

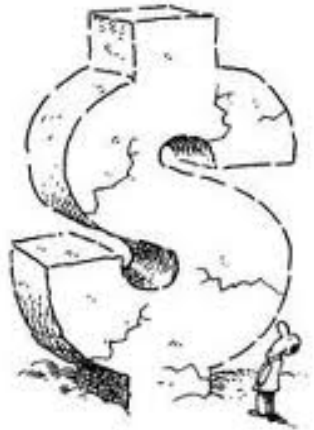


THE LIBERAL DEMOCRATS

# ALTER

ACTION FOR LAND TAXATION & ECONOMIC REFORM

## **LAND VALUE TAX AND THE FISCAL CRISIS**



The economic problems that confront the Coalition Government may be summarised in the form of a painful dilemma. The budget deficit is enormous, requiring huge amounts of borrowing to add to the existing vast level of public indebtedness. The deficit clearly is a function of the relative volumes of government revenue and government expenditure. Therefore the dilemma is either to raise more revenue or to cut expenditure (or, of course, a combination of both). In view of the high level of taxation inherited from the Labour Government, the Coalition has decided, not unreasonably, to concentrate on cutting expenditure.

What is perhaps less reasonable is the level of the proposed cuts and where they may fall. 25% reductions in most spending departments within five years – even 40% was mooted – will have a damaging impact on many vital services. Ring-

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fencing of the NHS is now in doubt. Moreover, all cuts have a secondary effect through the multiplier that leads to a reduction in spending by those whose incomes are initially reduced, and so on. Worse still, the impact cannot be uniform throughout the economy. Regions like the North East and South Wales suffer more than most, since they are heavily dependent on public expenditure for employment.

In view of this, should the Coalition have chosen the other alternative of substantially raising revenue? How might they have done this? Under the existing tax regime virtually all taxes inhibit production. This is not just because taxes deter people from earning more by work or enterprise. It is also because income tax, national insurance, VAT and the rest punish the margins of production, the marginal areas of the country, the marginal firms just breaking even, and also the marginal output of all firms, including the largest and most productive ones. Hence the Coalition was right not to raise existing taxes by very much.

Does this leave no alternative but the one chosen i.e. massive expenditure cuts? Not at all. The clue to avoiding the basic fiscal dilemma lies in understanding what has been said about the margin of production. Taxation should fall on non-marginal sources of output. Economic analysis since David Ricardo has taught that non-marginal value is primarily economic rent. By definition this rent is the excess of value produced over the value produced on the margin. What is the principal source of this rent? It is land.

Land value is far and away the greatest untapped source available as public revenue.

The moral case for taxing it is unanswerable. It is created by the presence of natural resources, by the work of the whole community and by the provision of public services. No individual or firm has any moral right to receive it. Yet a relatively small minority do receive it, often in the form of colossal increases in the capital value of the land to which they lay claim.

The only reasonable conclusion is that tax should be collected from the economic rent of land. This has long been a serious proposal of Liberals from Campbell-Bannerman and Lloyd George to at least one member of the current Cabinet. Much research has established that the best method is by a Land Value Tax. It could be introduced as a substitute for council tax, or better still in place of major national taxes. This is the main recommendation of ALTER.

LVT is not just a useful additional tax. It is essential that it becomes a means of reducing other taxes that hit production by taxing the margin. Thereby a stimulus to produce would benefit the whole economy, in particular entrepreneurs and workers, whilst rentiers who live off the production of others would take on the justifiable burden.

Such a tax shift would take time to haul the Treasury out of the horrendous pit into which it has been allowed to fall. But the process would be entirely restorative. Expenditure need only be cut where genuine inefficiencies are found. It would also fall when new jobs were created and unemployment reduced. A virtuous circle of higher output and greater revenue from rising land rents would replace the vicious circle of lower output from higher existing taxes and heavy expenditure cuts. LVT creates a balanced economy of producers freed from taxes and non-producing rentiers yielding public revenue.

There are important side effects of introducing LVT. Just one that is relevant to the fiscal issue may be mentioned. The capital value of all land would fall under LVT. This would be gradual, but it would ease the problem of excessive bank lending for land purchases, whether in the form of speculative property developments or home mortgages. Since these were the root cause of the economic crisis, this would give the new fiscal regime a sure monetary foundation on which to advance. It is time for radical alternatives to be tried. LVT is the one with by far the best credentials.

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One of a series of LVT information sheets, editor D Cooper ©ALTER MMX  
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