TAX JUSTICE FOCUS

The newsletter of the tax justice network

A TOOL FOR ECONOMIC DEVELOPMENT

A land value tax is a periodic tax (monthly or yearly) on those who have title to land, levied in proportion to the value that the land would have if it were not improved. A land value tax reflects the value that is added to land by public improvements such as streets, water service, sewers, parks, etc., but not the value of structures, fences, grading, draining or other improvements to an individual parcel of land.

Land value taxation promotes economic development in at least six different ways. First, land value taxation serves as a regular reminder to those who have title to land that they are not using, that they have something of value that could be put to use. Land is often in the hands of people who have other concerns and prefer not to think about what might be done with their land. A regularly recurring tax bill reminds people that they have something of this and if they have no use for their land themselves, they could save on their taxes by transferring the land to someone else. By putting land in the hands of people who will use it, such transfers of land promote economic development.

Second, land value taxation provides revenue for governments, permitting them to reduce taxes that have harmful effects on economic development. Taxes on wages discourage people from working. Taxes on saving or investments discourage people from saving and investing. Sales taxes and value added taxes

A key to funding transport infrastructure like Delhi's new underground? (photo: John Christensen)

TAXING NATURAL RENTS
VOLUME 6, NUMBER 1

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Political Economy of Taxation

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discourage productive activity generally. But a tax on land values does not discourage any productive activity. Thus any substitution of a tax on land value for a tax on wages, incomes, savings, sales or value added will increase the efficiency of an economy and promote economic development.

Third, land value taxation reduces the profit from land speculation. Land speculators leave land unused because they think its value will rise rapidly, so it should not be improved now. These expectations of speculators are often disappointed. Valuable land in the centres of cities is often left unused or very poorly used for generations. The inefficient decisions of land speculators to not develop land mean that economies must contend with artificial scarcities of land. When a tax on land value is implemented or increased, the potential profit from land speculation falls. Regular tax bills limit the capacity of speculators to speculate. As a result, less land remains in the hand of speculators and more land goes into the hands of those who wish to use it. With more land in the hands of those who wish to use it, economic development improves.

Fourth, land value taxation provides a special benefit to those who have limited access to capital, and in the process it promotes economic development. Other things being equal, when the tax rate applied to land value is increased, people who might want to buy land will reduce their offers according to the present discounted value of the increase in taxes. But every potential investor will use his own interest rate in determining the amount by which to lower his or her offering price in response to an increase in the rate of a land value tax. Those who have high discount rates will have lower present discounted values for future taxes, and will therefore have smaller reductions in the prices that they will offer for land, compared to those who face low interest rates and therefore have high present discounted values for future taxes. Thus a tax on land value will tend to move land from those who have low discount rates to those who have high discount rates. And those who have high discount rates (those with limited access to capital) tend to get returns on their assets that reflect those discount rates. Thus land value taxation puts land in the hands of those who do more with it, thereby promoting economic development.

"When a tax on land value is implemented or increased, the potential profit from land speculation falls"

Fifth, land value taxation has a particular capacity to finance infrastructure improvements such as road paving, bridges, water lines, and sewers. An infrastructure improvement is worthwhile if its benefits are greater than its costs. Because of the mobility of labour and capital and the fact that benefits of infrastructure tend to be limited to the vicinity of the infrastructure, the benefits of infrastructure tend to be reflected in increases in the rental value of the land in the vicinity of the infrastructure. This means that financing infrastructure by a tax on the land in the vicinity of the infrastructure has three important benefits.

"Any substitution of a tax on land value for a tax on wages, incomes, savings, sales or value added will increase the efficiency of an economy and promote economic development"

1. When infrastructure is financed by taxes on land there is no dead-weight loss from the taxes as there would be with most other sources of financing.

2. When infrastructure is financed by a tax on land in the vicinity of the infrastructure, assessed so as to reflect the increase in the value of the land that is caused by the infrastructure, no one is harmed by the decision to produce the infrastructure. Everyone is a net beneficiary. Even if the tax cannot be assessed so perfectly that no one is harmed, the effort to assess the costs according to the benefits to owners of land greatly reduces the extent to which net harm to individuals is caused by the taxes that finance infrastructure.

3. By financing infrastructure through taxes on those who will benefit from the infrastructure, land taxes avoid the problem of efforts by beneficiaries to persuade governments to provide infrastructure that is not actually worthwhile. When the beneficiaries are the ones who will pay for infrastructure, they have an incentive to push the government to provide the infrastructure only when it actually is worthwhile.

The sixth way that land value taxation promotes economic development is by generating confidence in governments. Economic development is often financed by foreign investment, and foreign investors ask themselves, before investing, how confident they can be that they will not lose their investments as a result of confiscatory taxes or regulations. Potential domestic investors will also ask themselves whether, considering the risk of confiscatory government action, they would achieve higher expected returns with investments abroad than with domestic investments.

There may be no way that a government can provide an absolute assurance that no future government will confiscate investments, but a government can provide evidence of responsible planning for a future that does not require confiscating investments. By collecting the rent of land and using it for public purposes, a government can provide a signal that it plans to provide for its future revenue needs without having to confiscate the capital that investors bring to the country. Thus in this way too, a tax on land value promotes economic development.

Nicolaus Tideman is Professor of Economics at Virginia Polytechnic Institute and State University

NATURAL RENTS

editorial

Carol Wilcox

The argument for land rent as a primary source of revenue has become marginalised -- though no coherent argument against land value taxation exists. Land rent is the natural source of public revenue.

Where there is concentrated landownership, the surplus from agriculture is scooped by the landowner, with the bare minimum paid to labour. Since political power universally resides in landownership, it is hardly surprising that as wages have increased due to economic development, landowners have been able to ensure that the main tax burden shifts not onto them, but onto labour.

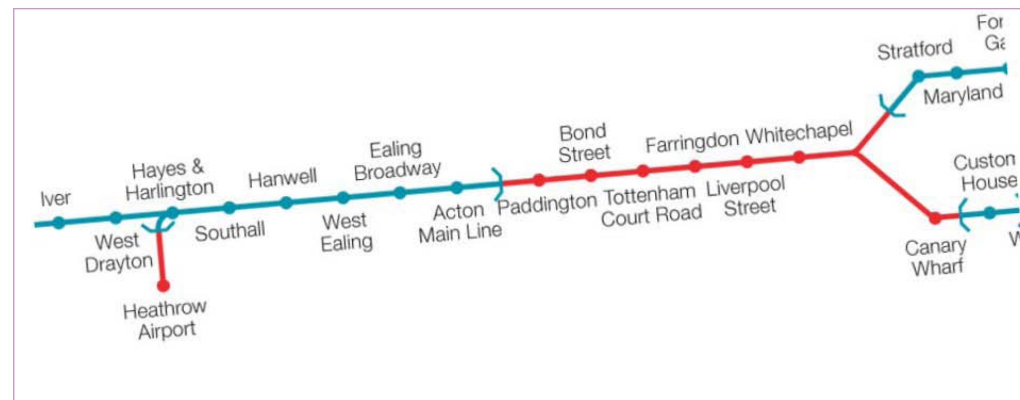
In classical economics, land is defined as one of the three factors of production, along with labour and capital. Economics text books tend to play down the subject. You will read that land consists of location -- the ground you walk on, and the permanent physical space and airwaves below and above it – and natural resources. Economists also recognise land's unique characteristics: that it has no cost of production, and it is in fixed supply. As Will Rogers, American humorist, put it, "Buy land. They ain't making any more of it." Land is different.

What is omitted, however, is a special attribute of land's location aspect. Although it is a scarce resource with alternative uses, it can be used continuously without requiring maintenance or, ultimately, being consumed, unlike its embedded natural resources. So idle land for which there is a demand represents a permanent loss to production, similar to the waste of labour when there is involuntary unemployment.

Wherever you look around the globe, under whatever political system, land is not allocated to its best use: just look at urban housing problems, for example. A well functioning land market should therefore be an important objective of any economic system.

The Public Revenue Problem

The main purpose of tax has always been to raise revenue for public goods and services (or, sadly, wars). Governments are hungry for revenues, and they generally slap on a tax wherever practical. Some taxes have overt secondary purposes: to reprice goods and services where there are significant externalities, or to redistribute wealth and income.



The £16 billion Crossrail project in London will provide massive windfall gains to the City, through higher property prices. With an LVT, the beneficiaries would pay for it, letting other British taxpayers off the hook. British land is distributed more unequally than in Brazil, where 1 per cent of the population owns 49 per cent of the land. In the UK, 0.3 per cent owns 69 per cent.

Well known criteria for a good tax system include fairness, affordability, minimal cost and ease of collection, certainty, transparency, and flexibility.

Direct taxes, which are taxes on the returns to the factors of production, usually provide the main tax base, even though it could be said that taxing labour and capital discourages wealth creation. But as the global economy has expanded, capital has become increasingly mobile and thus harder to tax. This has provoked a shift towards taxes on labour and indirect taxes, such as consumption taxes, which bear more heavily on the poor.

It is strange that treasuries have tended not to recognise the return to land -- rent -- as a direct tax source, when land is totally immobile. Direct taxes on land, where they exist at all, tend to be lightly applied and do not raise significant revenues.

Indirect taxes on land are more popular with governments, in the form of property taxes, which are hard to avoid. An ad valorem tax on residential property paid by

"as wages have increased due to economic development, landowners have been able to ensure that the main tax burden shifts not onto them, but onto labour"

owners is in effect a wealth tax – probably the only effective one of its kind. However, it is nonsensical for businesses to pay a tax on buildings, which require constant maintenance, and then receive tax reliefs on those maintenance costs.

Where there are tenant farmers on agricultural land, the landowner collects the surplus for doing nothing. Consider European Union subsidies paid per hectare under the Common Agricultural Policy. Although the subsidies are paid directly to the tenant farmer, the result is that the value of the land rises commensurately; and the landowner effectively captures the subsidy by using the greater land value to extract higher rents from the tenant farmer. Tax the farmland, and you tax the landowner.

The Inequality Problem

Inequality of both income and wealth within and between countries is a major concern. As the International Union for Land Value Taxation **notes**:

> *"Religion, philosophy, and other aspects of the major civilizations have always recognized that land is every human being's birthright. Society used to ensure that people had enough land for shelter and subsistence. Even slave owners and so-called noblemen who ruled over serfs, for all their indifference to freedom, recognized that a hungry vassal was not a productive worker. But gradually individual greed for land as a sign of power, as a way to become richer through speculation, and even as pastures for animals instead of residences for people (as in the case of British landlords over Irish peasants, or other examples of colonialism) led to privatization – usurpation – of the commons, the land originally provided by communities for their people, including the poor, for subsistence farming and wood gathering."*

The Boom/Bust Problem

The 2008 credit crunch had its origins in triple-A-rated mortgage-backed collateralised debt obligations which turned out to be junk. The trigger was, as always, an explosion of credit availability, but loose money makes its way inevitably towards landed property.

As land values soared, professional property speculators pocketed their windfall gains, and banks filled their coffers with ever increasing mortgage receipts - they were, in fact, collecting the rent.

Some pundits said that the property price bubble could have been pricked by raising interest rates. This may indeed have curbed the boom but it would also have halted general growth and precipitated the bust. A land value tax, by contrast, would have tempered the boom and redirected savings towards productive, rather than speculative, activities.

Conclusion

Global economic problems do not have simple causes or remedies, and land value taxation is not a panacea. Our movement does claim, however, that LVT meets all the criteria for a good tax: it will correct land market failures; raise large revenues; redistribute wealth; and stop the creation of property price bubbles. Land value taxation should be part of every good tax system.

In this edition, members of the international land value tax movement present their arguments for the annual collection of land rent for public benefit, as prescribed by the 19th century social philosopher, Henry George.

In our lead article **Nic Tideman** presents LVT as a tool for development. Poor countries have generally low land values so LVT is not commonly considered as a useful instrument for raising government revenues. Nic describes the mechanism whereby LVT can trigger a virtuous circle of increasing land values and revenues.

Henry Law discusses how LVT might be introduced. One of the main objections to LVT seems to be that it is impracticable, particularly that the valuation process is problematic. As can be seen below LVT has already been successfully implemented and land value assessment is becoming a simpler task with the development of improved software and other tools.

Molly Scott Cato then presents LVT as a green tax. Ever since value slipped its attachment to the natural world—around when fractional reserve banking was invented in the 17th century—money has become increasingly important, and the planet and its resources less so. To find solutions to the financial crisis and the environmental crisis, she argues, we must get our feet back on the ground.

Finally, **Joshua Vincent** describes the LVT experience in Pennsylvania and presents some interesting data. The split-rate taxes levied in Pennsylvania are probably the best documented applications of LVT in practice. In fact only a small portion of rent is collected in this way, which some say is insufficient to show the effects.

This edition also covers news of the recently issued Nairobi Declaration on Tax and Development, plus details of a forthcoming conference on the Political Economy of Taxation at Loughborough University, UK, in September 2010, a review of an IMF paper looking at the role of tax distortions and tax havens in the build-up of debt in financial systems around the world, and finally an invitation to support a documentary drama film.

Carol Wilcox is Secretary of the Labour Land Campaign

feature

A TAX THAT IS NOT A TAX

Henry Law

Land Value Tax (LVT) is not a tax, but a payment for actual benefits received, just as the charge for a parking space is a payment for a benefit. It is the collection of part of the annual rental value of land. It is not a charge on the selling price of land, or the sale of land.

Street traders and buskers understand rental value. In most cities a busker will earn more in a busy railway station in the city centre, than at the end of the line, where nobody would bother to set up their pitch. Somewhere in between, the reward makes it just worth while. These latter locations are the "marginal sites". The additional earnings on the better sites, over and above the margin, owe nothing to the skill of the musician. This is rental value, due to the benefits of location, economic rent. The more people that pass by, the higher the takings. The differences are due to the shape of the transport system and other local features – in other words, to the presence and activities of the community.

Buskers instinctively understand the phenomenon of economic rent, which was analysed by the economist David Ricardo when he formulated his Law of Rent. It applies universally but is largely absent from economic theory. Perhaps economics students should be sent busking or should operate a market stall for their first course assignment! Ricardo's Law means that LVT – the collection and use of the economic rent of rent as public revenue – is not a tax but a payment for benefits received.

"Buskers instinctively understand the phenomenon of economic rent"

The benefit principle

What are these benefits? The legal recognition, protection and defence of the owner's right of occupation, and the advantages enjoyed by the owner due to the presence and activities of the community, that give rise to the rental value. This rent will inevitably end up in someone's pocket. If it is not collected as public revenue or by a landlord, it will be farmed by extortionists or fought over.

Land rent as public revenue

Using land rent as public revenue has many advantages. It cannot be evaded or avoided.

Perfect pitch: busker at Oxford Circus, Central London

Parasitic speculation in the price of land titles becomes pointless, since land holding carries a liability to pay a charge proportionate to its actual present value. It inhibits corruption of the banking system through the trading of land titles, with consequential damage to the economy through boom-bust cycles.

Most of the so-called "obscene earnings" received by financial entrepreneurs are not earnings at all, since no labour has been applied and no wealth has been created. They consist either of profits made from the trading of land titles, usually concealed inside "assets" such as shares or property, or of land rent extracted by the financial system as interest charges on loans for the purchase of land titles: economic rent capitalised.

Under an LVT regime it is no longer possible to tap into this revenue stream. Income can only arise from wealth creation. The incomes that are diverted to tax havens are collected at source. Tax havens no longer have a purpose.

"In most countries, the lion's share of the most valuable areas of city centres is concentrated in the hands of a tiny elite of landowners. This gives rise to great political influence, working quietly in the background."

How much?

How much can be raised? In many countries, both in the developed and the developing world, land rent is being collected as public revenue today through property taxes in some shape or form. Their usual defect is the method of assessment: improvements are penalised, under-used land is not assessed at its potential value, and vacant and agricultural land is exempt. In Greece, for instance, buildings are left unfinished so as to avoid the tax. Even a simple switch from existing property taxes to LVT would therefore raise more revenue. And since the reduction of existing taxes would tend to drive up land rental values, a benign cycle would be set up in which the LVT tax base grew as existing taxes were phased out.

How might LVT be introduced

So long as some form of property tax is in place, a smooth and uncontentious transition to LVT is possible. There is no practical difficulty in carrying out a valuation of land and producing a set of rental values for all land. The land has to be registered, but there are many ways of getting this done. Owners could simply be required to register their property. There is no practical difficulty in collecting the revenue using the existing administrative apparatus.

In Year One of LVT, the LVT charge is levied on occupiers, based on the land value assessment instead of the present property tax. Nothing else changes. The total amounts raised can be set so that, perhaps, just over half of all bills are the same or less than in the final year of the old property tax. That will raise more revenue and minimise protests. In the case of business and agricultural premises, where leases are often subject to an upwards-only rent revision clause, introduction of the tax must be accompanied by a regulation setting aside this clause, which is in any case fundamentally unjust, so that tenants can if necessary renegotiate their rents downwards as well as upwards.

In some countries, the property tax is local rather than national. But LVT cannot be a local tax except for the first few years, when the rate is low and before significant cuts have been made in other taxes. Some administrative areas have, in aggregate, high land values and a solid land value tax base. Others have little. This is true of all taxes at a local level: the amount that can be raised depends on the area. The land value charge should therefore, over a few years, move to a uniform national levy.

If local authorities do not have access to the land value in their area as a tax base, how can services provided by local government be paid for? One possibility is a capitation payment distributed from the national LVT fund, with the local body receiving a pot of money to spend as they wish.

The real difficulties are political. Vested interests are powerful. In most countries, the lion's share of the most valuable areas of city centres is concentrated in the hands of a tiny elite of landowners. This gives rise to great political influence, working quietly in the background.

Objections also come from those who ought to be supportive. It seems to have arisen out of the concept of 'Rent of Talent', a notion that emerged around the start of the last century. It cast a fog of confusion over the term 'Rent'. The talents in question were those of opera singers or today's football stars. The argument goes that if land rent should be taxed, so should natural talent, thereby opening up the case for progressive income taxes. This helped the landowning interest by diverting attention from their privileged status. But 'rent' is the wrong term for the high earnings of opera singers. These are the rewards for labour: wages.

Always, the aim should be, above all, justice, and to promote the efficient use of resources, good behaviour rather than bad and reduce opportunities for fraud. LVT is a tax reform that achieves all of these.

Henry Law is a member of the Land Value Taxation Campaign

HARNESSING LAND VALUE AS A GREEN TAX

feature

Molly Scott Cato

The sense of vertigo you experience when trying to understand how financial alchemists have created so much meaningless monetary value out of thin air is an indication of the dislocation that financialisation has brought to the world economy. One reason why the regulators did not do their job was that the process of debt creation was alienating: it was technical and abstract and human minds are repelled by such stuff.

The growth logic is driving the planet to destruction (photo: John Christensen)

Ever since value slipped its attachment to the natural world—around the time the technique of fractional reserve banking was invented in the 17th century—money has become increasingly important and the planet and its resources less so. The early economic theorists - who called themselves Physiocrats - stated in their name their view that the land was the source of all value. But they were defeated by the mercantilists and then by classical economists, who argued that trade was what really mattered: it was trade that enabled the accumulation of money. Since that time economists have not been able to distinguish between money, wealth and value.

To find solutions to the financial crisis, as well as the environmental crisis, we need to get our feet back on the ground.

Whose Land is it Anyway?

From the perspective of a green economist, land is the primary source of all value; the nature of its allocation is therefore an issue of great political salience. This raises critical questions concerning the legal origin of a right to own land. In indigenous societies it would be considered blasphemous to make such a claim and even the notoriously legalistic Roman Empire had a law of *usufruct* that established the right of local people to make use of land if the landowner was not doing so. How many farmers who live from grants and subsidies would be able to justify their right to continued use of their land under such a legal stricture?

Behind these laws and customs lies the fundamental understanding within human communities of the inevitability of land as a common resource—how could something so fundamental to survival pass in perpetuity into the hands of a minority? The history of the alienation of peasants from their land during the Enclosures in England is well known although, unlike the Highland Clearances, it is not burnished with the same continuing sense of injustice. It should be. Because the lowland clearances that removed subsistence farmers from their livelihood opened the way for over-exploitation and species holocaust. Neeson (1989) even argues that the disruption of this ancient way of life led to the population explosion that caused such distress to Malthus and the economists who followed his path.

It is interesting that this year's Swedish Bank Prize (in spite of attempts by the economics profession to delude us to the contrary it is *not* a Nobel Prize) was given to a woman who is not an economist and has spent her life studying systems of allocation by commons. Elinor Ostrom's citation—'for her analysis of economic governance, especially the commons'—might be a hint that even in

"The early economic theorists – who called themselves Physiocrats – stated in their name their view that the land was the source of all value"

the higher realms of what Hazel Henderson called the snake-oil priesthood there are uneasy feelings that the private-property free-for-all may have gone a little too far.

The horrifying levels of inequality that have resulted from 30 years of neoliberalism have pushed the issue of redistribution up the political agenda. But the failure of the redistributive measures, despite their vast expense, to solve the problem of persistent poverty makes clear the inefficiency of solutions that rely on redistribution rather than the predistribution that green economists have long been arguing for. Land redistribution is one such means of predistribution, but introducing a tax on those who currently own land so that the value they derive from it could be fairly shared is another. From a radical perspective, land is a common source of wealth for the inhabitants of a nation, and should therefore be shared fairly between them. Taxing owners of land and distributing the receipts to those who do not own would be a crucial aspect of predistribution.

Land in a Sustainable Economy

These are not new arguments but what gives them added salience is the limit and pressure for change exerted by climate change. No longer can we rely on the production of food and its transport across the globe to feed our families. Climate change brings irregular harvests and rising food prices; it limits the amount of carbon we can waste in pointless food swaps; and it undermines the security of the infrastructure that a global food market relies on. No wonder that food security is the political issue of the moment.

As food becomes scarcer and more expensive the exclusive ownership of land becomes an increasingly indefensible privilege. Unless we find a way of treating the world's productive land as a common good the 21st century is going to degenerate into an era of food and other resource wars. This is why the virtual money that was created in the casino economy during the bubble was invested in land before it burst. The buying up of huge tracts of land in the poorer countries of the world that has become known as 'the great land grab' illustrates how, although the money was created by a computer, its power in the world is real.

Green economists argue for an economy that is just and sustainable, but such a world is not attainable without a reallocation, occupation or requisitioning of land. At the policy level we might suggest the immediate introduction of a Land Value Tax, which would require those currently in ownership of land to pay for this privilege. The value of land ownership could then be shared between the people of each nation or region—a policy response to Gerard Winstanley's definition of land as 'a common treasury'. Far from Hardin's empirically ungrounded critique of commons (1968), Neeson's account demonstrates how the best means of protecting a resource is to reconnect use-rights with shared ownership rights, backed up by a system of local social control. Being dependent on a resource emerges as a better protection than legalistic property rights.

It is money that has got us into this mess. The abstract nature of money has facilitated our dislocation and disembedding from the planet so that we can get more excited about an iPad than a squirrel or our own best friend. And it is the growth logic that is inherent in the way money is created under capitalism that is driving the planet to destruction.

"The buying up of huge tracts of land in the poorer countries of the world that has become known as 'the great land grab' illustrates how, although the money was created by a computer, its power in the world is real"

So three steps to Green heaven? First, replace money with land as the source of true value. Second, challenge the right of those currently in ownership to enjoy that privilege when it is so socially and environmentally destructive. And third, argue with renewed vigour for the immediate introduction of the taxation of land value as the central source of national revenue.

Molly Scott Cato is a Reader in Green Economics at Cardiff School of Management and Economics and Speaker for the Green Party in the UK

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feature

A TALE OF TWO CITIES

Josh Vincent

LVT is used most extensively in the state of Pennsylvania. Indeed, the first tax in Pennsylvania in 1693 was a land tax.

Harrisburg, PA – LVT has contributed to sustained economic resurgence

Harrisburg

Harrisburg first employed LVT in 1975 to battle the twin disasters of nature (Hurricane Agnes) and humanity (land speculators). After the storm had wiped out much of the downtown and industrial sector, speculators quickly snatched up land and held it for future gain. At the time Mayor Arthur Swenson reasoned that LVT would both promote construction through the tax relief afforded buildings and provide an incentive to use vacant land.

Recent long-time Mayor Stephen R. Reed and other City administrators credit Harrisburg's use of LVT as a key initiative in promoting the revitalisation of their City. LVT encourages the highest and best use of land and rewards those who properly maintain or invest in buildings.

One of the effects of LVT is to benefit the lower-income homeowner and small business owner to keep and maintain their homes and businesses. It also has the residual effect of keeping rents lower than they would otherwise be. It rewards productivity and investment, in contrast to a flat rating tax rate system that penalises both.

Once considered the second most distressed cities in the nation, Harrisburg, since 1982, has sustained economic resurgence that has garnered national acclaim. Mayor Reed was voted "US Mayor of the Year" in 2006.

In 2002 the City issued 1,567 building permits. They represent a total of $269.7 million in new investment, the highest total for any year in the City's history. Even in the face of the recession, in 2008, 1,623 building permits were issued with a value of $90.2 Million.

Since 1982 Harrisburg has issued a total of about 30,000 building permits reflective of $3.2 billion in new investment. In 1982 the total assessed value of taxable real estate in Harrisburg was $212 million. In 2007, it was over $1.8 billion, which is reflective of the additions to the tax rolls from new investment.

By the end of 2007, the number of businesses on the City's tax rolls had risen to 5,278 -- the highest number ever recorded. This is in sharp contrast to the number that existed in 1985: 1,908.

Harrisburg is the only municipality in Central Pennsylvania to subsidise the area's transit system. Harrisburg received the "Distinguished Budget Presentation Award" from the Government Finance Officers' Association, and was awarded the "Certificate of Achievement for Excellence in Financial Reporting" by GFOA.

"Once considered the second most distressed cities in the nation, Harrisburg, since 1982, has sustained economic resurgence that has garnered national acclaim."

These results are impressive when one considers the fact that 45 percent of the land in Harrisburg cannot be taxed because it is state, county, or non-profit real estate.

Administrative costs to implement the two-tiered tax system were minimal. The appearance of the bills and an explanation of the change to a two-tiered tax system were the only administrative changes that took place. The current ratio of land to buildings is 6:1.

A current city fiscal crisis brought on by the failure of an independent authority has brought Harrisburg back into the news recently. Current Mayor Linda Thompson will resort to land value taxation to close a huge hole caused by the default of this authority's debt, which can't be paid; legally the city and county then must step in to pay off the bonds. LVT may again be called upon to provide revenue stability and a modicum of local control over its economic destiny.

Pittsburgh

The story of Pittsburgh and LVT goes back a long way. Implemented in 1911 by an act of the state legislature, the growth and low tax atmosphere of Pittsburgh during those early years and especially during the expansion of LVT in the late 1970s was remarkable.

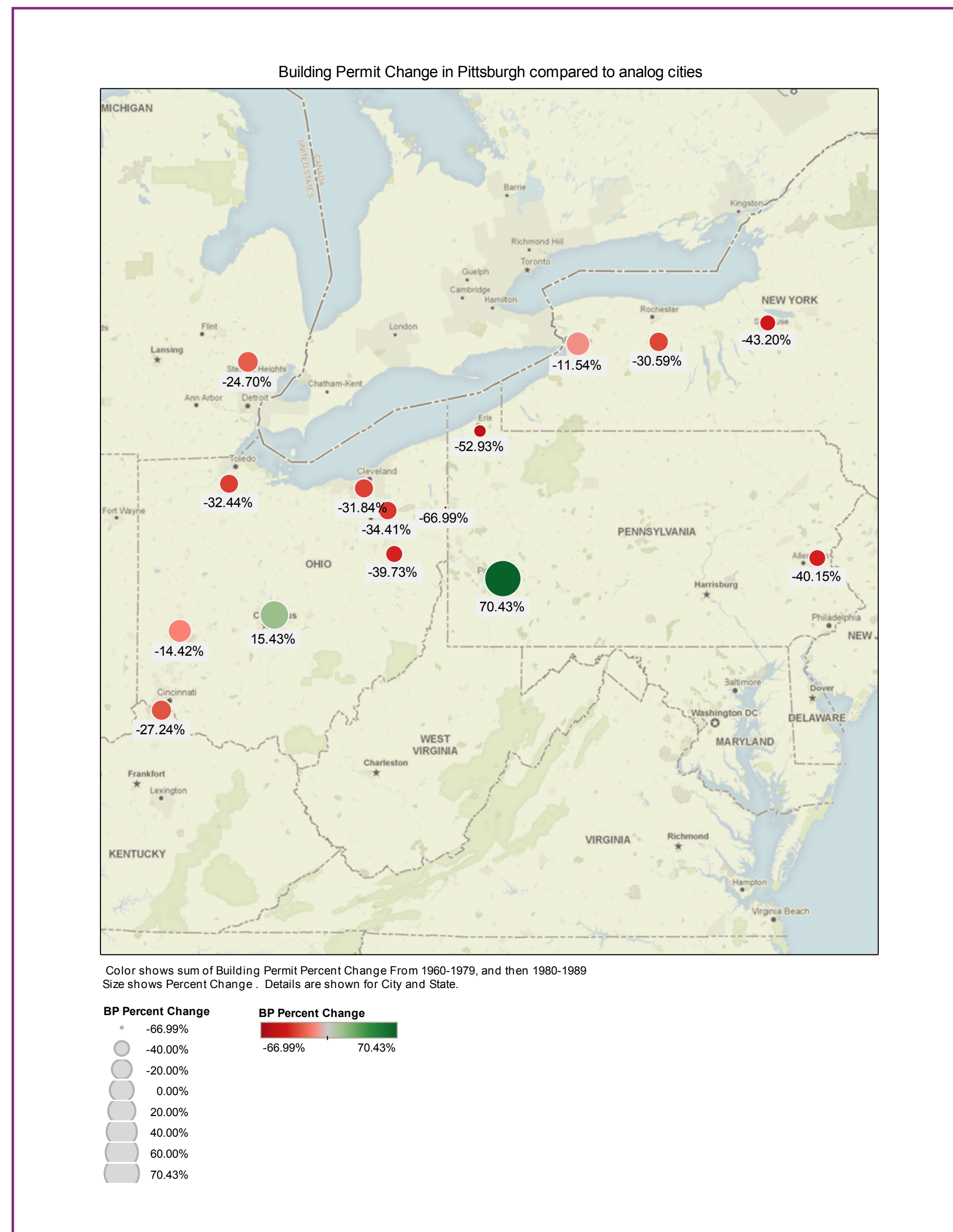
Research in the mid-1990s concluded:

> *"The basic data are clear on certain things. Following the change in regimes at the end of the 1970s, Pittsburgh experienced a striking building boom, far in excess of anything that took place in the other major cities in the region. The building boom was basically a city phenomenon; it did not extend to the rest of the metropolitan area. It was, moreover, a boom primarily in commercial building activity.*

The residential sector experienced only a modest increase in new construction (although even this is noteworthy in the context of the nationally depressed housing markets of the early 1980s). The central thrust took the form of several major new office buildings in the Central Business District in response to a marked shortage in office space that characterised the transformation of the Pittsburgh economic base from its earlier heavy manufacturing orientation to a more diversified, service-oriented economy." (Oates,Schwab 1997)

How to measure the success of LVT in Pittsburgh? It is accepted by most urban development experts that tracking the dollar value of building permits is the place to start. The Oates and Schwab numbers are

Building Permit Change in Pittsburgh compared to analog cities



> Most often, property tax falls equally on land and the attachments. For example, if there were no land value tax (LVT) Harrisburg would have a tax rate of 8.64 mills (or .864%). Currently the rate on land is six times the rate of buildings: 28.67 (2.867%) mills on land values and 4.78 mills (.0478%) on buildings.

impressive: Splitting 15 "Rust Belt" cities into two time frames (1960-1979 and 1980-1989), the rapid decline in construction was notable in its severity. These time frames are important since they mirror the period from relative industrial health to a near total collapse of traditional heavy industry in the region. Yet, Pittsburgh surged against its analogs:

Only Columbus, Ohio registered a gain, and that was due to annexation of land outside the city.

Pittsburgh rescinded LVT in 2001. Why? In the midst of a botched property valuation, there was a bitter mayoral primary campaign. Wealthy areas were struck by inaccurate assessments. Rather than strike at the root problem, the challenger called LVT the enemy, not acknowledging that largely working-class communities would pay higher tax if LVT were lost. He claimed that the downtown buildings crowded into Pittsburgh in the last 30 years would pay more without LVT (true), although Pittsburgh's traditionally business-friendly LVT kept rents low for tenants and productive businesses. "Economic development" is reserved for deep-pocket speculators who refuse to do anything without tax abatements and givebacks shouldered by the poor and middle class homeowners.

What happened to Pittsburgh after it lost LVT?

The Center for the Study of Economics and Dr. Steven Cord looked at building permit issuance after rescission. Pittsburgh's private new construction (now more taxed) declined 19.57% (inflation-adjusted) in the three years after rescission as compared to the three years before, while the value of construction nationwide increased 7.7% (also inflation-adjusted).

An analysis of the Pittsburgh assessment data found that rescission caused 54% of all homeowners to pay more property tax and 70% of poorer homeowners. As for non-landowning tenants (office tenants also), eventually they all paid more space-rent because more building tax was passed on to them but the land value tax never can be.

Since that time, vacancy rates in Pittsburgh have been higher than the suburbs and the city has flirted with insolvency with no end in sight.

Joshua Vincent is Executive Director of the Henry George Foundation USA/Center for the Study of Economics, Philadelphia

Oates, Wallace and Schwab, Robert (1997) 'The Impact of Urban Land Taxes: The Pittsburgh Experience', *National Tax Journal* **L1**

TJN is working with Speak-it Films the production company behind the award-winning film 'Black Gold', which changed the way millions of people think about their coffee and became a clarion call for trade justice across the world.

Speak-it Films' new project, "Cashback" (working title), will be a cinematic feature-documentary thriller about illicit financial flows. It will tell the story of how money is drained out of developing countries by a network of bankers, accountants, and lawyers into secret, offshore Western bank accounts, undermining the lives of millions of people. It is estimated that for every dollar of aid that goes in to developing countries ten dollars comes out under the table.

How does this happen? Why is no-one paying attention? This landmark film will peel away the secrecy to reveal one of the 21st century's biggest scandals.

Cashback is intended for a mainstream cinema release in 2012 and will act as urgent wake up call to the public and will also become a powerful tool for organisations to use for lobbying and public mobilisation.

The release of the film will be supported by a 5 year global outreach campaign co-ordinated by TJN and our colleagues across the world.

We are now inviting the TJN community, who are committed to changing the status-quo, to be part of this groundbreaking project. If you are an individual, NGO, business or funding organisation and would like to become a funding partner please get in touch and join us on the CASHBACK journey.

Please contact **info@taxjustice.org**

Or visit **http://www.tippingpointfilmfund.com/projects/cashback/**

reviews

Paper review: Debt and equity

In June 2009 the IMF Fiscal Affairs Department issued an important paper, *Debt Bias and Other Distortions: Crisis-Related Issues in Tax Policy*,[1] which looks at how tax distortions have contributed to the build-up of debt in our societies. **Nick Shaxson** explores.

This IMF paper has a central premise: that tax distortions and tax havens have played a major role in the build-up of debt and complexity in the financial system, contributing to the latest financial and economic crisis. It supports **previous TJN analyses** from 2007 onwards pointing out exactly these problems.

Two main issues stand out.

First, when a corporation borrows money then pays interest on the loan, it can generally deduct the interest payments against tax. In addition, if the subsidiary or financing partner records those interest payments in a zero-tax haven, it cuts its tax bill that way. The distortion is that if the corporation, by contrast, funds itself through equity finance, it gets no comparable deduction. The distortion gives corporations powerful incentives to load up with debt, rather than to seek financing through equity markets.

The effect is very large: "These distortions create advantages to the use of debt measurable in hundreds of basis points," the IMF says. With a corporation tax rate of 20 percent, it estimates that a debt-equity ratio that would be 40 percent under a neutral system, would increase to roughly 45–60 percent. In almost all cases, this makes debt finance cheaper even than the use of retained earnings in most countries.

Leveraged buy-outs are a case in point. Private equity firms and others routinely borrow to buy profitable companies, then deduct the interest costs in the high-tax country, and realise the interest income tax-free, offshore. At a corporation tax rate of 30 percent, the taxpayer gives a 30 cent subsidy to the private equity company for every $1 of interest paid. This engineering does nothing to promote higher productivity or real value creation – it merely transfers wealth directly from taxpayers to private equity firms, and indirectly transfers wealth by boosting leverage in the financial system, which has led to taxpayer bailouts.

A second problem with the tax distortions, the IMF concludes, is that they encouraged the use of complex financial instruments and arrangements, creating new risks and damage to the real economy. "Financial innovation has been driven primarily by the search for new ways to allocate risk, but also by tax avoidance," it said. Securitisation creates three main tax issues: first, whether capital gains on assets placed in a Special Purpose Vehicle (SPV) are taxable; second, whether the SPV itself is taxable; third, whether and how payments to holders of SPV assets are taxed. One focus of financial innovation, the IMF notes, has been to construct hybrid instruments with many features of equity but enough features of debt to attract interest deductibility. This comes at a cost: not only loss of corporate income tax revenue, but also "increased complexity and opacity of financial arrangements" which "may hamper financial supervision." As TJN has noted, certain jurisdictions – notably Delaware and the Cayman Islands for the U.S., and in Ireland, Luxembourg, Jersey, and the United Kingdom, for Europe – specialise in creating exactly the right legal environment for such engineering. **All** are major secrecy jurisdictions.

These distortions are especially important with respect to financial services corporations, and go a long way towards explaining the rapid growth in size and riskiness of the financial services industry. As the IMF notes, the tax bias towards debt for financial firms conflicts directly with financial regulation, which tries to lean against debt. And debt is especially important for financial institutions, because they have been so unusually profitable – making the returns on this debt-related tax engineering all the greater.

The paper also notes that the OECD's recent (feeble) efforts to address problems caused by tax havens entirely ignores these issues, by focusing merely on criminal tax evasion, while ignoring these issues of legal tax avoidance.

The IMF is quite right to identify these major and harmful distortions in international tax. Capitalists are supposed to take risks with their money – and reap the profits or losses that flow from them. Instead, these tax subsidies (and the IMF explicitly agrees that they are subsidies) help capitalists take, and even magnify, their profits – then shift the risks and losses onto others; in the process, capitalism has been thoroughly corrupted. Reform these distortions, and capitalists will do what they do best – take on both the risks, and the rewards.

Having made these extremely useful and important points, however, the IMF then loses its nerve, and veers off in completely the wrong direction.

1 http://www.imf.org/external/np/pp/eng/2009/061209.pdf

reviews
(cont'd)

The answer, it says, is artificially to create a hypothetical return on shareholders' equity, which it calls Allowance for Corporate Equity (ACE,) and then make that tax-deductible! In other words, leave interest payments tax-deductible – but give these subsidies to equity capitalists too: cut the tax burden on the wealthy. Perhaps by way of an excuse, the authors add that "little is known of the welfare costs of these distortions." (Later, while discussing the issue of interest deductibility in the mortgage markets, for which these problems are also a major issue, they admit that "deductibility likely favors the better off.")

The IMF mentions, but fails to endorse, the obvious and much better alternative: stop allowing corporations to cut their tax bills by deducting interest payments. This would level the playing field towards equity finance just as effectively – and help stem the tidal wave of wealth redistribution, from poor to rich. And it would give the tax havens a kick in the teeth, to boot.

By Nicholas Shaxson

news

African Voices Call for Tax Justice
by John Christensen, TJN

Tax justice is on the agenda (photo: John Christensen)

Since its launch in 2007 TJN for Africa has given priority to mobilising African civil society around the issues of tax and domestic resource mobilisation. In March 2010 delegates from 17 countries and 3 continents met in Nairobi, Kenya for a **Pan-African Conference on Tax and Development**. The conference had three key themes: harnessing domestic tax policies for development; taxation of extractive sectors; and closing the floodgates on illicit financial flows.

At the end of the conference the delegates issued the following **Declaration**, which calls on African governments, African regional bodies, the international financial institutions, the UN, the OECD, aid donors and civil society to take steps to strengthen the transparency, accountability and overall integrity of tax systems and to recognise the crucial role played by tax in development processes.

The Nairobi Declaration on Taxation and Development

1) We, the undersigned organisations and networks, having shared extensive research on the problems facing sub-Saharan African countries at the inaugural Pan-African Conference on Taxation and Development held in Nairobi, 25-26 March 2010

  a) recognise the common threat to political progress, sustainable economic development and to poverty eradication that results from the unacceptable domestic and international obstacles to effective taxation for development.

  b) affirm that effective and equitable taxation and is critical to the independence of African countries; and to the strengthening of channels of political representation and government accountability.

  c) commit to work together for reform in the areas of domestic taxation, revenues from natural resource extraction and international taxation.

1) Domestic taxation

  a) Having regard for the importance on tax compliance and accountability for tax revenues and expenditure we:

  b) call on African governments to commit to full transparency on tax revenues and tax expenditures.

  c) call on African governments to remove tax exemptions for multinational corporations and wealthy individuals and elites.

  d) call on revenue authorities to simplify the tax code and reduce the compliance burden, particularly for small businesses.

  e) call on fiscal research institutes to investigate the feasibility of land Value taxes in urban areas to funding of local infrastructure provisions, and to conduct analysis into the benefits of Export Processing Zones to African countries.

  f) agree to work within civil society to promote taxpayer education and compliance and call on other civil society organisations to do so.

African Voices Call for Tax Justice (cont'd)

g) commit to ongoing research and advocacy with regard to the impacts of tax policy on men, women and vulnerable groups.

2) Revenues from natural resource extraction

a) Having regard for the importance of strong governance to ensure African governments benefit from natural resource extraction we:

b) note the power and information asymmetry between African governments and multinational companies in negotiating fair contracts and the lack of capacity to determine appropriate prices.

c) question the lack of transparency in mining contracts across the continent which increase potential for bribery and corruption and undermine accountability.

d) call on African governments to audit natural resource bases before signing mining contracts.

e) call on African governments to strengthen legal provisions relating to contracts, possibly including measures to over-ride stability agreements that prevent future governments from re-negotiating contract provisions, possibly including limits to length of the contracts.

f) call on African regional bodies to explore regional coordination and harmonisation of fiscal regimes, and information exchange to challenge harmful tax competition in the mining sector.

g) call on African regional bodies to commit to South-South learning of successful tax practices in relation to mining.

h) call on African governments to sign on to the Extractive Industry Transparency Initiative (EITI), and to ratify the United Nations Convention Against Corruption.

i) call on aid donors to build the capacity of civil society in monitoring the activities of mining companies.

j) affirm that if it is not possible to arrive at a fair contract that, resources should be left in the ground for exploitation by future generations.

3) International taxation

a) Having regard for the leakages which undermine the tax bases of African countries we:

b) note that developing countries lose more as a result of international tax evasion and avoidance than they receive in foreign aid.

c) note the need for policy coherence among aid donors to take steps at the national and international level to challenge international tax dodging.

d) affirm the need for international and regional tax cooperation to challenge harmful tax competition and stop tax leakages.

e) challenge the widely held assumption that low tax rates encourage economic growth and development.

f) call on the UN, IMF, World Bank and OECD to include civil society in international processes to challenge tax leakages.

g) call on the G20 to involve African countries in international processes with regard to tax cooperation.

h) having regard for the need for greater transparency among multinational companies, we call on the International Accounting Standards Board (IASB) to adopt a country- by - country reporting of key financial information for all listed companies

i) having regard for the corrosive impact of financial secrecy in offshore financial centres we call on the G20 and the UN to move towards a multilateral agreement for the automatic exchange of tax information between jurisdictions, particularly developing countries.

j) call on African regional and pan African bodies to initiate effective multilateral programmes for exchanging tax information to combat tax evasion.

k) call on African governments to introduce legislation to make tax evasion a predicate offense under existing anti-money laundering provisions.

l) call on aid donors to invest in strengthening the capacity for revenue authorities and to provide technical expertise in monitoring large taxpayers, in particular, transfer pricing issues.

m) commit to research the impact of current tax regimes and campaign for reforms at the international level to ensure that the taxing rights of African countries are not undermined by abusive international tax practices

Signed

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Sandra Kidwingira **Kenya** Tax Justice Network -Africa
John Christensen **United Kingdom** Tax Justice Network /IS
Dereje Alemayehu **Kenya** Christian Aid- East Africa
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Nara Monkam **South Africa** Africa Tax Institute
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Abdoulaye Doudou Sarr **Mauritania** Publish What You Pay
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Saviour Mwambwa **Zambia** Centre for Trade Policy & Development
Evariste Munyampunda **Tanzania** GTZ- East Africa

INTERNATIONAL CONFERENCE ON THE POLITICAL ECONOMY OF TAXATION

SEPTEMBER 29, 2010

An interdisciplinary conference on the Political Economy of Taxation will be held at Loughborough University under the auspices of the Centre for the Study of International Governance. The conference will include contributions on the following core themes:

Core Themes

- Tax Competition and Neoliberalism: The Politics of Tax Havens; Tax Avoidance & Tax Evasion; Transfer-Pricing and Taxation; Paradigm Shift in the International Governance of Taxation?
- Taxation and Development: Taxation regimes in Emerging Economies; Taxation regimes in less developed economies; Taxation and mercantilism
- Taxation in the European Union: Tax Harmonisation: VAT & Excise Duties; Taxation and Enlargement; Taxation Policy in the Framework of Macroeconomic Regimes; Environmental taxes
- The Politics of Tax Progression: Taxation and Redistribution; Flattening the Curve of Progression; Flat Tax Debates and Regimes; Laffer Controversy?

Discussions have already begun with a publisher to produce an edited volume of conference proceedings, using the best of the day's papers.

If you wish to attend the conference on September 29 2010, you can request an application form from the Centre for the Study of International Governance at the above address or via **email**.

Tax Justice Network plans to hold a pre-conference meeting at the Centre for the Study of International Governance on September 28, 2010, starting at 18:00hr. The meeting will include discussion on recent research on secrecy jurisdictions and proposals for development of the Financial Secrecy Index.

Further enquiries about the Conference can be obtained by contacting the Conference Organiser: **Dr Jeremy Leaman**

Supported by: Centre for the Study of International Governance, Loughborough University (01509-222981)

http://www.lboro.ac.uk/departments/eu/CSIG/ContactUs.html