

Down with land price subsidies

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Valuers are listening to the high pitched pleas for a return to normality in the housing market with a good dose of skepticism. Our work is often paid for by the same bankers who have speculated with other people's savings and lost. Their toxic wagers are precisely the abnormality which has caused trillions worth of assets to blow off and millions to become cash-strapped. Did valuers give comfort to the process?

When we examine the havoc which house prices wreak it is easy to forget that dwellings are a depreciating asset, seldom enduring for more than a generation before the demolition gangs or the refurbishers knock.

Yet valuers know full well that the value of bricks and mortar will reduce by some 4% each year due to obsolescence unless improvements are continuously made. So when house prices rise by 10% the land value, say 40% of the total price, will have increased by 30%. When a house price falls by 10% the land price has fallen by 20%.

Valuers also know that land prices are contrived. They are a State subsidy. Remove that backing and it will be curtains for property booms or busts. The temptation to earn something for nothing through rising land prices, everyone's dream and every banker's obsession, will fade quietly away.

Of course the subsidy arises because land rent is only partially taxed, as a portion of property rents, capital gains taxes, rates and taxes, stamp duty, transfer duty, donations tax, estate duty income tax and VAT.

If it was fully taxed, if all of the pure land rents were appropriated by SARS, the price of such land would become affordable to all four million landless and jobless families.

What is pure land rent? Well I am not sure how that is taught today but Ricardo's Law defines land rent as the surplus product of each site once all costs, including depreciation have been accounted for. This is an economic law. It is as reliable as Newton's law of gravity. The difference in land rents between two identical farms where one has a borehole and the other not is the difference in net sales. The price difference is of course the rent difference multiplied by the P/E ratio.

The capture of land rents are also an orthodox free market fiscal intervention as the open letter to Mikhail Gorbachev at the fall of communism in 1991 from Nobel Economics Laureates F. Modigliani, J. Tobin and R. Solow as well as other academics:

"It is important that the rent of land be retained as a source of government revenue."

This also begs the questions that if land has no production cost why [on earth] should it be subsidised? Why too are the rich being subsidised when it is the poor who are needy?

In the nineteenth century in South Africa a massive proportion of taxes came from the land. It was then held under British sponsored perpetual quitrent tenures. Over time the refusal by the landowning Parliamentarians to properly tax land prices drained the state coffers and successive governments increasingly relied on alternative taxes on wages, salaries, profits, interest and trade.

This made an already lethal financial system even more potent. The least visible but the most incredible consequence is that many house owners do not pay taxes but merely advance funds to the State and then wait for rising land prices to pay them back. These hand outs are beyond the reach of the landless.

Of course it is not landowners who are being criticised here but the law. There are other iniquities in personal taxes:

- Conventional taxes are robbery. This is a criminal act and can only be tolerated on the grounds that there is no substitute for larceny in public finance.

Land taxes however do not “take” anything personal. The weather, fertility, water, views, infrastructure, location, amenities, zoning and services as well as security of title are not things that fall off the back of a truck. They nevertheless create and sustain all land values.

- Conventional taxes also cause grievous sovereign losses when some citizens gain windfall land profits at the expense of others. For example a number of Transnet pensioners were given ±R6Bn of development rights in the VandAW by the City of Cape Town. This is 18 months of the City’s current annual rates and taxes revenues.

The case history on the probable R88bn land windfall profits for a R22Bn public investment around the new Gautrain stations still has to be written. It will show that infrastructure projects are self-funding and the increase in land values by public spending can be captured.

In effect then land taxes are the privatisation of personal taxes which make way for the simultaneous nationalisation of all pure land rents, but not land nor personal property. The appropriation of these rents by the State returns to the community only those values which the broad society generates.

This is a profound change. It heralds the start of a free-land tax haven, like Hong Kong citizens enjoy. This is a mighty generator of wealth and resolver of the landless and jobless plight as also in Japan, Taiwan, Singapore, Botswana and Ethiopia.

With a free land-entry policy and no onerous taxes what can then stop dirt poor South Africans from building their own homesteads, growing their own orchards and vineyards, rearing cattle, chickens and sheep and playing cricket on the village green on Wednesdays, hunting on Saturdays, and owning a flat in the city? What too will stop GDP growth from tripling or quadrupling?

So valuers might more brusquely deal with clients or employers who attempt to influence their work. Prof Joseph Stiglitz a Nobel economics laureate reported in the November 2008 Harper’s magazine that USA assessors were certifying mortgage valuations which were inflated because they assumed continuous growth in house, aka land prices.

South African valuers might also more confidently recommend alternate valuation systems or techniques which target land values such as sec 45.3 of the Property Rates Act encourages.