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A systematic framework of location value taxes reveals dismal policy design in most European countries

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ABSTRACT

Location values have long been recognized as an attractive instrument to raise municipal revenues. First, they increase fiscal efficiency and equability compared to traditional property taxes. Second, they can be used to enhance sustainable urban planning. The question of how to design a location value tax has long been discussed in various strands of literature, but there are few efforts to create multidisciplinary approaches. This lack of reconciliation hampers the discussion on optimal designs that includes all economic, social and environmental considerations. Here we combine literature on public finances, urban economics and value capture with that of sustainable urban planning to narrow this gap. We develop a framework to assess the design characteristics of location value taxes from a sustainability perspective, and apply this framework to assess current practices in Europe. The analysis reveals severe shortcoming in policy design in most European countries, although Denmark provides a more promising example. Nonetheless, location value taxes have a high potential for improving sustainable urban planning.

1. The rationale of a location value tax for urban sustainability

Cities constitute both sources and solutions to climate change and other sustainability challenges. While diverse disciplines address some aspects of urbanization, there is a need to integrate this knowledge in order to find optimal – or at least appropriate – pathways that could minimize the negative impacts as well as maximize the positive outcomes of the urbanization process (Rosenzweig et al., 2011; Seto et al., 2014). Solutions are strongly related to policy instruments that enhance synergies among multiple objectives, and well-designed urban plans exhibit great potential (Seto et al., 2014; Zanon and Verones, 2013). On the one hand, they efficiently limit urban externalities (Arnott, 2011; Brueckner and Kim, 2003; Kaza and Knaap, 2011). On the other hand, they may alleviate municipal budget constraints (especially in Europe) for low carbon urban infrastructure investment (Dexia and CEMR, 2012; Mathur and Smith, 2013; Rybeck, 2004).

Location value tax (LVT), a tax that recovers the value of properties that has not been created by landowners, could explicitly support sustainable urban planning objectives (Batt, 2011; Brandt, 2014; Panella et al., 2011; UN-HABITAT, 2011a; UN HABITAT, 1976) (we argue in favor of using the concept LVT instead of the common term land value tax based on a proposal to homogenise nomenclature; see Fig. 1 in Section 3.1 for clarification). First, it increases fiscal efficiency. As the provision of land remains cost-free, taxing away urban location values (LV) does neither harm the economy nor does it distort markets (George, 1879; Kunce and Shogren, 2008; Mattauch et al., 2013). Revenues have been used to finance sustainable urban infrastructure in different contexts[1] (Ingram and Hong, 2012a,b; Kitchen, 2013; Medda, 2012; UN-HABITAT, 2011a; Zhao et al., 2012). Second, it is legitimate to tax away LV. The share of property's worth which is not produced by landowner's labour, but from public intervention, community actions and environmental quality, is an unfair burden on those whose activities had given it value (Albouy, 2012, 2009; Arnott and Stiglitz, 1979; Brandt, 2014; Brueckner, 2000; Fainstein, 2012; UN HABITAT, 1976). These capitalization dynamics, exacerbated in the last decade, have provoked a strong call for reconsidering the property tax (PT) base and shift it from real estate towards LV for wealth distributional objectives (Antony and Seely, 2013; Brown and Smolka, 1997; Dwyer, 2003; European Environment Agency, 2010; Foldvary, 2006; Gaffney,

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[1] Cord, (1985) found that an annual land rent tax would yield nearly two-thirds of all taxes in place for the U.S.

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Table 1
Design characteristics of LVT influencing sustainability effects. X indicates the most suggested option literature refers to when looking at the sustainability effects. Abbreviation characters explained in Table 2.

	Criterion	Sub-criterion	X
1. Tax base	Natural resources (N)		
	Private improvements: investment nearby (T)		
	Environmental externalities (Q)		
	I Public/community intervention (C)		
	II Public intervention: urban infrastructure (E)		
	III Public intervention: land-use regulations (O)		
	Private improvements-owner: non-structural (M)		
	Private improvements-owner: structural (G)		
	Site value (*S*) (T + Q + C + E + O1 + M)		
	Location value (LV) (T + Q + C + E + O)		X
	Land value (*H*) (T + Q + C + E + O + M + N)		
2. Tax subject—Ownership	All urban owners (AUO)		X
	Private ownership (PO): private owner-occupied (POo) and Private owner non-occupied (POn)		
	Legal Entities (LE): legal enterprise (LEn), public (P) and institutional (I)		
	Tenants/users (U)		
3. Tax subject—location use	All land uses (ALU) (under restrictive urban land use planning)		X
	All economically usable activities (AEU): residential (RES); commercial (BUSS); industrial (IND); scientific parks (SPK)		
	Non-economically usable (NEU): non-profit (NP); religious (R); education (EDU); health (HEA); public (P); infrastructure provision (IP); natural reserves (NR)		
	Location beneath buildings (L1)		
	Location not beneath buildings (L2)		
	Vacant building ground (V)		
4. Valuation method	4.1 Basis of assessment	Market value (MV) (HBPU)	X
		Area based assessment (ABA)	
		Cadastral value (CV)	
		Flat base (FB)	
		Location gains (LG)	
		Annual rents (AR)	
		Appraisal: HBPU	X
		Appraisal: current use (CU)	
	4.2 How to appraise	Traditional techniques: abstraction (AB), allocation (ALL), teardowns (TD); contribution (CON)	
		Sales comparison (SC)	
		Self-assessment (SA)	
		Massive econometric appraisals (MA); computer assisted mass appraisals (CAMA)	
		CAMA + GIS (CAMA-GIS)	X
	4.3 Frequency of assessment	<5 years	X
		≥5 years	