

Henry George News

Volume 58, Number 5

September - October, 1994

Henry George Day 1994



Susan K. and George C.

themselves, were Susan Klingelhoefers (Robert Schalkenbach Foundation Assistant Director) and Michael Hudson, (HGS Research Director). If you missed the event, you can read their remarks in this issue!

A large contingent of students, trustees and friends gathered at the New York HGS on September 1st to view proclamations from the Mayor and the Speaker of the City Council, share the traditional birthday cake, and hear firsthand reports on the momentum for Georgist reform in Russia. The two speakers, who had just returned from Russia



Grace and Michael Hudson

How Large is Russia's Land Rent? How Will it be Used?

by Dr. Michael Hudson

(Editor's note: In this issue, Dr. Michael Hudson, the new HGS Director of Research, begins his regular commentary on economic issues.)

What would happen if the land in Russia were privatized in such a way as to let its rent and price gains be taken by absentee speculators — and the mortgage bankers lining up behind them to load this property down with debt?

In June, I travelled to Russia with Nicolaus Tideman to meet with some of our Georgist counterparts and help create a program for local communities to collect land rent. Our first task was to estimate the magnitude of local rental and land values. However, it soon became apparent that trying to determine an economic price for Russian real estate was premature. Security of ownership is unclear in a political environment that continues to be marked by corruption. Real-estate taxes are not being paid, as owners collect rent but avoid divulging their ownership to the tax authorities. In the absence of a legal system defining property rights, there is scant basis for collecting public rents, to say nothing of allocating changes in land values and rent rates between the current users of properties, their localities, and the national taxing authority in Moscow.

Moscow and St. Petersburg are now ranked as the highest-cost cities in the world to live, at least for foreigners. A Western-type hotel may charge \$350 a night. To be sure, there are very few such properties, which is why they are so expensive. The seedy hotel I stayed at in St. Petersburg was mainly for native Russians, and cost just \$35 a night. Everywhere I went, I found a similar double standard. The Moscow art museums charge foreigners \$4, but Russians only have to pay 40 cents. Lunch — if one can find a restaurant — costs about \$25; most Russians skip it altogether, or take it in their company dining rooms.

This double standard has a major effect (continued on page six)

Volga Economics: For More Progress and Less Poverty

by Susan Klingelhoefers

(Editor's note: This is the conclusion of Susan's article from our last issue, in which she described the shipboard conference/cruise from St. Petersburg to Moscow between the 12th and 23rd of June.)

The curtains were closed in the St. Petersburg cruiser's "musical saloon" when our conference group met. Had they been open, each of us would have been distracted by the brilliant sky and clouds, and the quays of the Moscow River. On the day of the ship's departure from Moscow on June 14th, conference participants joined in the "saloon" to hear speeches from an illustrious panel.

Nicolaus Tideman, who has been in Russia enough to know the prevailing mood there, spoke first about the potential of public collection of rent in Russia. Few would be surprised by Nic's statement, "Nearly everyone agrees that things have to change in Russia." But we Americans may not realize that, "There is among Russians a strong identification with the idea that land inherently belongs to everyone."

Nic reminded his listeners that this burgeoning awareness is going to come, if at all, from the grassroots, and "is not going to be met with a single decision." His strategy in Russia stems from this knowledge. "There are city officials all around Russia that now understand the ideas to a significant degree; there are legislators in the Duma; there are professors in research institutions. That is what makes me feel that I should continue to promote public collection of rent in Russia."

Kemer Norkin, General Director of the Moscow Mayor's office, gauged Moscow's readiness to reform its taxation system. He said, "I, myself, am absolutely for the ideas of Henry George, but some of the ideas are vulnerable. The ideas... will work full-scale only when we would make a transition from [a] taxation system as it is now to the rent system."

Vladimir Tikhomizov of the Henry George Association of Moscow succeeded Nic and Kemer. He reported on the tens of thousands of copies of Russian *Progress and Poverty* and *Protection or Free Trade* that have been published by the Henry George Association of Moscow. He also promised a seminar at Moscow University at which students will be taught Georgist economics.

During the cruise up the Volga River, I became involved in the translation of the letter, entitled "Is Russia Ready to Accept the Theories of Henry George?" At the behest of Ecograd Director Tanya Roshkoshnaya, I gladly assisted her, and Michael Horsman, our friend from Ireland, in the translation. *(The letter appears, with commentary by Nic Tideman, on pp. 4-5 - LD)* While this letter, which was sharply critical of Henry George's ideas, was largely inaccurate, it was the consternation of its writers that excited me, Michael, and Tanya, knowing this document would be read (continued on back page)



Tamara Chistyakova and Kemer Norkin aboard the cruise ship "St. Petersburg"

Henry George News

published by

Henry George School
of Social Science

121 East 30th Street
New York, NY 10016
(212) 889-8020

Edward J. Dodson
President

George L. Collins
Director

Lindy Davies
Editor

David Domke
Writer

AFFILIATES

LONG ISLAND

Stan Rubenstein, Director
P.O. Box 553
Cutchogue, NY 11935
(516) 734-7543

PHILADELPHIA

Mike Curtis, Director
413 South 10th Street
Philadelphia, PA 19147
(215) 922-4278

NEW ENGLAND

Ernest Kahn, Director
114 Ames Street
Sharon, MA 02067
(617) 784-3086

CHICAGO

Sam Venturella, Director
1772 W. Greenleaf Ave.
Chicago, IL 60626
(312) 338-6698

CALIFORNIA

Wendell Fitzgerald, President
1568 Schrader Street
San Francisco, CA 94117
(415) 661-6933

Harry Pollard, Director
Box 655
Tujunga, CA 91042
(818) 352-4141

Evelyn Friend, Director
5216 Fernwood Way
Sacramento, CA 95841
(916) 331-1490

DOMINICAN REPUBLIC

Lucy Silfa, Director
Apartado Postal 758
Santo Domingo,
Republica Dominicana
(809) 565-6725

CANADA

School of Economic Science
2267 Westman Road
Mississauga, Ontario L5K 1M7
(416) 822-4694

Gaye/Gerry Shaw, Co-Directors
3017 25th Street, S.W.
Calgary, Alberta T3E 1Y2
(403) 242-4291

Public Goods and Private Communities *Review by Lindy Davies*

When a newcomer asks, "Is the Georgist Philosophy a right-wing or a left-wing point of view?", the natural answer is "Yes." Although most social and political movements tend to line up in one camp or other, ours is not so easily pigeonholed. Our conferences attract individuals of every political and ideological stripe, who may agree only on one vital point: that the rent of land belongs to the community. That, however, is a tune that can be played a million different ways. There are many opinions on how the rent ought to be collected, by what agency, at what level of government, and who should decide how to spend it. As much as we proclaim (justifiably) to present society with a "middle way," we must acknowledge the differences among Georgists — and a great many of them have to do with government. How much of it is necessary, and how is it to be made accountable to the people? Should government play any economic role beyond simply collecting the rent? Should it exist at all?

In his new book *Public Goods and Private Communities*, Fred Foldvary examines one assertion about government that has achieved the status of a truism: the notion that government cannot supply public goods efficiently. The reason commonly given is the "free-rider" problem: if access to the public good, such as a roadway or a school, is open to all in the community, then individuals will have an incentive to avoid paying its cost. The alternative has always been for government to finance improvements with tax revenues — and/or public debt.

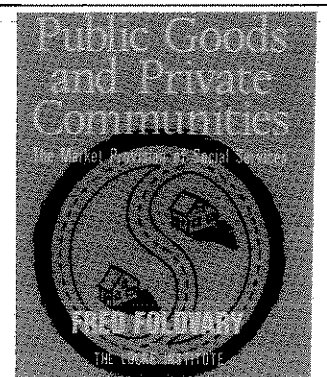
Now Fred Foldvary believes that conventional methods of taxation are destructive and wrong, that they penalize production and ought to be replaced by the community-created fund of the land rent. He has to explain this position to his mainstream readers, but not to us at the *Henry George News*. For us, the provocative part of his thesis concerns how the rent fund ought to be collected and used to pay for public goods — and that ought not to be done by government as we know it today. The public sector, in its attempt to counteract "market failure," has created the worsening monster of "government failure." Government typically provides goods that are more expensive than they need to be, and benefit influential people at the expense of common taxpayers.

Foldvary's analysis seems to establish that the market-failure hypothesis is actually wrong — that there is no real reason why entrepreneurs cannot efficiently and profitably provide all the roads, schools, power grids and sewers that people want. The reason why is the territorial aspect of these public goods, a fact that is overlooked by most theorists. Although public goods are almost always considered to be non-excludable (in other words, available for everyone to use), Foldvary argues that that is by no means necessarily so; many examples exist in which public goods have been freely provided by entrepreneurs.

He details a number of fascinating case studies of such "private communities," including Walt Disney World, the single-tax enclave of Arden, Delaware and the entrepreneur-planned city of Reston, Virginia. In all these communities public infrastructure of all kinds have been very effectively provided by private, contractual arrangements. This method of providing public services, he notes, is much more responsive to the needs and desires of the general population — because people have a direct ability to fire the service providers, not an amorphous stake in the outcome of some future election.

Why is it profitable for private entrepreneurs to provide public services? Conventional theorists have focused on the general citizenry as the "free riders" on openly-provided public goods, but the true free rider, Foldvary notes, is the landowner. Public goods and services, which are normally financed by taxes on production, benefit the landowner in increased rents. If landlords are allowed to retain some or all of those increased rents, then it is in their interest to pay for public improvements themselves. They will provide those improvements with the utmost market-induced efficiency, so as to lower their own costs. The people will get the public goods they want at the most competitive prices, and the wasteful edifice of "big government" will be revealed as a huge mistake. This, Foldvary believes, would allow cities to overcome their seemingly intractable problems of urban decay and public finance; instead of our current, decayed system of city government, he envisions decentralized, "contractual communities" providing just the right services to meet each community's needs.


One might question the applicability of Foldvary's examples to the wider economy.



Public Goods and Private Communities: The Market Provision of Social Services by Fred Foldvary, published by Edward Elgar, Inc. for the Locke Institute, 264 p.

Undoubtedly the entrepreneurial choices made in public-service provision has enhanced the desirability, and hence the land rent, of such places as Reston, Virginia and Walt Disney World; that was the whole point from the start. But such communities exist in a wider society. People want to come to a town like Reston to get away from the disagreeable, crime-ridden city of Washington, DC—and they travel back and forth on federally-subsidized highways. Rental values in Reston are high primarily due to all the high-wage jobs in the nation's capital; for all these reasons, Reston seems an ideal place to locate a "planned community"—and indeed, a number of towns like Reston have appeared around Washington, DC. Other communities, such as blighted areas in DC itself, are not so attractive to private investors. Walt Disney World is, clearly, a unique development whose very singularity is the source of its high rents. And even Arden, by virtue of its history as an arts colony, as well as the fact that other towns failed to see the wisdom of its public revenue policy, became a uniquely desirable place, better at generating rents than its neighbors.

Indeed, it may be that Fred Foldvary has eloquently and persuasively argued a moot point. His analysis of the chosen examples of "private communities" shows that public goods can be provided by private businesses—where is it profitable to do so. A more compelling question might involve the impetus for entrusting government with the provision of services in the first place. Was it because of the "free-riding" average citizen, who Foldvary shows not to actually have been free-riding at all? More likely, it was because the market could not be trusted to provide public goods equitably—given the existence of pockets of poverty and the flight of capital away from them. No one really tries, after all, to argue that the government is more efficient than the market at providing much of anything. But when local conditions have become deeply polarized, larger sovereign institutions have tended to step in to remedy the problem according to some widely-shared conception of human decency or rights. It was never really a matter of efficiency, but one of justice.

The great strength of Henry George's insight as a "middle way" out of our economic dilemmas lies in its ability to reconcile the seemingly opposed forces of efficiency and equity. As George writes, "Liberty is justice and justice is the natural law." It is hard to see how that reconciliation could be effected by clearing the field for "decentralized, contractual communities" to provide public goods for profit, within self-defined profitable areas. 

Editor's Notes

We are thrilled to welcome two new members to the staff at the New York HGS!

Vesa Nelson takes over as the school's librarian, replacing Pia DeSilva, who has left the HGS to finish her college education. A professional (M.L.S.) librarian, and graduate of the school's political economy courses, Vesa is planning to enhance both the accessibility and the breadth of the school's library resources. He has announced expanded library hours (3:30 - 6:30, Monday-Thursday, and others by appt.) and is busily looking into the new information-gathering resources available on computer networks. He asks that students and researchers make their needs known to him, so that he can build the kind of Henry George Research Library that best suits them.

Carmen Crespo joins the team as afternoon and evening receptionist. A P&P graduate, Bible scholar and film buff, C.C. has been enjoying the give-and-take during her first term at the front desk.

Welcome, Vesa and Carmen!

Groundswell Sports New Look

Groundswell, the publication of Common Ground USA, returns with its July-August 1994 edition with snazzy new desktop graphics and expanded scope. *Groundswell* reviews national and international progress in the movement for public collection of land rent. In particular it keeps a knowledgeable eye on tax-reform efforts in this country. Notable letters-to-the-editor, emerging from Common Ground's "letter lobby" initiative, are published here as well. This issue reprints letters by indefatigable correspondents Earl Hanson in Utah, Marvin Saillard in Washington, Frank Nelson in Delaware, Nadine Stoner in Wisconsin and Ben Russell in Arkansas, who have all gotten their Georgist commentaries into the local press.

Subscribers actually receive two publications: Inside *Groundswell* is found the newsletter *Insights*, published by Stan and Marion Sapiro, which offers Georgist perspectives on the news. The current issue focuses on the Russian economy, and also treats such diverse issues as the World Bank, the future for Ethiopia, and the controversy over city funding for sports stadiums.

Readers of this issue also got the annual report of the *Georgist Registry*, listing

movement groups worldwide, and summaries of their activities and progress for 1993.

Groundswell is interested in contributions from readers, particularly Georgist letters that have been published in the press. Inquiries may be addressed to Interim Editor Nadine Stoner, 1118 Central Avenue, Beloit WI, 53511. Non-members of Common Ground USA can get a year's subscription to this bi-monthly publication for \$12.

Andelson Articulates Middle Way

"Henry George and the Reconstruction of Capitalism" is the title of a lecture given by Dr. Robert Andelson at the American Institute for Economic Research this July, and published in chapbook form by AIER, in cooperation with the Public Revenue Education Council of St. Louis.

In his essay, Professor Andelson, who is Professor Emeritus of Philosophy at Auburn University, applies Henry George's economic philosophy to the modern-day search for a just and efficient "middle way" of organizing economic relations.

Appendices contain a bibliography of works by and about Henry George, and a listing of prominent Georgist organizations. Copies are available for \$1.50 from the Robert Schalkenbach Foundation, 41 East 72nd St., New York, NY 10024.

International Georgist Network

From across the world in Melbourne comes an offer from Tax Reform Australia Inc. to "bring Georgists together into 'Geonet,' a worldwide network." To achieve the laudable goals of solidarity, cross-fertilization of ideas, sharing resources and pre-

senting a united front, Tax Reform Australia is proposing to organize an international support system for our movement. When Georgists are traveling, they can look up "fellow travelers" along the route and organize to stay with them. The idea is a proven one. A similar arrangement is practiced quite successfully by another small-but-worthy group, the Quakers, who circulate a directory for "traveling Friends" which facilitates travel and fellowship worldwide.

An additional benefit of this network could be to get our far-flung colleagues in touch through electronic mail and the Internet, which would be an ideal way to coordinate all sorts of plans.

Interested readers may write to us here at the NY-HGS (*continued on back page*)

Yang Yen [circa 780 ad] was a great reformer. He abolished all other direct taxes and reduced them to the land tax only.... The only basis of direct taxation was the land, not the person. It was simple and uniform. The officials could not practice corruption, nor could the people evade their dues.

- From *The Economic Principles of Confucius* by Dr. Chen Huang-Chang (quoted in *Insights*)

Is Russia Ready to Adopt the Theories of Henry George?

Commentary by Prof. Nicolaus Tideman

— Translation by Tatiana Roskoshnaya

The paper reproduced below was written by Olga Kaganova ("a member of the Honorable International Society of Land Economics, St. Petersburg") and Raymond Struyk (Program Director of the U.S.A.I.D. and Co-operation with Russia in Housing). It offers arguments against Russia's adoption of tax policies based on ideas of Henry George. The paper has been widely circulated among Russian municipal authorities. According to Professor Tideman, who comments here on specific points, "Some of the arguments presented by Kaganova and Struyk are completely unfounded. Others reflect reasonable concerns about the manner in which payments for land are implemented, without refuting George's fundamental idea, that governments should be financed by collecting virtually all of the rent of land."

The ethical basis of Henry George's ideas is that, because no one made land, no one can properly claim private ownership of it. The value of land comes from nature, from the growth of communities, and from the provision of public services. Therefore public services should be financed by charges on those persons who are awarded exclusive use of land. And, if governments refrain from taxing labor and capital, that will fulfill the ethical ideal of recognizing each person's right to what is produced by his or her labor.

There is also an important economic efficiency argument for Henry George's ideas. Taxes are generally levied in such a way that people can reduce the taxes they owe by being less productive. (Work less, and reduce your income tax. Sell less, and reduce your sales tax.) The payment owed for each parcel of land, on the other hand, is independent of how productive the possessor of that parcel is — productivity is unharmed when land is the source of public revenue.

Kaganova and Struyk correctly point out that the perceived security of rights is an important determinant of investment. If enough potential investors are alienated by leases, this will be a strong reason for using some other form of land rights. If, however, enough Russians feel that to grant titles of land ownership would be an iniquitous plundering of the heritage of all generations of Russians, that too should weigh heavily in the decision. There is a viable third option: Assign access to land through "titles of private possession," which would grant the right to determine how the land would be used into the indefinite future, be transferable without restriction, for any payment that was agreed between buyer and seller, and oblige the possessor to make regular payments to the local government equal to the rental value of the land.

From the perspective of economic theory, access to land need not be governed by titles of private possession. The choice of a name for the institution of land rights is a matter of deciding between the psychological needs of potential investors and the psychological needs of Russian citizens.

Yes, foreign firms can often take a credit against their domestic profits taxes for payment of a Russian profits tax. However, this is not reason enough for Russia to tax profits. It is as if foreign countries say, "if you will bobble your domestic firms with a profits tax, then we will give our firms a break on their taxes at home." The harm that is done to Russian firms and to the Russian economy by taxing production (rather than land) is not adequately compensated by the tax credit for foreign firms. Taxing land lowers the price of land and removes the superior access that foreign firms have to Russian land by virtue of their lower costs of capital.

The Russian constitution was presented to Russian voters for a single yes or no vote. There may not be majority support for private ownership of land — and even if there is, it is possible that many would find that a system of private possession of land provided the individual rights that they sought. It would be very surprising if Russian citizens insisted on a system of private retention of the rent of land irrespective of its adverse effects on their economy.

FOLLOWERS of the theory of American philosopher H. George — both in Russia and abroad — persistently advise the government of the Russian Federation to follow two basic principles while creating the systems of land relations and taxation:

- a) to preserve public ownership of land and to rent it to private users; and
- b) to increase public revenue mainly by collecting payments for the use of land.

This radical view has wide support in modern Russia. That is why it is important to pay serious attention to this theory....

Practical experience for the proposed system is rather scanty, for there are few governments in the world which implement such a radical program. Those who dared did it only partly. H. George's supporters usually use the example of Hong Kong and several cities in the United States, where a real boom in construction industry took place after the tax on buildings was reduced (though all other taxes were preserved.)

The land tax is attractive for its simplicity. But it is very important to examine the proposed program thoroughly before the final decision is made about its practical implementation in Russia is made. We would like to give the following considerations:

1. Which of the models, "private ownership" or "leasehold" will be more effective for the development of the property market will depend, theoretically speaking, upon the bundle of rights given by each of the models. If in the new land legislation there will be the opportunity to lease land for 99 years, to sublease land freely and to sell the leasing rights freely, then the "leasehold" model will be the stronger.

2. In modern reality legal guarantees of property rights and leasehold rights given by city authorities are not the same. It looks as if property rights received from the State suggest more guarantees. While leasehold rights determined by leasing agreements that state the most important terms, such as duration, review of rent, bases and probable increase of land rent, compensation to the leaseholder in case the lessee does not conform to the terms of leasing agreement, etc. Under the conditions of relatively lawless culture of society, extreme nihilism of town authorities, it is possible to foresee that the leasehold model will produce a lot of cases where interests and rights of leases will be neglected. This will, in turn, influence the flow of investments into city real estate.

3. From a political point of view, refusing to recognise private ownership of land means that one of the fundamental rights of the citizen that is mentioned in the new Russian Constitution is not recognised. It is important to remember that the promise to introduce private ownership of land was one of President Yeltsin's main declarations; should this promise not be fulfilled, it will automatically mean that the reform programs are discredited.

4. The introduction of the proposed reform of taxation will put Russia outside the international system of investment, because foreign capital will be double-taxed. In Russia, investors will pay the full tax which will be called "Land payments" and at home "profits/income tax." If the taxation systems in countries are similar, there are agreements between States about mutual recognition of tax liabilities.

5. There is no other way to determine land rent (if it is possible to do so at

These statements reflect a fundamental misunderstanding of the nature of rent. What economists mean by "the rent of land" is the amount of money that a person would pay for the use of unimproved land in a competitive market. If an owner of land allows someone to use land for less than a competitive market would offer, or uses land inefficiently, the rent of that land is still what the market would offer. The rent of land does not depend on how profitably the land is used. The rent of land varies continuously with location. Two adjacent parcels of land will have nearly equal rents, irrespective of any differences in how the two parcels are actually used.

The assertion that procedures exist to identify the profits of taxpayers will seem quite exaggerated to anyone familiar with business in Russia!

Collection of land rents does require skilled professionals, but it is not highly labor intensive. The identification of rent is not a matter of examining the records of enterprises, but rather of observing the market for land use and applying the proper adjusting formulas.

While it is true that Russian land cadasters are often not up-to-date, this is not a devastating problem. Governments only need to announce that the legal recognition of land rights will be contingent upon the payment of land taxes. Land cannot be hidden. It is easy enough to compare a map of all land with a map of land on which taxes have been paid, and announce that anyone is free to claim the land on which taxes have not been paid.

all) than to determine the revenue received from the property and to try to separate land rent from the total revenue. This is done when assessing the land value according to the income from real estate. But as in any case everything is based on income, which is the base for determining profit, debating whether to tax profit or to collect land rent is more an argument of terminology than an issue of substance.

6. The transfer from taxation of profits to collection of land rents is fantastically labour-intensive, if possible at all. It is well-known that a lot of enterprises disguise their profits, but at any rate, a procedure to register tax payers and their profits exists, and it works. The question is how to register rental income when the majority of legal entities are not the direct land-users, only renting a part of a building and very often not at their legal address, and sometimes illegally. There are no renewed registers which include, at least, official users of buildings, or full land cadasters of direct land users. At any rate, this is the case for the majority of cities. Besides, it is quite obvious that if land payments depend on the incomes of enterprises (and this is, as we see it, the basic idea for extraction of land rent and systematic review of rental payments), it means that enterprises will disguise their incomes as they are doing now with profits. This is the bookkeeping technique.

7. The example given by Georgists of the construction boom in the U.S. cities where taxation of buildings was abolished and they are only paying land tax, can perhaps be interpreted the following way: advantages rarely appear, and then only in comparison with surrounding cities which preserved the former system. But it is possible to imagine that such a reform took place everywhere, as it is proposed for Russia, then the effect resulting from this difference in conditions will disappear. Besides, not long ago, there appeared evidence that if we will fulfil exact econometric analysis, results of the well-known Pittsburgh experiment can be explained only to a small degree by changes in the taxation of real estate.

That is why we have to determine the clear criteria for evaluating the result before we start an experiment on any scale, and these criteria should be analysed by independent experts, perhaps international.

8. Nowhere in the world do they manage to collect the full land rent. This is recognised by Georgists themselves. The full realisation of this idea will possibly destroy the advantages of the centres of cities and their attractiveness to investors. For Russian cities it will be disastrous because centres are in particularly poor condition.

9. Regular review of land rent, for example annually, will of course discourage investors. Obviously, in the course of time, this problem will be sensibly solved. Authorities of those cities who will be especially active will gradually understand that they are losing investors. But now, when there is no experience of sensible land policy, and the cities need urgent investment, such orientation of local politicians can be especially harmful.

Arguments given here confirm our opinion that there are no reasons to adopt the programs of Henry George followers for payments from the land. More than that, we are worried that Russia will start once more to experience new, practically untried ideas. The country once followed this way in 1917 and the results were rather poor.

It is because the rent of land does not depend on actual profits that public collection of rent is such a beneficial way to raise public revenue. The payment that an enterprise must make for the use of land does not depend on its profits, but only on how much someone else would pay to use that land. The incentive for enterprises to make as much profit as they can is not diminished at all by public collection of the rent of land.

No city in Pennsylvania has eliminated its tax on buildings. What 17 cities have done at various times is to shift some of their taxes from buildings to land. Dr. Steven Cord has compared rates of building in some of these cities with surrounding cities before and after the tax changes, and shown that these modest tax changes have induced significant increases in construction. It is plausible that a full tax shift from buildings and production to land would induce a very large response in economic activity.

It may be true that no government collects the full rent of land, but landlords manage to come close. Actually, some governments do fairly well in collecting the full rental value of mineral leases. The trouble is that no government has tried to collect the full rental value of all of its land. It is reasonable to believe that if a government did try, it could manage to come fairly close.

The question of the optimal frequency of land reassessment is worthy of detailed investigation. The answer depends on the volatility of economic conditions. With prices rising as rapidly as they have been in Russia in the past few years, it is essential that land assessments at least be adjusted frequently for inflation.

This again reflects a misunderstanding of what rent is. An assignment of value to land that is so high that no one is prepared to pay it is an improper assessment. Still, an assessor need not strive for absolute 100% land use. Just as a well managed hotel can have a few empty rooms for the travelers who might arrive, a well assessed city can have a few unused parcels of land that new entrepreneurs can acquire at any time. What would make the centers of Russian cities attractive to investors would be the combination of available land at affordable prices and the reduction or elimination of taxes on their productive activities.

How Large is Russia's Land Rent? How Will it be Used? (continued from front page)

on what Russians believe their apartments and other properties to be worth. A typical Russian apartment is about four rooms, and is occupied by numerous family members, often spanning at least two generations. Such an apartment may be valued at about \$80,000, and some indeed are changing hands at this price. The typical buyer is a foreign company with business in Russia, finding it cheaper to pay this price than to put up its executives in one of the foreign hotels.

But what are most apartments worth, or what would they be worth if there were a free market in real estate? To western-trained economists, property values are based on the revenue they can generate. This in turn reflects what renters can afford to pay. A rule of thumb is that residential tenants are able to pay about 25% of their income as rent. Salaries for skilled professionals in Moscow and St. Petersburg average only about \$1200 a year, suggesting a maximum rent-paying ability of about \$300 — or \$1200 for a household of four wage earners. Meanwhile, Russian interest rates are widely advertised at 33 1/3% per year for dollar-denominated deposits immune from rouble inflation. This indicates a property value of only \$3600 for a Russian apartment (\$1200 divided by 1/3).

How can one reconcile this calculation with prices in the neighborhood of \$80,000? How can a Russian family ever earn the money to buy an apartment at these prices? Few Russians are able to save any of their salary, their rouble-savings have been wiped out by inflation, and foreign accounts are illegal. Many Russians are getting by only by selling assets in the thriving market in family heirlooms.

The explanation is to be found in the remarkable way Russia's property rights were created. At the time of the revolution, most Russians simply were given the apartments they occupied and the farms they worked. Eager to extol the virtues of privatization, President Yeltsin wanted to convince Russians of something they wished to believe in any case: that they were getting rich, at least on paper. Some families exchanged large apartments against smaller ones, providing a thin market from which property values were able to take off.

How can today's property values be supported out of proportion to rental income? Part of the answer is that property is becoming a hoarded good. The Russians have learned to fear their banking system. The "vouchers" that each Russian worker was given as equity in his or her company

were worth only about \$25 each. The largest and most popular stock market vehicle — the MMM mutual fund — has gone bust. Real property seems one of the few investments worth having.

For local authorities, how much tax can such properties be expected to yield? Should they be assessed on their current rental income, or on the largely unrealisable sales values their holders imagine them to have?

Obviously location plays a major role, but most Russians do not seem to be very familiar with this concept. Neighborhoods in central St. Petersburg and Moscow remain most desirable, even though high construction costs are needed to bring these buildings up to western standards. For most of the population, prices in the \$80,000 range are far out of proportion to rent-



yielding ability. A typical salary of \$1200 a year, with four wage-earners per apartment (each paying a quarter of their salary on rent), produces a price/rent ratio of \$80,000/1200, or 61 times. This means that it would take a lifetime — over 66 years — to buy an apartment.

In this respect the Russian housing market has experienced nearly as great a bubble as Japan. For most countries, Russian-style price/yield ratios would imply a speculative market, as most speculation is funded by credit. But there has been almost no mortgage lending in Russia. What makes its case even more unique is that the economy is so poor in absolute terms, unlike Japan and America in the 1980s, Holland in the late 17th century or England and France in the 1710s during the South Sea and Mississippi bubbles.

Suppose that a real-estate market would develop, enabling Russian workers to take out mortgages on their apartments — say, just half their value, or \$40,000. This is almost as much as a Russian can make in a lifetime at today's wage levels. Why shouldn't he take the money and run, retire abroad or invest his money at the going 33 1/3% rate of interest and use just a fraction of that yield to pay rent somewhere else?

Mortgage lenders are not so foolish as to lend under these conditions. The result is that most Russians have little choice but to stay put, for nearly everyone has an inflated view of their home values. Indeed, I found that most Russians put an inflated value on nearly every asset they have, from their apartments and rugs down to their collections of phonograph records and family heirlooms. Many seem to be waiting for "the big kill," the sucker who proverbially is born every minute, to dump his assets at an inflated price.

This does not suggest that Western mortgage lenders should hold their breath waiting to load down Russia's land with interest charges. There may indeed be local would-be Donald Trumps eager to borrow money in exchange for pledging the land as security. But could they reap a high enough land-value gain to pay off their creditors and keep a net balance for themselves? How much higher can the price be expected to rise?

"Foreigners" also are making the market for Russian factories, mines and other enterprises. But in a country with no working legal system, where there is no legal recourse against fraud or embezzlement, it is hard to attract foreign investors. I suspect that when one sees a foreign company putting in \$10 million or more into a Russian venture, it may well be holding as collateral the foreign bank account of some Russian directly involved in the operation. An estimated \$13 billion of Russian foreign exchange reserves have simply disappeared, apparently into the hands of the former bureaucracy, which is now drawing on this money to fund its new operations within Russia.

The upshot is that Russia has progressed far beyond the United States in becoming a postindustrial society. One only can marvel that it offers the highest rate of return in the world (33 1/3%), yet has few consumer or capital-goods industries of its own, save for Stolichnaya vodka. When I visited Moscow's statistical agency and asked how it was possible to compile retail sales statistics in an economy dominated by sidewalk kiosks, I was told that the figure was simply based on import estimates for that month! Little domestic production is occurring except for raw materials. The Russians are surviving by selling off assets and treating these sales as current revenue.

This does not leave much room for a credit system to develop. Without credit, there is little way for real estate values to be confirmed in the sense that we Americans

are familiar.

One must conclude that many Russians are being led to confuse democracy and free enterprise with selling off their land, natural resources and industry to foreigners and to the former Soviet *nomenklatura* who got extremely rich at the very outset of opening to the West. Russians feel rich when they look at the prices widely accepted for the real estate rights they have been given, and see 33 1/3% being offered on dollar-denominated savings. Some mutual funds have experienced a remarkable bubble, with returns of 1000% per year being promised, or at least reported if not actually "earned." But the most popular bubbles already have burst. Matters do not seem likely to improve until more Russians recognize the difference between earning money and simply receiving money for selling off assets. As they sink further into poverty, the danger of a real estate crisis grows.

This problem cannot be blamed entirely on communism as such. Nothing comparable is occurring in China, for instance. While Russian land prices in the large cities (and indeed, food prices and most other prices) are nearly those of the United States, China has kept its land prices and other domestic costs low. Russia exports virtually nothing save raw materials, while China is increasing its exportation of labor- and land-intensive industrial manufactures. China enjoys a major competitive advantage in not having to factor high land-rents into these products. It is not hard to guess which economy will be better placed to export its way out of foreign debt. Land rents are an important element of pricing, as are interest charges, taxes, and the overhead of corruption.

As Adam Smith warned, interest rates often are highest in countries going most rapidly to ruin. He also warned that landlords love to reap where they have not sown. His *Wealth of Nations* is now being translated into Russian for the first time. Perhaps it will help alert Russians to the precariousness of trying to create a *rentier* economy without a productive foundation, living by selling its natural endowments and other assets rather than the products of current labor and capital.

To upgrade the productivity of its existing labor and capital will require a credit system based not on lending against land or other collateral that creditors can seize for nonpayment, but against the new earning power that productive credit may help finance. This is the only way that interest-bearing debt has been able to uplift economies. A debt overhead that leaves productivity untouched would be merely parasitic, not productive. ☒

Back to School!

by Lindy Davies

The first lesson in a *Progress & Poverty* course is a touchy thing. Of course, the initial meeting of any class is important for the establishment of authority, rapport and rhythm. Every teacher must do these things distinctively. Some go in with regal bearing and indisputable dignity; others tend to, y'know, hang out — no matter, as long as you establish authority. That is Job #1. You must carefully pick your way between the disciplinarian rock and the hard place of unregulated gabbing.

Remember that teaching is a performance event. The members of your class really do consider themselves to be of a lower rank than you. Disputatious as they might get, students come into your classroom to receive your instruction. They generally do not want too much autonomy — especially at first. This means that as the teacher, authority is yours to lose. If you can demonstrate clear knowledge of who you are, what you're teaching, and how to relate to the administrative functions outside your fiery crucible of knowledge, then most students will happily pay attention to what you have to say.

The teacher of *P & P* has two additional challenges. First, one has to find some way to get people to come back for the next lesson. And, we have to deftly field that sharp question that's on most minds: "What's the catch? Is this some kind of cult or something?"

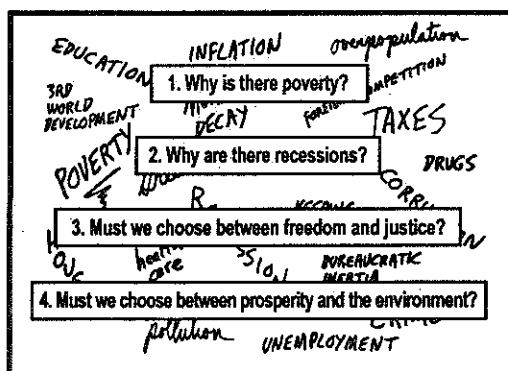
"Political economy deals with various and complicated phenomena," wrote Henry George, "yet they are phenomena which may be resolved into simple elements, and which are but the manifestations of familiar principles." This is not a partisan statement, but rather a very reassuring one, indicating that a meaningful understanding of economic issues can be had without the benefit of advanced training. What we can offer our students, apart from any specific reform proposal, is "a free course that sheds light on today's baffling problems." If they think they really can get that here, then they'll come back!

The first lesson is a good time to focus on those problems. One way to do that is to list them. Ask the class to name all the economic problems they can think of. The teacher will then write them up on the board, in (apparently) no particular order. Things will seem to be getting more and more confusing for the poor students, and "This," you say to your skeptical class, "is a fairly accurate picture of what most people think of when they hear the word 'economics'." You won't get much disagreement on that point!

You seemed to be writing that list of problems up on the board impulsively, helter-skelter — but there was method in your madness. You have placed certain "right-wing" issues like taxes, crime, "big government," etc. on one side of the board, opposing "left-wing" issues such as poverty, housing and education on the other. In general, you have opposed opposing issues (like inflation and unemployment — or population and environmental destruction)

in such a way as to highlight the ostensibly intractable contradictions of economic policy. Noting these connections, you can then lead a discussion in which the class draws connections and comes up with a list of basic questions that a course in political economy must deal with. For added visual effect, those questions can be recorded right over top of the mish-mash you've already generated: order emerges (potentially, at least) from chaos!

TEACHERS' CORNER



Volga Economics

(continued from front page)

internationally. My favorite quote, which Michael and I thought carried more weight than any other, was "Land tax is attractive by its simplicity... it is very important to examine the proposed program thoroughly before the final decision about its practical implementation in Russia is made." At first, we considered this to be merely a rhetorical flourish — but after hearing from Russian participants later in the conference, our excitement increased as we realized that the authors had meant what they said about widespread support for George's ideas!

By night, our meeting room served as a disco, complete with a dance floor, loud music, and flashing neon lights. By day, the room simmered with ideas and information. Galina Stepanova, chairperson of the land committee of Kingisepp, a subregion of St. Petersburg, detailed the geography and economics of her district. She reported on the taxation office, noting that they are able, for the most part, to collect land taxes, but that it is difficult to force the enterprises (businesses) to pay on their leases. She said that although paying for the land is not seen as particularly burdensome, people still don't want to pay. Galina admitted, "I feel like I am two people — one person who understands Henry George and the importance of collecting land rent — and the other person who [must make a living as] a civil servant."

Another female speaker, Galina Kubasova, serves as deputy mayor of her town, Kostomuksha in the republic of Karelia. She said her city is very young — ten years old — and that is why they do not have the problems reported by other speakers. She added, "Ecograd got us to participate in the land rent program, and we saw this as a safety belt. Officials of the city support us at all levels and they are ready to help us with programs connected with land rent." From Kostomuksha's chief architect, Sergey Leushev, we heard about land rent for city development. Fred Harrison met with the Mayoralty and assisted in data collection. Sergey said, "we have started to lease our land... we already feel some results... bit by bit we are going to achieve our aim."

In a final presentation to our conference group, Tamara Chistakova of Ecograd spoke on the Center's work in St. Petersburg in a report entitled, "The Complex Economic Assessment of Territory." Tamara detailed the assessment methodology that Ecograd uses. Responding to Irene Hickman's question, "Does it (Ecograd's assessment) include housing and what is needed?" Tamara answered with a resound-

ing, "Da." She continued, "We analyze the plans that exist and make corrections from the point of view of what is better for a certain area. We define the degree of harm which taxes are doing to this particular area, and we fight against it."

Irene expressed heartfelt gratitude at her news, and that seemed to exemplify our responses to all the positive reports we'd heard from the Russian speakers. It was wonderfully exhilarating to cruise, as we did, from town to town, optimistic in the knowledge that each would be a new adventure. Yes, we knew it would be a long hard pull — but in that heady, lovely Russian setting, the promise of Georgist economics in Russia seemed as certain as our camaraderie was joyous.

Editor's Notes

(continued from page three)

(or email to hgsld@echonyc.com) for more information on the Geonet, and a free copy of the questionnaire.

"Back to Earth" Appeal

Fred Harrison and London's Centre for Incentive Taxation have been tirelessly at work promoting the cause of public collection of land rent in Russia. But Fred has also been working on ambitious publishing projects. The next offering will be called *Back to Earth*, and will complete a trilogy that "reappraises the cultural foundations of our society." *Back to Earth* "explains how society could be reconstructed along the lines of the Georgist paradigm." The first two books, already in print, are *Costing the Earth* and *Now the Synthesis*.

The scholarly work is done, but the Centre needs financial help to complete its project. Fred Harrison asks everyone who believes in its importance to send as generous a contribution as possible. Checks from the U.S. and Canada may be made payable to the *International Union*, and sent to this address, c/o the Henry George Institute.

Our Need of a Vigorous Journal

by Mason Gaffney

(Editor's note: We all know Mason Gaffney as one of the most respected and accomplished professional economists who "sees the cat." But the following excerpt from a 1974 article shows some fine, cranky Mark Twain wit, while making a point that still deserves hearing.)

Some of the characteristic faults of Georgist journalism are the following. It is too often amateurish, peevish, cultist, preachy, ego-tripping, accommodating to patrons, incestuous, slanted, quarrelsome, dogmatic, cranky, scolding, narrow, nitpicking, self-righteous, arrogant, conceited, other-worldly, idolatrous, negative and bitter. The same writers repeat and repeat, narrowing the circle and boring the reader. There are frothy opinions without punch or substance. There is brash presumption ("We know, why are you so dumb?") There are vain attacks on assorted innocents merely for ignoring us. There are selected quotations from big names who contradicted themselves the day after. There are too many cheap shots and easy debater's points, too little deep and hard research and analysis. (Is research dull? What was the best news story of 1973?) There are too many obituaries, too much in *laudam temporis acti*. There is refusal to play in anyone else's ballpark — all issues must be redefined in our terms. It reminds one of William Jennings Bryan at the Scopes "monkey trial" in Dayton, Tennessee, — and you remember what happened to him.

Henry George School of Social Science
121 East 30th Street
New York, NY 10016

Address correction requested

Non-profit Org.
U.S. Postage
PAID
New York, NY
Permit No. 7759