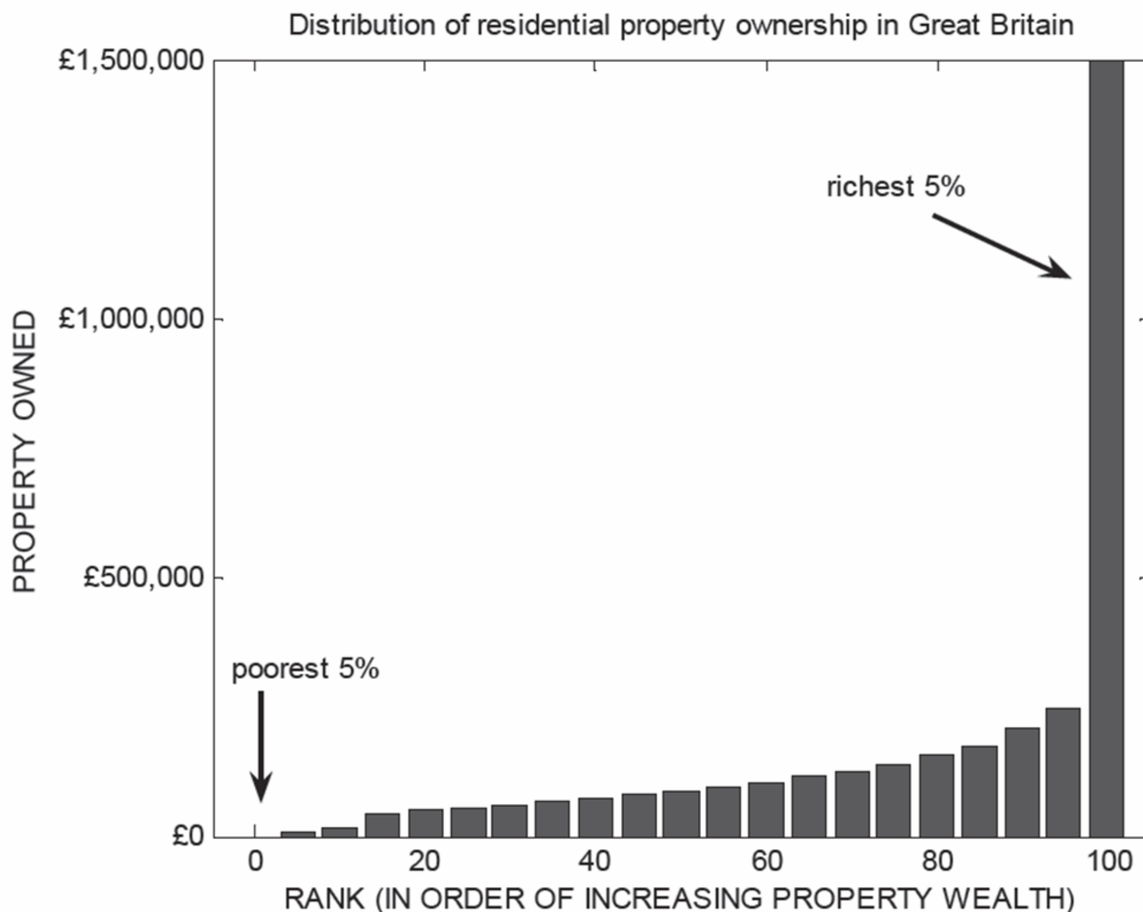


Source: Institute for Fiscal Studies, Report *Inequality and Poverty*

This procession is illustrated in the "distribution of income" bar chart. The population of Great Britain has been divided into five-percentile groups, from lowest earners to highest earners, and the bar chart shows the average income received by each group. It should be noted that a few individuals in the top five-percentile receive considerably more than £1,200 – for example, professional footballers or bankers – but this is made up for by the many individuals who receive slightly less.

Income tax seems to be a fair way of raising money for government expenditure. Provided it is levied at a rate that is proportional to income actually earned, the result is that the richest in society pay their fair share of its costs. The British income tax system is "progressive", i.e. a higher tax rate is levied on higher incomes. So far, so fair.

Unfortunately there is a problem, especially in Britain. While income is distributed unevenly, ownership of wealth (such as property and financial assets) is distributed yet more unevenly. This is shown in the "distribution of residential property ownership" bar chart, which illustrates the distribution of property wealth, again divided into five-percentile segments of the population. While the distribution of income is certainly uneven, it is nothing like as skewed as the ownership of wealth.



Source: HM Revenue & Customs, Estimated wealth of individuals in the U.K., 2003 (year of death basis)

In fact, if you made a procession of 100 people in order of property wealth, the richest five would own almost half the total. They would be on average six times wealthier than the next five persons in the procession – themselves relatively affluent individuals – and 15 times as wealthy as persons in the middle of the procession. Over half of all UK wealth is privately-owned residential property[1].

Broadly speaking, property wealth and high income go hand in hand, so the people at the top of the "property" procession are pretty much the same as those at the top of the "income" procession. In the "income" procession, the five persons with the highest income get about 20% more income than the next five, so they pay over 20% more tax. But due to the distribution of property, they are in fact 600% wealthier.

When tax is based exclusively on income, individuals who are just outside the wealthy elite will compare themselves with others who are many times wealthier and see that the amount of tax they pay is not very different. The more unequal the distribution of wealth, the worse this group is affected since the tax system erodes their limited wealth at a disproportionate rate. However, the evils of gross inequality – so tellingly documented in the book *The Spirit Level* by Wilkinson and Pickett – affect all. Unless politicians find the courage to tax wealth and not just income, gross inequality will continue to afflict British society.

Tax will never be welcomed, but it should at least be fair. A tax based on wealth in the form of land must be part of a fair system, operating along with income tax. Such property wealth is an excellent indicator of overall wealth, and is especially easy to identify: land cannot be moved or taken offshore, unlike financial assets. Any property tax needs to be well-implemented, free of distortions, and truly reflect market values (unlike the notoriously regressive council tax, which is almost a flat rate poll tax based on outdated valuations). This is entirely feasible; site valuations are transparent and supported by an open market. There are economic advantages: property taxes levied on the value of the land holdings encourage efficient use and discourage speculation.

There is a popular belief that income tax is the fairest tax, since it reflects ability to pay. This is wrong. Income tax is easy to extract, and for the very wealthy is relatively painless, but it does not truly reflect ability to pay. With a tax system based primarily on income, conservative-minded middle-income earners will continue to complain bitterly that their taxes are too high. They will be right, but the real pain will be endured by the poor.

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[1] *Source: Office for National Statistics, "Capital Stocks, Capital Consumption and Non-Financial Balance Sheets 2008". Net worth of UK is ~£7tn. Value of privately owned residential buildings is ~£4tn.*

We Can Do It This Way

by Tony Vickers

In 2006 the Liberal Democrats adopted a policy in favour of a major switch of the tax burden off wealth creation and onto wealth accumulation, lifting millions of low-paid earners out of income tax altogether and closing the loopholes which enable the very rich to avoid paying their dues. There was also a commitment to "green" taxes. Council tax would be abolished and replaced with a "fairer" tax which might be local income tax, although ALTER would not recommend that. NNDR, the present business rate, would be replaced by Site Value Rating, the name usually used for LVT as a local tax. The Tax Commission was expected to revisit the issue of a replacement domestic property tax in 2007, but this never happened.

ALTER proposes that LVT should be introduced on all types of land primarily as a national tax, initially at a low rate, but progressively replacing other taxes as the rate is increased. We suggest that the first to go would be other taxes related to property (i.e. stamp duty and inheritance tax). However, we would also wish to raise the basic income tax threshold further and faster. Local councils should be able to choose between basing their tax on either LVT or income tax or both: something that Party Conference overwhelmingly agreed to in 1999 in the motion "Choice for Revenue Raising", which – for presentational reasons – has been ignored ever since. Local government would use the well-tried method of "precepting" to obtain its share of LVT from the central pot.

Introducing LVT

For any tax on land values, we need to know the owner and the value of each land site. A Land Register must be completed with values assigned to each piece of land.

Our Party policy already calls for "national land valuation within five years". This does not require primary legislation. A decision, in principle, to tax land owners would trigger compulsory retrospective registration of land rights. In any case, nearly 80% of land sites in England & Wales are already registered. This accounts for only half the land area but probably 95% of total land value.

Altogether, enough information is held by government (albeit often not in a suitable form) to achieve a full nation-wide valuation for tax purposes within one parliament.

The property industry needs better information for property markets to work more efficiently; information systems are already being designed around their needs, as well as the public need, for a national property database. The cost of a modernised tax system could be underwritten by private sector partners, but we would probably wish to see the tax introduced before this detailed preliminary work had been completed. It is possible to derive an approximate land value by taking the gross property value and deducting a standard allowance for the buildings based on average construction costs in the area. An appeals process should pick up any serious anomalies and landowners could be invited to self-assess, with local authorities being given the right to acquire undervalued sites. These interim valuations would be replaced as more accurate figures became available. This procedure should be politically acceptable as the interim valuations would be seen to be far more accurate than council tax bands.

"Highest and best" land use

Like most developed countries, Britain has a highly regulated land use system. It would be grossly unfair to demand that a landowner pay tax on a vacant site assessed to be fit for housing if that site had just been refused planning permission. So the valuer has to decide for each site what use will command the highest rent and also be acceptable to the planner. Planning regulations have an enormous effect on land values, especially at the fringes of urban areas where agricultural land is under pressure to provide much-needed homes. Within towns and cities, "garden grabbing" – largely a consequence of defining "brownfield" land such that any house in a generous plot is threatened with demolition – can have major land value impacts.

Valuation for LVT would be "plan-led". For each site, valuers would assess whether any new use which offered a higher financial return to the owners was permissible under current local planning policy. This "highest and best use" would be the basis for taxation. For the vast majority of sites the current use is also the highest and best use. Where there is doubt, valuers would obtain a "Certificate of Development Potential" from the planning authority: this suggestion was made 30 years ago and has never been seriously questioned. The default taxable site value is then the market value minus the value of buildings and other "improvements" (e.g. roads, services and earthworks) already on the site.

A 2008 study[2] by Kingston University indicates that enough evidence exists under the emerging planning system to create a national land use database quite rapidly.

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[2] *The author was Researcher on this Scoping Study for the future of the National Land Use Database of Previously Developed Land (NLUD-PDL), published in September 2008.*

Kent County Council has estimated that it would only take one person, with minimum training, a week per district ward to capture existing land use information. This puts the cost of an initial sweep of the country at a very affordable £6-10 million.

Continuous monitoring of values

Thereafter, the database must be kept up to date. The old rating system and the present council tax have both fallen into disrepute partly because of government's failure to conduct revaluations. Sir Michael Lyons, in his report on local government finance in 2007, estimated that some 17% of households (3.7 million) were probably paying too much council tax because of the lack of revaluation since 1992. With LVT being a more significant tax than council tax, regular revaluations are essential. Fortunately, as LVT is only concerned with the land and not the buildings on it, revaluations would be much easier and cheaper than a revaluation for council tax.

Commercial property investors are increasingly developing automated valuation systems based on actual property transactions. Some of these systems review valuations every month. Such a rolling register would be very useful for assessing LVT. It could be used to make interim adjustments outside the regular annual or biennial revaluations.

This would be particularly beneficial to people who find their property's value threatened by an unwelcome development – a noisy motorway or a drop-in centre for offenders. Most of the objections to planning applications are related to such perceived loss of value for nearby sites. Where this fear is justified the loss of value would be noted and the tax could be lowered ahead of the normal revaluation. LVT would take much of the sting out of planning decisions for "losers". At the same time, it would recover much of the unearned gains by "winners" on neighbouring sites which are improved by the new development.

How LVT will affect taxpayers

LVT is levied on the annual rental value of the site in question, which relates directly to the capital value. The level of tax should not be so onerous as to oblige the owner to disown the land. It should, on the other hand, be high enough to oblige him to use the land. As owner he is the custodian of a valuable asset in which the community at large has a direct interest.

How much will the tax yield? In 2007 residential land in the UK was valued at an estimated £1.9 trillion, giving an annualised rental value of £140 billion. In the absence

of national land valuations, these figures are necessarily approximate; the true values are likely to be higher. They then need to be increased by at least £600bn (£50bn rental value) to allow for commercial land and other land not currently taxed at all. So a 5% rate of LVT would yield around £9.5bn and a 50% rate around £95bn. These compare with current receipts of £22bn for council tax, £13bn for stamp duty and £148bn from income tax. Since the full economic rent – particularly for commercial land – is much more than any estimates related to amounts paid to landlords, the potential tax revenue available from annual rental values is much greater than these figures suggest.

A high rate of tax would cause considerable disruption throughout the economy if it were introduced immediately, so the initial rate would need to be much nearer 5% than 50%. This could be raised over a period of five to ten years to a rate that would bring about really beneficial changes of the type mentioned in these essays.

The political dimension cannot be ignored. In 1909, and again in 1931, the introduction of LVT was quickly nullified by Conservative governments. The benefits of the tax must become evident to the general public within the life of one parliament. Therefore it is crucial to ensure that the taxes abated during the transition are those which hit the poorest and the most enterprising in society, where injustice is most evident in the present system.

LVT is levied on the landowner, and it will not be possible for landlords to pass it on to their tenants. Except in very unusual circumstances, the tenant will already be paying the full rental value of the property. If the landlord tries to pass on the new tax, the tenant will simply walk away. The tax will impact on landlords and owner-occupiers.

There will be fears that some homeowners, especially pensioners, will find it difficult to pay the tax. To deal with this there could be provision for pensioners (and perhaps other homeowners on low income) to defer payments until the home is sold or re-mortgaged, or the occupants move or die. But the plight of the "little old lady forced to leave her home" should not be exaggerated. It is part of the rationale of LVT that single people occupying family-sized homes should be encouraged to move into more suitable accommodation and release the house for family use or sub-let some part of it. Nevertheless, there are a few (less than 2%) owner-occupiers in Bands E-H who are in the bottom quintile of poor households, and they might feel aggrieved.

Even though the new land tax will be offset by a decrease in other taxes, there is a continuing concern that people should not be heavily taxed on their home. To allow for this, ALTER recommends that a "Homestead Allowance" be introduced, reflecting

the fact that shelter is a basic human need. It would be analagous to the personal allowance provided for income tax payers. The allowance would be based on the land value of a very modest house in that local area.

Many US cities have introduced what they call incentive or "split-rate" taxation, where the shift from building value to site value is made gradually. This might be useful in those cases where LVT was being introduced as a local replacement for business rates on commercial sites. On residential property, council tax is such a poor tax that it would be hard to make a case for continuing it any longer than we had to.

There should be no exemption for agricultural land under LVT. Because there is so much of it (85% of Britain's land area), people from rural constituencies have often been nervous of LVT. But the value of all this land is less than 5% of the total for the UK. Any reduction in general taxation would benefit all farmers and LVT would mean more marginal land was available for new entrants. To existing tenant farmers, LVT would make no difference to their rent levels which are always at the most the farm will bear. When agricultural land was relieved of rates in the 1920s, farm rents rose to take up the slack.

All or nothing

ALTER strongly recommends that LVT should be introduced in its simplest and purest form from the start, even though it could be at a low rate. There have been many attempts in the past to capture land value in other, more complex ways. Far from succeeding, they all had adverse effects.

A Development Charge was introduced by the Labour Government in 1947 and a Betterment Levy in 1967. Both raised tax when an increase in land value was revealed by the sale or development of the site. In both cases landowners waited for a change of government to remove the levy, and the supply of land temporarily dried up. Labour tried again with the Development Land Tax in 1976. An 80% tax on development gain was merely an incentive for developers to hold back until the tax went away. More recent attempts to recover some of the developers' profits – Planning Gain or Section 106 agreements – have equally deterred what might be desirable development.

All these taxes were simply one-off attempts to recover some of the increase in value at the time of the development and, once paid, no further charges were made. There was no attempt to collect the increased value on adjacent sites, nor the historic accumulation in these and all other sites that should be paying their dues.

Even our present Liberal Democrat policy of LVT (SVR) on business land but not on residential property is fraught with problems. For instance, SVR would be immediately payable whereas residential land could stand unused and untaxed. So there would probably be a spate of commercial sites "released" for housing but not necessarily developed. Is a switch to residential use necessarily what we need? What about the interests of starter firms who would benefit from more business sites being forced into use?

Conclusion

What this chapter has shown is that LVT is a simple tax to collect, cheaper than most and, of course, impossible to avoid: land cannot be hidden. In a technical sense it is certainly easier to implement than it was a hundred years ago, thanks to the invention of the computer.

Now that we have a government in which Liberal Democrats participate, our members of that government ought to press more strongly for a major shift of the tax burden off those who create wealth and onto those who merely accumulate it. George Osborne introduced the 2010 Budget as part of the Coalition's "new model of economic growth" which would lead to "enterprise-led recovery, which rewards enterprise". In the 2002 pamphlet *Regulating Modern Capitalism*, Vince Cable used similar words, committing his Party to "a free market economy in which enterprise thrives".

For both electoral and economic reasons, it should be possible to persuade the modern Conservative Party, with its shrinking rentier-monopolist tendencies, to follow a "tax shifting" path to recovery. Coalitions within parties, as well as between them, can be shaken by profoundly disturbing events in the wider world, such as climate change and global financial meltdown. The case which ALTER presents, if taken up convincingly by our leaders in this cabinet, has the potential to frame the Liberal Democrats' identity in terms of both head and heart, for social and economic liberals. It could transform the economic and political life of the country and lead the developed world down a truly sustainable path towards progress without poverty.

Sustainable Taxation and Modern Liberalism

by Tony Vickers

Liberals need to prepare for a century of immense and unprecedented challenges to humanity on Planet Earth. This essay compares the world that faced Lloyd George's government with today's world to see what lessons can be learned in the spheres of philosophy, politics and economics. It draws on *A Liberal Theory of Natural Resource Property Rights*, a published doctoral thesis by the Harvard political economy student Joseph Mazor, which may provide the kernel of what could be the rebuilt foundation for global Liberal political action on sustainable taxation.

Lloyd George's world

When the Liberal Government came to power in 1906, manned flight was in its infancy, as were radio, electricity and the telephone. Humanity was still ignorant of many of the fruits of nature that science had yet to discover. Yet these things were part of Creation all along; their importance to us was merely undiscovered.

Henry George, in Lloyd George's formative political years, was prompted to expound on the distortions in wealth distribution which modern capitalism was exacerbating. However, to the masses in the growing franchise, economic justice was all about landlords of *terra firma*, scarcely at all about other natural resources. There was no understanding of "sustainability", nor the fragility of the planet's life support systems.

Industrial society and global trade were largely powered by coal. Other carbon fuels had little importance. Banking was mainly to support mercantilism and not personal lending for home purchase.

In the domestic political environment, perhaps the most significant change that began in Lloyd George's time concerned home ownership financed by massively increased personal debt. This has changed the dynamics within which "land taxers" must operate. Home ownership has grown from 14% to 70% of households in a century. Although many tenants in 1909 were denied a vote, Lloyd George could afford to marginalise owner-occupiers; indeed, he could sell LVT as a move towards a wider franchise, home ownership and liberty from landlordism. Today it is the asset-rich, income-poor homeowner who dictates how tax shifting can happen in Britain.

Our world

The trend towards owner-occupation may have peaked. Changes in employment patterns have contributed to a new challenging of the popular assumption that owning one's home is "a good thing". Typical first-time buyers are couples both needing to earn and to use parents' equity to raise a deposit. By the same age (35), a homeowner of my generation had paid off half his loan – the borrower was usually the man – and was sitting on equity worth two-thirds of the home's value.

Borrowing to buy anything substantial – not just a home – has become the norm in our society, totally replacing thrift. The savings culture, common up to fifty years ago, has disappeared almost entirely from native Britons. "Ownership" for most equates now to "responsibility for servicing a debt", rather than "responsibility for looking after a property". In such a culture, how can good stewardship of the planet be cultivated?

The defining moment for many millions of my generation worldwide was the first TV picture of Earth from space. The space race was significant not so much for the "giant leap for mankind", but because it allowed us to clearly see how precious, alone and vulnerable our world is. The space race was also a great stimulant to scientific discovery and engineering. It led to countless inventions that have benefited society. It allowed us to monitor from near space what we are doing to the planet. And it has brought within the domain of politics and economics numerous new aspects of nature and potential rent from resources.

Property rights: a lacuna

In this new "New World", "land" is not merely *terra firma* but has an extra-terrestrial and multi-dimensional sense. With atmospheric or microscopic "nature", it can even be invisible. The classical philosophical concepts of property rights seem inadequate today. As Mazor puts it, "liberal political theory lacks a satisfactory account of natural resource property rights".

The challenge for this century is to devise policy instruments that ensure human society shares fairly the responsibility both for managing finite and overstressed natural resources and for distributing the wealth accruing to those who exercise rights of access to their use. Whether that be the carrying capacity of oceans and atmosphere, the interconnected carbon and nitrogen cycles, the electromagnetic spectrum, aircraft landing slots and airspace, or even exploitation of the genome: land or nature is set to become far more valuable, not less.

Mazor asserts that there is "widespread liberal support for the general proposition that people have equal claims to natural resources" but divergence among liberals when it comes to ideas about how society should respect such "equal claims". Hence the lack of agreement over how to deal with property rights. He cites a wide range of "liberal" philosophers, among them Hobbes, Locke, Smith, Paine and Mill:

- Thomas Hobbes in *Leviathan*: "equal distribution is the Law of Nature", acknowledging that there are few ways yet discovered by which to achieve it, and choosing "types of lot" as the least bad, "because other means cannot be imagined".
- John Locke in *Second Treatise on Government*: labour is "self ownership" but the fruits of the earth "belong to mankind in common, initially at least" and those who appropriate them must leave to others "enough, and as good".
- Adam Smith in *Wealth of Nations*: the product of labour is "sacred and inviolable" but "land rent is naturally a monopoly price … arising from some improper form of government protection and inimical to the public good" and "no discouragement will be given to any sort of industry" by "a peculiar [i.e. special, not odd] tax on land rents", which we call LVT.
- Thomas Paine in *Agrarian Justice*: "every proprietor owes the community a ground rent for the land which he holds".
- John Stuart Mill in *Principles of Political Economy*: "It would be the height of injustice to let the gift of nature be engrossed by individuals if it were possible to clearly separate the value added by labour from the value of the earth itself".

These quotes, selected by Mazor, illustrate the limitations of classical liberal theory: firstly, the focus is very largely on land as *terra firma*; secondly, the practical political and technical constraints of the day limited the ability of thinkers to imagine either a "proper" form of government or adequate means of valuation.

Sustainable economic justice

Compared with previous centuries, "values of particular natural resources change unexpectedly" and more rapidly now. This enhances the importance of the issue of what Mazor calls "inter-generational equal division" of the rights of "Future People". However, he suggests that "problems [in devising ways to respect such rights] can be solved using modern technology" through frequent and transparent revaluation of resources and by "different length leases for different natural resources". This provides

a more comprehensive philosophical framework within which Liberals can develop policy tools to manage natural resources other than *terra firma*.

The humble parking meter illustrates how new devices for collecting rent as public revenue develop. In the 1950s, parts of cities became so congested that highway authorities were allowed to lease out roadside space – which had become very valuable – to motorists prepared to pay a charge.

Note that the whole highway remains **public**: unlike most land, it has not been privatised. No public benefit normally derives from assigning roadside space permanently to a particular person. The efficient period for "lease" of a parking slot need be not more than a few hours. Auctioning the slots would not be cost-effective to either the highway authority or the vehicle drivers.

This illustrates how a particular natural resource becomes a viable source of public revenue when all the following conditions apply:

1. scarcity, leading to competition;
2. a recognised government authority that can manage the resource;
3. an efficient, fair means of assessing and collecting the rental charge; and
4. the revenue collected exceeds the cost of assessment and collection.

Mazor considers the issue of "eminent domain", wherein the state retains residual power and responsibility, under many jurisdictions, to recover privately-owned land. He suggests, perhaps wrongly, that compensation must be paid, yet he appeals to the liberal principle of "equal claim" and believes governments have a duty to ensure that land, or any natural resource, is managed in such a way as not to impose costs on society in general, now or in the future. Taking a "long view" of economic justice, compulsory purchase is justified as a last resort if a resource has been abused or its current use causes harm.

Extending rent as revenue

Aircraft landing slots

The use of harbour pilots can be considered in part the collection of rent for use of a scarce natural resource: safe landing places. This relatively simple system for seaports was initially satisfactory for airports.

The rapid growth in market value of aircraft landing slots, which are among the main assets of airlines, has resulted from inflation in the value of time. Here the "lease" may be as short as a few minutes.

This is especially marked at hub airports, while smaller regional airports might even have to pay an airline to land. By definition, there can only be a limited number of hubs that serve the total network. Slot value at an airport differs according to day and time. It is the national and regional economy of the area surrounding a hub airport that gives it value, while massive investment – public and private – sustains it.

Governments could conduct periodic rolling auctions at individual runways or airports to establish a free market in slots. The revenue would be shared between the airport authority, local authorities nearby (to mitigate the harm caused by noise and air pollution) and governments needing to maintain air safety, immigration and customs controls. The total value of landing slots at Heathrow alone has been estimated in the region of £5bn per year.

An aircraft landing slot is really an exceptionally valuable kind of parking space. Therefore, as with the parking meter, the similarity to LVT is easy to grasp. Following the aircraft up towards the troposphere, we depart entirely from nature as *terra firma*, but we encounter two aspects of Nature that are vital to modern society, namely the electromagnetic properties of the ionosphere and the composition of the atmosphere – notably carbon and nitrogen.

Radio frequencies

The theory of electromagnetism became central to the emerging Information Society before Lloyd George died, less than 100 years after its discovery. Media moguls like Rupert Murdoch owe much of their massive fortunes to having been granted exclusive rights of access over populated parts of the globe to certain radio frequencies of the electromagnetic spectrum which have the peculiar characteristic – discovered by Marconi in 1895 – of bouncing off the ionosphere.

The ionosphere is as much "land" in the economic sense as the land site upon which Broadcasting House sits. It just so happens that the business model for broadcasting developed without governments being aware, or taking account, of any philosophical framework for ensuring that humanity as a whole – including future people – recovers its rental value.

With few exceptions (such as Gordon Brown's auction of 3G mobile phone frequencies in 2001), spectrum slots have been virtually given away to broadcasters, who can then sub-let them to programme providers at vast profit. Current government revenue from the "upstream" end of the broadcasting business, as opposed to the companies that produce programmes and their employees, is minuscule.

It ought to be possible to emulate the 3G auctions more generally. As broadcasting licences expire, frequencies should be leased by auction to the highest bidders. For as long as this is not done, other taxes have to be paid by the broadcasting industry (and others) which breach the "sacred and inviolable" product of labour, as defined by Adam Smith.

Global natural sinks

Whereas the ionosphere has, in effect, been sold off at a knockdown price, it is (we believe) resilient, unlikely to suffer physical damage from its use. In the case of the chemistry of the atmosphere and other natural "sinks" for the by-products of human activity, we cannot be so sure.

The broadcast spectrum can be leased by discrete wavebands, similar to land sites. No economic model for managing activities that impinge upon sea and air chemically yet exists. The EU's Emissions Trading Scheme may represent the birth of such a model. Signatories to the Kyoto Treaty have, in effect, signed up to creating or joining similar schemes. In the centenary year of "The People's Budget", a conference in Copenhagen in December 2009 attempted – and failed – to create a truly global carbon trading marketplace.

So what level of government can exercise the necessary authority to manage and police such a marketplace? Unlike conventional markets in commodities, the natural resource is renewable, if managed sustainably. It is the raw material of all life that is being traded.

One way to look at the problem is perhaps to treat global carbon sinks like land, which is also a natural resource that is never "used up" if managed sustainably. A "basic income" of carbon could be allocated to each member of the human population; a "fair" share of sustainable carbon emissions. The exercise could be repeated every few years as human population changes and knowledge of climate and ocean science develops. This accords with what Mazor calls the "Equal Division" principle for the allocation of all natural resources.

Conclusion

Liberals believe in devolving power to the lowest level of government consistent with ensuring equity and justice. Some natural resources are fixed and definitely "local", such as land sites. These, together with the revenue from their rent, can be assigned to particular local, regional or national jurisdictions. But for resources that cannot be contained yet are finite, existing global institutions are incapable of supplying the authority to manage them sustainably or fairly.

The biggest challenge to political scientists as much as to natural scientists in the next century is devising sustainable ways of governing the global commons. Laws that can be applied and policed globally are needed. As Mark Corner says in *Towards a Sharing of Global Sovereignty*, we need a stronger governance of the Global Natural System. The economic rents from global carbon sinks ought to be more than sufficient to finance the necessary measures, with any surplus helping to replace existing taxes on economic activity.

A new "People's Budget" will need to look well beyond *terra firma* for its revenues but land value tax will still be the best tool to use. Time is short for this new Liberal-inspired government to devise, with others globally, the necessary measures to secure massive increases in revenues from economic rent derived from natural resources.

Our Contributors

Jock Coats was once a city stockbroker and investment analyst – in the days before big bonuses! He has been a Liberal Democrat local councillor with responsibility for housing and housing policy scrutiny in Oxford and currently chairs the Oxfordshire Community Land Trust. He is a committee member of ALTER.

David Cooper is by profession an engineer, and is a Liberal Democrat activist. Since being introduced by Tony Vickers to the concept of Land Value Taxation and the works of Henry George, he has taken an active part in ALTER and is currently secretary.

Christopher Glover has a Masters in International Banking and Financial Studies. He is a Chartered Accountant with a background in Stock Exchange investment analysis and corporate finance. His work has included the valuation of a number of banks, both in this country and abroad. The fifth edition of his book *The Valuation of Unquoted Companies* has just been published. He is a committee member of ALTER.

Margaret Godden was introduced to Land Value Taxation at the School of Economic Science in the 1950s, when she was a law student at King's College, London. She has stood for the Liberal Democrats in two parliamentary elections and was Group Leader of both Oxford City and Oxfordshire County Councils. In 2004 she chaired a cross-party group which produced the Oxfordshire Study on the practicalities and likely effects of a switch from Council Tax and NNDR to LVT in a typical area of Oxfordshire. She is a committee member of ALTER.

Brian Hodgkinson qualified as a Chartered Accountant before taking an Oxford PPE degree. He lectured in Philosophy at Sussex University, and later taught Economics and History. In addition to editing an Economics journal, he has published four books, including *A New Model of the Economy* (Shepheard Walwyn), which introduces land into economic theory. Brian is a member of the committee of ALTER.

Catherine Hodgkinson (née Stratton) was educated at University College, Swansea, where she was chair of the Liberal Society. After university, she trained as an investment analyst and became a member of the London Stock Exchange in 1975. She left the City in 1992 to work as an independent research analyst/consultant in the Plant Hire sector. Catherine is a Fellow of the Securities Institute. She served as a Liberal member on Hammersmith Borough Council from 1975 to 1978 and more recently was a Lib Dem member of Oxford City Council for four years. She is Treasurer of ALTER.

John Howell went to St Paul's School, from which he won a scholarship to Clare College, Cambridge, gaining an Honours degree in Geography. He then went into teaching and for the next 35 years worked in various colleges and independent schools in London. He has been a lifelong supporter of LVT. He recalls his difficulty as a student in trying to reconcile the many contradictions of conventional economic thought, and vividly remembers how these were resolved by the concept of economic rent as the natural source of public revenue. John is a member of the ALTER committee.

*__Geoffrey Lee__ was one of the authors of a major work on world trade, and for many years worked on yearbooks for the *Financial Times*. The author of many short stories and articles in the national press, he became assistant editor of an architectural magazine and then deputy editor of *Country Life*. In retirement he worked for the Historic Houses Association.

*__Duncan Pickard__ was born and raised on a dairy and sheep farm in Lancashire. He followed an academic career which included a lectureship in Animal Physiology and Nutrition at the University of Leeds until 1990. The Pickard family moved to Fife in 1992, having bought a 600 acre farm. Currently they contract farm an additional 700 acres. The main enterprises are cereals, field vegetables, beef cattle and sheep. Dr Pickard is the author of *Lie of the Land*, published in 2004, and has been a member of the Henry George Foundation for more than 30 years.

Tony Vickers is a lifelong Liberal, chartered land surveyor, land policy researcher and part-time lecturer at Kingston University, where he completed a doctoral thesis on Land Value Mapping. He worked for speculative housing developers before becoming a Royal Engineers officer in 1976, serving in Military Survey for 14 years until 1995, when he resumed active politics. He has been a Liberal Democrat councillor in West Berkshire and Chair of ALTER for most of the last 15 years, stood for Parliament twice and been policy officer of two national charities. He was a member of the Party's Tax Commission and is author of *Location Matters*, an introduction to modern LVT.

**These authors are not members of ALTER and we are especially grateful to them for their contributions to this publication.*