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Land Value Taxation and the planning system

Submission from the Labour Land Campaign to the Labour Planning Commission

Planning is essentially a land use issue. This submission shows how taxing land values is the key to improving the planning system. These topics will be addressed directly:

- Planning gain and capturing uplift in land values
- Improving land supply
- Diversifying housing suppliers
- New towns and garden villages
- Infrastructure
- Plan making
- Building regulations
- Improving the quality of the built environment

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Introduction

Land has been ignored by the mainstream since neoclassical economics took hold in the early 20th century. It is one of the prime factors of production, along with labour – all wealth is created by labour using land and its natural resources. The environment is land.

It is no surprise then that the land market is dysfunctional. It does not allocate to best use, which is what markets are supposed to do. The market can be corrected by re-pricing to eliminate the externalities and that is what land value tax does.

Properties are composed of two elements: land and building. They are inherently different commodities, land having no cost of production and being in fixed supply, whereas buildings, being capital goods, require maintenance and renewal to maintain their value.

There are three things which contribute to land value:

- Natural attributes, such as natural fertility, mineral deposits, fish stocks, an attractive view.
- Local goods and services.
- Permitted use.

Land values change, sometimes very quickly, but generally increase in line with growth in the economy.

The demand for, and hence value of, natural attributes depends on their abundance but can be affected by local planning decisions (obstruction of a view, for instance) and, in the case of anthropogenic climate change, by global decisions.

The provision of public and, to some extent, private goods and services is under central and local government control.

Statutory permitted use is ostensibly under local democratic control and administered by planning departments, notwithstanding that sometimes national agencies can override decisions taken by local planning authorities.

Planning gain and capturing uplift in land values

It should be noted that the idea of land value capture is deeply embedded in UK legislation, notably in the 1961 Land Compensation Act that provides for 'hope value' in the case of compulsory purchase. This captures the uplift in land value resulting from the granting of planning permission even before said permission has been granted - albeit solely for the benefit of the private landowner at the taxpayer's expense! The All-Party Parliamentary Group on Land Value Capture has reform of this Act as one of its objectives.

Section 106 Agreements (S106s) and Community Infrastructure Levy (CIL) are the main current vehicles which attempt to capture the uplift in land value due to change in permitted use. They can both be classified as development land taxes (DLTs) which, like all taxes, discourage the activity being taxed, in this case development.

DLTs have an ignominious history in the Labour Party¹. It is a pity that the Town & Country Planning Act of 1947 did not build upon the policies of the previous Labour government which had enacted a land value tax (although it was never implemented and was later repealed by the Conservative government).

As a result of the Barker Review of Housing Supply (2004) there was even an attempt to repeat the folly by proposing the Planning Gain Supplement. Largely thanks to the intervention of Labour Land Campaign President, Dave Wetzel, at the verbal inquiry at the Treasury, the idea was abandoned. But the last Labour government persisted in its belief that DLTs had merit and introduced the CIL just before it left office.

¹ http://www.labourland.org/downloads/papers/Vic_Blundell_DLT.pdf

Tory governments abolished Labour's Development Charge, Betterment Levy and Development Land Tax, and introduced S106 Agreements in the Town & Country Planning Act 1990.

S106s and CIL only seek to capture land value at the point of change of use and ignore other sources of land value. With a new development, much of the increase occurs long after the developer has left the site.

It would be interesting to know how many S106s and CILs have achieved their initial objectives of funding local facilities and providing 'affordable' housing as well as, in this context, the impact of subsequent changes to viability criteria.

The fact that these DLTs discourage development and fail to realise their anticipated outcomes are not the only problems. They are also distortionary and can lead to corruption where squeezed local authorities are pitted against corporations with huge resources. Even small builders can access websites which show them how to game the system. Their overall effect is to usurp the power of local authorities to plan proactively.

Other taxes which collect land value

Stamp Duty Land Tax (SDLT) is a transaction tax and, as stated above, discourages the activity being taxed, in this case relocating. Sometimes, discouraging some activity is the intention (tobacco taxes) but there is nothing beneficial about discouraging property transactions. People and businesses need to be able to move as circumstances change. SDLT may decrease the selling price, because there is an inverse relationship between taxes and prices, but this is not perceived by buyers. And, as with DLTs, SDLT only captures land value at a single point in time.

The OECD (Organisation for Economic Co-operation and Development) considers that the most effective taxes are "recurrent taxes on immovable property". The UK has three annual property taxes: Council Tax, Business Rates and the Annual Tax on Enveloped Dwellings (ATED) – a tax on houses owned by companies.

Since its inception in 1993, Council Tax in England and Scotland is based on eight price bands which have never been reassessed. Failure to revalue coupled with the fact that many local authorities in areas where property values are low have higher demands for public services than in better-off areas mean that Council Tax has largely become the poll tax it was hastily introduced to replace, e.g. the owner of a mansion in Westminster pays almost the same tax as the tenant of a bedsit in Weymouth. The intended abolition of the central government grant system, which used to represent half of all local government expenditure, can only exacerbate the situation.

The amount of land value captured is minimal in the most expensive areas – far less than with the original Domestic Rating System. This is one of the main drivers of the house price boom and, hence, the housing crisis.

Business Rates on commercial properties are far higher than Council Tax rates and thus collect a higher proportion of land value. The fact that the per-square-metre price of a plot of land with permission for commercial use is lower than that of the next-door plot of land with permission for residential use provides a neat illustration of the inverse relationship between taxes and prices. But Business Rates also fall on the building, part of working capital, and sometimes even on plant and machinery! Business Rates therefore discourage capital investment, e.g. to enhance productivity or working conditions.

So, not only do these property taxes fail to maximise land value capture, they also have defects which distort the land market and compromise its efficiency.

ATED, introduced in 2013, has some innovative features. It is cheap to administer because it requires self-declaration, with the valuation costs met by owners. The top rate is £220,350. This is the most effective current property tax, but it covers only a very small part of the housing market, namely property owned by companies.

Land Value Tax (LVT)

Land value is not created by landowners - it is unearned wealth and income. Natural justice dictates that it should be collected for the benefit of the community which, as a whole, inherited it as a birth-right and creates and sustains its value.

LVT is the only practical way this can be done. Simply, all land is valued on the basis of its optimum permitted use in its location, a rate is set and landowners receive the bill. There would need to be a long transition period before rates for owner-occupiers and owners of income-generating land could converge because the residential land market is so distorted.

It should be understood that infrequent revaluation brings property taxes into disrepute. It led to the demise of the superior Domestic Rating System and will eventually kill off Council Tax. Although revaluations for Business Rates take place every five years (unless it becomes seven for political reasons) this can prove fatal for businesses in decline, such as high street retailers.

Valuing land is easier than valuing property, i.e. land plus any structures upon it. Australia values its land every two years. Annual revaluation is optimal and is perfectly feasible with modern technology.

For income-generating land, adjusting the tax to current valuation means that it is inherently affordable as LVT is proportionate to the benefit received from the location by both the landowner (in rent) and tenant (in turnover).

Importantly, LVT is paid by the landowner. The UK is probably unique in levying property taxes on tenants. With no revaluations for Council Tax, local improvements allow landlords to raise rents without any outlay on their part.

Improving land supply

Usable unused land is a permanent loss to production (like unemployment). LVT will ensure that land is not wasted as it requires an income stream to service the tax.

Although its supply is ultimately fixed geographically, land can be used continuously without deterioration by changing its use to residential, agriculture, business, recreation or maintaining the ecosystem. Changes to permitted use are under the control of local authorities, and thus so is land supply.

It is possible for non-residential land and buildings to be used on a temporary basis for a different purpose than that which is statutorily permitted, and local authorities could consider allowing some buildings to be used more intensively on a permanent basis, with different uses for different time slots.

With houses there is a need to discourage under-occupancy (which the Council Tax single-occupancy discount positively encourages). LVT has an important role to play in this. By imposing a higher rate on all but principal dwellings this would induce a reduction in multiple home-ownership and under-occupied dwellings.

LVT would decrease house prices significantly in the most expensive areas. In fact, under full implementation the price of land would tend to zero. This would have the important effect of curbing the kind of speculative property acquisition that underlies so much under-occupation.

Some LVT advocates support the idea of 'rollover', to allow 'the poor widow in a grand house' to stay put until her demise. But there is a case for persuading the widow (through her tax bill) to downsize or take in lodgers. Also heirs might not be so keen to keep granny in her expensive home when the land price is insignificant and the building only retains its value by constant application of money.

Diversifying housing suppliers

The UK population has grown by 10% since the turn of the century, so there is undeniably a need for more new homes. It should not be necessary to leave the decisions of where to build new houses solely with big developers or for government to force local authorities into squeezing more and more homes into desirable locations.

It is important that brown-field sites are developed quickly where there is already infrastructure in place but this rarely happens. LVT would solve this problem: the value of the site would be assessed according to current use so it would not be possible for the owners to do nothing - they would have to get on with redevelopment or sell to those who will.

LVT will also ensure that the big house builders would no longer be able to maintain major land banks. These are usually green-field sites, purchased at low prices. LVT will be applied to all land, including agricultural, so production would likely be maintained until full planning consent is obtained.

With DLTs abolished, there will be no delay whilst haggling over S106s and CIL proceeds, nor any extra cost for local authorities.

Large sites often do not get built out quickly as it is not in the interest of developers to put too many houses on the market at one time. To solve this, LVT be payable as soon as planning permission has been granted.

This should help to break down the oligopoly in house building which has developed, particularly since the financial crash, and allow the entry of smaller businesses.

Small builders do not sit on valuable land and the abolition of DLTs will also benefit them.

Local authorities should be able to decide where new houses are built, purchase green-field sites at agricultural prices, provide infrastructure and sell plots to small and self-builders. With full LVT, as previously explained, land prices would be low whatever the use.

There is no reason why land awaiting redevelopment could not have a temporary use of benefit to local residents, such as horticulture or play areas, for which no LVT would be charged, as there is no market value for land so used.

New towns and garden villages

Landownership in the UK is extremely concentrated. As recently exposed: "A few thousand dukes, baronets and country squires own far more land than all of middle England put together."²

It should be possible for planning at the highest level to designate underused 'estates' as the location for a new garden city, village, urban extension or new town. The value of the location would rise and the owner would have to pay a large LVT bill every year in order to preserve the family estate or be forced to develop or sell to those who will, which could be the local authority. Reform of the Land Compensation Act would not be necessary since LVT would eliminate 'hope value'.

Infrastructure

New infrastructure such as a school or a new transport link can dramatically increase local land values. The example often quoted is the Jubilee Line Extension which cost the general taxpayer £3.5 billion to build, yet in the 10 years from 1992 to 2002 this project created an unearned uplift of more than £13 billion for landowners in the vicinity of the 11 new stations. It was thus shown that the Extension could have been funded entirely from local land values.

² Guy Schrubsole *Who Owns England?* Kevin Cahill's *Who Owns Britain* made the same observation in 2001

The research was commissioned by Transport for London and as a result, for the Crossrail project, a Business Rate surcharge was levied in the development area, which provided part of the funding.

LVT could create a virtuous circle where public spending increases land values which increases LVT revenues which could be used for increased public spending. There would be no need for local authorities to negotiate S106s or CILs. They could be allowed to borrow from central government with the loan being repaid from the extra LVT generated.

The beneficiaries of Crossrail, as for the Jubilee Line Extension, are and will continue to be, the landowners, as the contribution from businesses (paid by tenants) will be less than the increase in value. The main beneficiaries are the owners of residential land who made no contribution to the project but will see the highest increase in the value of their property.

Here it is important to distinguish between owner-occupiers and landlords; the latter will not only see an increase in their asset wealth but they will also be able to put up rents.

Building regulations

The UK has the smallest and worst maintained housing stock in the developed world. Developers appear to have persuaded the legislators that, because of the high price of land, building regulations cannot prescribe decent sized homes, adequate fire protection, efficient insulation or other measures to protect the environment. This is a fallacy, as the market will always adjust to higher standards. This excuse will no longer apply once LVT is introduced, as it will reduce land prices from the start. It would then be feasible to mandate the Passivhaus standard to cut down the very significant contribution of domestic greenhouse gas production.

Improving the quality of the built environment / Plan making

The planning permission system represents a powerful tool for social engineering and has always been used as such, even in communities with less central control than the UK: zoning systems in parts of the United States and many far less developed countries are stricter than in Britain and work better when it comes to placemaking and creating vibrant, well-integrated communities.

LVT provides an efficient adjunct to this aspect of planning through the valuation process. The primary factor that determines land value is its location and the secondary factor is its permitted use, i.e. its planning permission. If social utility is taken into account in the course of valuation, LVT becomes a potent instrument for sensible planning: while the land under a residential property in central London will be worth more than a similar plot in the highlands of Scotland, adjacent plots in both places with planning permission for a public hospital would be worth the same, i.e. close to zero, because both places need a public hospital and the purpose of public

hospitals is to keep people healthy, not generate revenue. This principle applied across the board would complement current planning permission modalities to ensure developments with an appropriate, socially optimal mix of services, jobs, resources, facilities, open spaces, etc.

Similarly, LVT could be a powerful adjunct to current planning instruments when it comes to environmental engineering. Land granted permitted use as wilderness would be valued at zero and therefore exempt from LVT; land granted permitted use for organic farming could be valued lower than farmland granted permission for intensive exploitation. Thus, the valuation process could be advantageously used to take into account the kind of pernicious externalities that are currently ignored or even encouraged by our economic and fiscal systems. Across-the-board application of such a principle could help planners direct environmentally positive evolution of the built and rural environments on a rational, efficient basis.

The land valuation process, which would be mandated for LVT implementation, could also be useful to planners in assessing the viability of a project by providing the basis for more accurate cost-benefit analysis.

Conclusion

It is recommended that all current property taxes be abolished and replaced by LVT. This would bring down land prices, stop land being wasted and enable land to be distributed more fairly and efficiently by the market.

This would necessarily mean root-and-branch reform to reinforce the planning system which would assume far greater importance than is currently the case because permitted use is an essential determinant of the value of any plot of land.

Moreover, through influence over the system used to value land, planners would find themselves with a powerful new tool to direct rational, efficient, socially beneficial and environmentally friendly urban and rural development, in the broadest sense of the term.

A useful tool for planning – and a democratic right – is a free-to-access cadastral map of the UK. A cadastral map is defined as "a public survey of land for the purpose of taxation". Land will not be valued unless it is taxed.

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