Land Rent in a Tax-free Economy

Outline of remarks by Mason Gaffney, for use at Moscow Congress, 5/21/96

1. Rents are a taxable surplus. I estimate that this taxable surplus constitutes 35% or more of the national income in most nations with market economies, and more in resource-rich nations.

What is rent? Marx and market economists define it much the same. Marx spells it out in *Das Kapital* (Vol. III, Part VI, Chap. 46-47). In simple feudal conditions, the whole of surplus value is rent. Under capitalism, an industrial landowner gets a "surplus profit" above the cost of capital; location exerts the "overwhelming influence"; the landowner is "passive … contributes nothing and … risks nothing, unlike the industrial capitalist." Rent for housing land is "tribute for the permission of inhabiting the earth." "Space [is] required as an element of all production and all human activity." In urban industry, to increase production "demands also an extension of the land area."

Marx continues, one can distinguish house value from land value. House and land are often even "owned by different persons." Growth of capital "necessarily raises rent" (while it lowers rates of profit on capital). "[Land], not the house … forms the actual object of building speculation in rapidly growing cities." Machinery and other capital wear out, "but the soil, if properly treated, improves all the time." Marx calls for a "Trinitarian Formula": capital; land; labor.

In mining, rent comes from the low-cost mines, because they sell their product at the same price as the high-cost mines. In all fields, high product prices are "converted into ground-rent and … fall into the hands of the landlord," concludes Marx.

2. The value of rent is huge. Every economy produces a large excess over wages. To be sure, not all of it is surplus. Some of it goes to replace capital that wears out each year. This is not part of the net surplus, nor income to the capitalist; it is a return *of* capital.

Second, some goes as a return *to* capital, over replacement. This is pure income. Income to capital is not a taxable surplus, but a functional incentive: it moves people to form and supply capital. This entails securing new capital (by saving, and borrowing) and conserving old capital (avoiding dissaving, and avoiding export of capital).

Capital income serves another useful function: it steers capital into the most productive uses. Steering capital to its best uses has the same useful function as securing new capital, and conserving old. Using capital effectively is as beneficial as securing more capital, and ever so much cheaper. The Great Transition in Russia now is learning to allow income on capital, to secure these benefits. The trick is to do it without allowing more than is needed.

The rest of the excess over wages is captured in the rent of land. It is a true taxable surplus. The amount is already huge, and will become huger yet when existing taxes are abated.

The size of rent is not reported in capitalist nations, except to trivialize it. Their national accountants, dominated by landowners, neglect or conceal it artfully, to protect it from being taxed. Local governments do, however, measure and tax property by value. More than half the value of property is land. In Vancouver, B.C., 73% of the value of all property assessed for taxation is land, even though much land there is exempt from tax, and not assessed at all. In California's major cities it would be just as high if only we assessed land here as accurately as they do there.

3. Rent will become huger yet when you abate taxes presently levied on production and exchange, because these now depress the rent of land. That is, in a tax-free market economy, the benefit of abating present taxes will lodge mainly in land rents. The taxable surplus simply shifts from one form to another.

This is more than a simple shift of a fixed amount. When you substitute land revenues for existing taxes, the surplus actually grows, as if by synergy. You gain more revenue base than you lose, because existing taxes now suppress much latent production. Payroll taxes directly drive workers from taxable jobs to untaxed gains from crime. Abating those taxes will unleash suppressed economic giants, along with all the new surplus values their latent production will generate. "Monetarists" warn you that "there are no free lunches." In fact, however, good policy creates lots of "free lunches." It makes the whole greater than the sum of its parts. Imagine the benefits, alone, of turning people from destructive careers in crime to useful jobs producing goods.

At the same time, the effect of socializing land revenues is to stimulate better land use—the opposite of the effect of existing taxes. Every landowner, to pay the required land charge, is pushed to steer his land to the best use (just as paying interest steers capital to its best use). Thus, the shift to rent-based revenues doubly induces new production: it releases the brake of present taxes, and replaces it with an added push to produce. This is "supply-side economic policy" in the best and truest sense. It generates yet more surplus. You may take all of rent to support government functions, without damaging private market incentives, but only sharpening them.

This policy lets us achieve and reconcile two policies that many now believe are incompatible, viz.: free markets and common rights in land. It is a kind of miracle, yet simple to understand and implement. Monetarist advisers would bind you in a dilemma: they claim you must choose between private markets and common rights. In fact, you may have both at once. Public revenue is simply the kind of socialization that occurs in a market economy. Socialize the rent of land and you socialize the net benefits of owning land, even while privatizing the management of land, and gaining the benefits of using free markets.

The combined effect of all this stimulus would be a burst of growth such as few economies have ever shown, except in wartime. We learned in the United States in World War II the astounding effects of simply taking the brakes off production. U.S. GNP doubled from 1941 to 1943; all willing workers were fully employed. This same miracle can occur in Russia, 1996 to 1998. The natural resources and human talent are here: you only need the right incentive structure to turn labor from idleness and crime to producing goods and services.

4. Some of the benefit of abating existing taxes will lodge in higher after-tax wage rates, rather than higher rents. For the present and near future, however, the supply of labor in Russia is highly elastic because so many potential workers are now unemployed, or underemployed, or occupied in crime. In this condition, raising demand for labor will raise payrolls by raising the number of good jobs, more than by raising wage rates. On balance, therefore, this effect on jobs will create new rents, more than it cuts into old ones. After Russia shall have achieved full employment, wage rates may rise and cut into the surplus of land rents, but if this should then create a new kind of problem (which I doubt), it is more pleasant, and easier to solve, than those that afflict you now.

5. Many varieties of natural resources generate rents. City land is the greatest single source. For example, one city, Vancouver, contains half the value of taxable property in B.C.—a province of 934,000 square kilometers, or 70% larger than France.

However, many other resources yield rents. Some of them are also huge in value, even though some are inconspicuous. Here are a few varieties of them: access points to transportation (by water, rail, highway, air, etc.); clean air (or the license to pollute it); aircraft time slots and gates in airports; amenities (good views, warm weather, soft breezes, freedom from pests, riparian access, etc.); aquifers; dam and reservoir sites; water in arid zones; rights-of-way; preferential use of "common" lands (e.g., street parking in New York); covenants over lands of others (e.g., covenants against competition); easements (e.g., the right to pass over land); fisheries; forests; franchises (exclusive right to sell in certain areas); the gene pool; geothermal energy; grazing; licenses; minerals and gas (rent includes the rise of value of minerals *in situ*); orbits; some patents (giving effective control over minerals); ability to wield political influence (meetings at private estates; special voting rights); foreign holdings and ocean shipping routes protected by national forces; soils; spectrum (radio, TV, communications); legal standing; strata rights; space on the streets; advertising sites; water; wildlife (for hunting, viewing, etc.); wind (for power); zoning permissions; etc.

Some of those varied resources are highly valued. For example, newly minted fishing permits offshore of Washington State sell for $1 million @. Their owners retire and rent the permits to working fishermen, creating an instant class structure where before there was equal opportunity. Imagine the value of an exclusive right to take Caspian sturgeon. Radio spectrum amassed by the McCaw Company recently passed to AT&T for $13 billion. Dmitri Lvov estimates that your oil and gas revenues alone could support the entire national government (*Practicable Course of Economic Reforms in Russia*. Moscow: Russian Academy of Sciences, Central Economics and Mathematics Institute, 1994). They might even surpass urban rents in value, if they were valued at world market prices. In arid lands, access to water is life itself.

You may measure rents that these different varieties of resources generate, once their products sell in markets that tell you their true value. As mentioned, when we restricted fishing rights to those with licenses, licensees immediately began renting them out, creating a market price. If there is a market for logs, you may estimate the value of forests from which they come, using the "netback" technique. There is already an active world market for radio spectrum—and the price is very high, so do not neglect it. There is a world market for mineral leases to produce oil and gas. It is shark infested, so enter it carefully, but there are hundreds of experts to advise you how to get your fair share from the minerals you own, and prosper like the sheikhs of the Persian Gulf or, better, like the ordinary people of Alaska, Alberta, the Netherlands, or Norway.

A challenge for Russian science and statecraft is how best to tap for public use or equal distribution all these varied rent sources. Each poses its own technical problems. Once you commit to pricing resources in free and world markets, however, markets generate the price data needed to measure taxable surpluses that each kind of resource generates. The Russian people, who spawned so many world-class composers, writers, and scientists, who turned back Hitler, and launched the first Sputnik, obviously have talent, industry, courage, and ability to organize and govern. It is a matter of bringing these virtues to bear on the question at hand.