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Land Value Tax in Ireland: revenue potential in post-crisis equilibrium

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Irish fiscal situation: a solvency crisis and an impeding liquidity crunch

- Ireland is experiencing a number of simultaneous and closely related crises:
  - Fiscal crisis
  - Public debt crisis
  - Assets bust
  - Banking crisis and liquidity trap
  - Economic growth crisis

Collapsed tax revenue exacerbated by rising public spending: 12-13% deficit in 2011

- Structural nature of the crises amplifies both the duration and the depth of the current adjustment to a New Normal of slower long-term growth:
  - Fiscal crisis has resulted in a public debt crisis
  - Assets bust has led to a long-term reduction in private sector propensity to invest at home
  - Banking crisis has resulted in a deep redrawing of competitive environment in Irish banking, resulting in higher long term costs of capital
  - Economic growth crisis has widened the gap between public sector (unproductive) and private sector (gaining in competitiveness, although slowly)

Private sector investment has fallen off the cliff

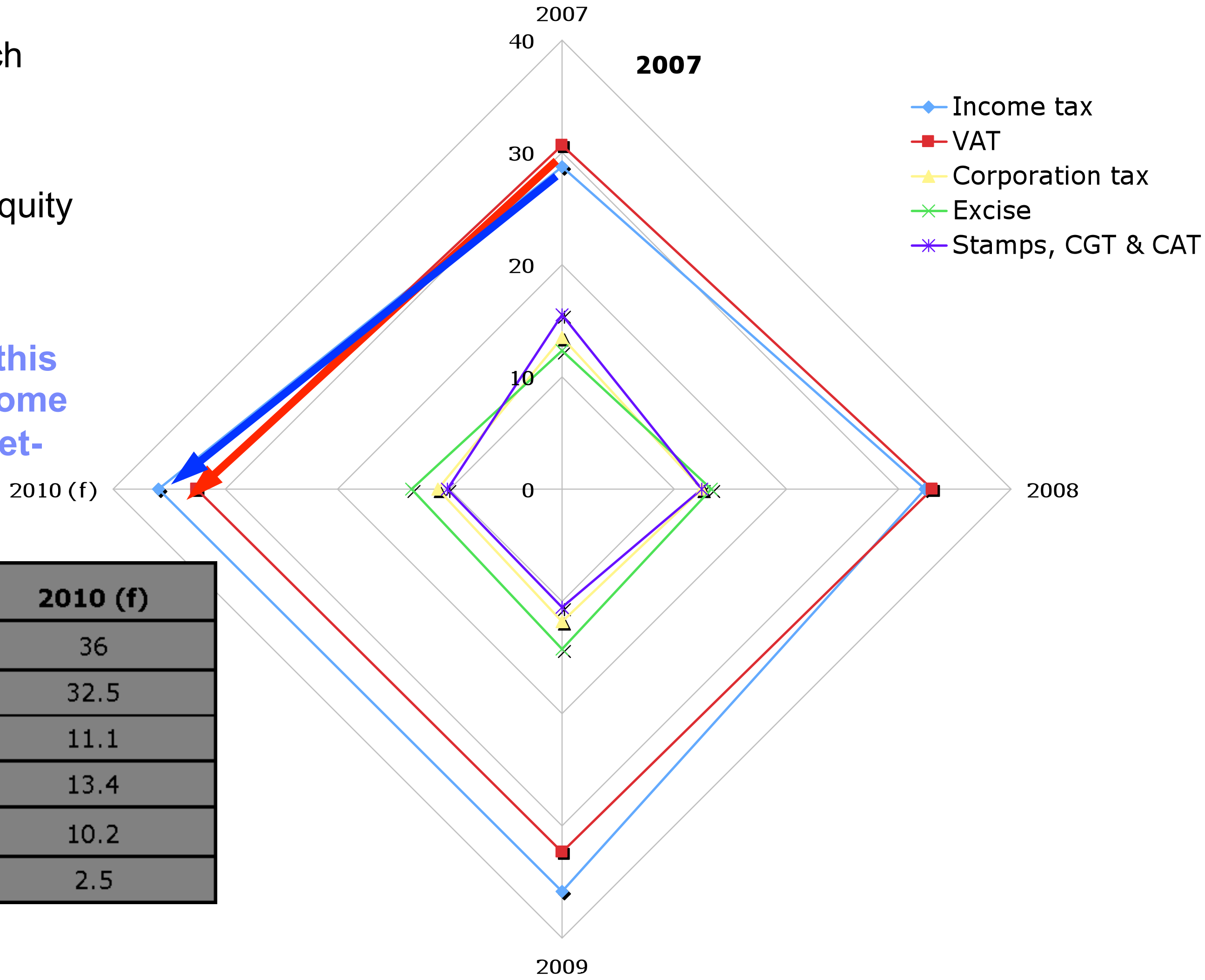
No confidence in measures to rebuild banking sector

Croke Park & tax increases are acting to reduce potential GDP growth to <1.8%pa

We need rebalancing of revenue sources, not an increase in revenue

Annual tax heads as % of total receipts

- Irish tax system has become much more dependent on income & consumption taxes
- Just in time for severe negative equity and household debt crisis
- **Fiscal adjustments required to restore productive capacity of this economy – shift away from income tax, in favor of more stable asset-base tax (LVT)**



	2007	2010 (f)
Income tax	28.73	36
VAT	30.68	32.5
Corporation tax	13.53	11.1
Excise	12.36	13.4
Stamps, CGT & CAT	15.55	10.2
CGT & CAT	7.40	2.5

Yield-based model linked to development values is the best benchmark absent actual sales data

- Assume:

  - Peak to trough decline in property values from €370,000 average to €175-185,000 average

  - Current share of land value in end development value = 20%

Supply of land for residential development, *2011-2012*

Assumed densities	Prices per unit, €	Estimated acre yield, €
25 units per acre (Peak Market)	370,000	9,712,500
12 units pa (av post-crisis)	175,000	1,662,500
15 units pa (urban post-crisis)	185,000	2,109,000
		Estimated land supply
12 units per acre		**113,333**
9 units per acre		**151,111**
6 units per acre		**226,667**

Equilibrium model of returns suggests stabilisation of property prices around 10% above the bottom of the cycle

- Assume:

  - Peak market share of land value in end development value = 45%

  - Current share of land value in end development value = 20%

- Total stock of housing set at 1,750,000 units
- Total stock of unsellable and social housing (with no recourse to tax) – 390,000 units

Supply of land for residential development, *2013-2017 horizon*

Assumed densities	Prices per unit, €	Estimated acre yield, €
25 units per acre (Peak Market)	370,000	9,712,500
12 units pa (av post-crisis)	195,000	2,223,000
15 units pa (urban post-crisis)	205,000	2,921,250
		Estimated land supply
12 units per acre		**113,333**
9 units per acre		**151,111**
6 units per acre		**226,667**

Revenue potential of Land Value Tax is linked to equilibrium assumptions and the scope for imposing a non-distortionary levy

- Using residential property density and yield assumptions:
- We can expect ca €640-1,280 million in returns from the land value tax at current property valuations
- At a taxable base of ca 1.75 million units of which 390,000 are assumed to be outside tax net, this level of taxation yields an annual charge of €471-973 per household.
- Allowing for variation in zoning reflective of densities and use, the tax yield can rise to ca €926-1,852 million per annum
- The level of average household burden consistent with this scenario will range between €681-1,362 per annum

Tax yield, post-crisis equilibrium €mln

	Higher density	Mid-range	Lower density	Average
Peak of the market:				
1% pa	4,953	6,605	9,907	
2% pa	9,907	13,209	19,814	
Equilibrium:				
1% pa	641.2	854.9	1,282	926.1
2% pa	1,282	1,710	2,565	1,852

Second order effects of LVT on equilibrium valuations of land

- LVT can be expected to
  - Reduce overall volatility in the markets for development land
  - Ameliorate speculative purchasing of land and land banking
- Using the above model, assuming tax elasticity of x1.5-2.5, the effect of LVT prior to the peak of the market would have taken between €12-24 billion of value out of the market for land, annually
- Almost ½ of the asking prices correction to-date could have been avoided in the presence of LVT

Land market valuation reductions, pre-crisis equilibrium with LVT, €bn

	Lower bound	Upper bound
Peak of the market:		
1% pa	495	990
Peak in the presence of LVT:		
€ billion (2000-2007)	397	798
% reduction (2000-2007)	-19.7%	-19.4%

Irish fiscal reform must include LVT as a substitute for existent tax burden on ordinary income earners

- Public austerity crisis has highlighted the need for significant restructuring of tax revenue streams to reduce dependence on transactions taxes

LVT reduces overall volatility of tax revenues

- Contraction in public and private investment requires significant innovation in raising revenue for infrastructure investment

LVT is efficient in capturing private gains to infrastructure investment

- Tax burden shifting onto the shoulders of higher human capital-intensive workers and entrepreneurs must be reversed for Ireland to succeed in the new age of knowledge-intensive growth

LVT can provide room for significant reductions in tax burden on income earners

- The economy must be rebalanced away from speculative bubbles in property and land, without restricting productive investment in property development

LVT reduces incentives to land bank & to speculatively invest in land without dis-incentivizing productive investment in property

LVT can be a significant contributor to fiscal and longer-term economic recovery for Ireland – a much better alternative to traditional property taxes and to the current path of rising overall tax burden on income earners