

# Debt Death and Deadweight

## CHAPTER 4

# Denmark: the constitution of a happy nation

Lasse S. Andersen

**D**ENMARK is one of the European nations that can be held up as a model for others to emulate. It is evident that this small Scandinavian country has accomplished things that are universally envied. For many years it has been ranked as one of the happiest places on earth, seconded only by Norway in 2017. It is the least corrupt country in the world according to Transparency International. And it has the best quality housing stock in Europe, measured in terms of living space.

These outcomes are the result of many things, not least the country's long and peaceful tradition of compromise and cooperation in parliament. But it is also to a large extent the result of Denmark's long history of taxing and regulating the housing market.

This history begins early in the 19th century when Frederick VI, who ruled from 1808 to 1839, abolished hereditary servitude and liberated the peasants from the landlords. This allowed a new class of smallholders to emerge. And in the same period, a system of land taxation - the so-called *hardkorn* tax - was introduced by the liberal-minded landlord and nobleman Count C.D.F. Reventlów (1748-1827). This tax was basically a tax on the estimated produce of land and it ensured that a steady revenue flowed from the large manor houses and rural estates to the crown. As such, however, it was clearly designed for an agrarian society and it gradually grew insufficient and unfair as industrialisation and urbanisation progressed during the 19th century.

In 1903, the government abolished the *hardkorn* tax in favour of a tax on income and property in general. This government, however, was dominated by landlords and large farmers who, in effect, tried to shift the tax burden away from themselves and onto the small farmers, the industrial workers, and the urban elites. The property tax was particularly hurtful to the small farmers because it was a tax on buildings as well as land and, naturally, buildings

constituted a higher share of the total value of their small farms. Luckily, the small farmers were highly organised and educated due to the existence of rural folk high schools, created by the priest and politician N.F.S. Grundtvig (1783-1872). A counter-movement quickly took hold in many of these schools.

The small farmers wanted land to be liberated from the entailed estates of the noble landlords and they wanted to implement a system of land value taxation which fell equally on all land – urban sites as well as farm land. They had been inspired by what had happened in the 1880s. That was when a debate had arisen in Denmark about the merits of the solution proposed by Henry George, the American social reformer whose book *Progress and Poverty* had made it clear that the rent of land was the only ideal and just source of taxation. A group of folk high school teachers led by Jakob E. Lange heavily influenced the public debate on the issue of tax reform, and by 1905 they were represented in parliament by a new political party, the Radical Liberals, who demanded and quickly achieved the regular revaluation of all land for the purpose of taxation (Lefman & Lassen 2000).

And so, because people reacted to the shifting of taxes in 1903 and steadily gained more representation in parliament, the tax system was gradually improved. In 1916 all the land in Denmark was revalued. In 1919 all entailed estates were abolished, liberating a lot of idle land to productive use. And in 1922 and 1926 property taxes were replaced by a general tax on land values, with the gradual removal of taxes on improvements on the land. Also, a system of regular revaluation of all sites was initiated; a system which has continued – in various guises – to this day (Müller & Mørch-Lassen 1989).

Denmark was one of the richest countries in the world by 1930, and in spite of the Great Depression its economy kept growing in strength and enjoyed a Golden Age in the decades following World War 2. With the subsequent growth of the welfare state, however, the income tax quickly became the primary source of public revenue, and the revenue from the land value tax, which reached its peak in 1960, fell in proportion to the income tax and, later, also the consumption tax (VAT). In 2015, the revenue from property taxes accounted for about 4 % of total tax revenue.<sup>1</sup>

## A civilized housing market

Even though revenue from the land value tax generally has declined since the 1960s, this fiscal policy has nonetheless contributed significantly to stabilizing the housing market. Along with some key regulations, it has safeguarded the Danish market from the excesses of property speculation which distort the London property market. Foreign nationals operating as

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1. <http://www.skm.dk/english/facts-and-figures/the-tax-structure>

cash-rich speculators can buy and sell houses and apartments in the British capital purely to make a quick profit. Alternatively, 'hot' cash can be invested in upmarket dwellings (and left empty) as a safe haven for investors who do not wish to risk their money in the stock markets. This is not permitted with real estate in Denmark. Section 1(1) of the Acquisition of Real Property Act stipulates that persons who are not residents of Denmark and have not lived in the country for a total period of five years previously may only acquire title to real property after having obtained permission from the Ministry of Justice.<sup>2</sup>

Since 1972, because of the fear that Germans would buy all the summer houses near the beaches, Denmark secured an exemption from EU rules to protect the ownership of these dwellings. Some cities have (on a dispensation from the rules) allowed foreigners to buy city houses to be used for vacation purposes. The owners are, in the main, Norwegian nationals in northern Jutland. But they have to demonstrate a relationship to Denmark, such as having a history of vacationing in the area for many years.

Long-term vacancy of properties is discouraged in Denmark. If an owner moves and does not wish to sell his property, he must rent it out - or at least try to sell it. If a property is empty for more than six weeks, the owner has to report to the municipal authority, which then seeks to provide tenants which the owner has to accept. This is why, in Copenhagen, we would not experience the situation that existed in London, where 1,652 high-value properties were vacant for up to two years in the borough where an estimated 80 people were burnt to death in Grenfell Tower in June 2017. Of the survivors, only 12 households had been re-accommodated a month after the inferno, with dozens of people living in temporary accommodation. Some of the owners of the nearby vacant properties included foreign royalty and east European oligarchs. More than a third of their properties had been vacant for more than two years (Batty *et al* 2017).

Because vacant land is subject to the land value tax, property owners in Denmark have an incentive to ensure that the dwellings are occupied. Urban sprawl does therefore not blight Danish cities as it does cities in other countries. And anyone in Denmark can log onto the government's website and view the valuation of each site in the country. If the land value tax was returned to its former glory and levied at a higher rate, the regulations mentioned above, which limit the liberty of the owners, would be less necessary, but in the absence of a substantial land value tax, they have proven to be very beneficial for the housing market.

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2. <http://justitsministeriet.dk/arbejdsomraader/civilret/foreign-citizens-acquisition-real-property>

## Politics and property owners

Almost all politicians in Denmark are reluctant to go against the interests of the country's many home owners. In the autumn of 2016, however, the level of anxiety among politicians reached a high-water mark when a new and improved system of land and property valuation was presented for implementation by the Ministry of Taxation. It was estimated that the new system, because of its accuracy, would cause taxes – especially the land value tax – to spike in the large metropolitan areas, which had been substantially undervalued for decades. For this reason, mainstream politicians quickly initiated talks about how to protect property owners from future tax increases. The result of these negotiations was a broad settlement about property taxation that heavily favours the current home owners.

The present minority government is composed of three political parties: the center-right Venstre, the Conservative and the Liberal Alliance parties. The latter two wanted to abolish the land value tax completely (claiming that they saw no justification for this method of raising revenue). All three parties shared the desire to render the property tax less progressive, but they were opposed in this by a majority composed of the other six parties in parliament. And so, on May 2, 2017, the Danish government concluded a settlement on property taxation with three of the opposition parties. Thus, six parties out of nine represented in parliament supported a settlement that was intended to ensure that the new and improved system of valuation (which would come into operation in 2018/2019) did not generate a higher total revenue from property taxation. This, however, was only the latest in a line of political initiatives that were supposed to stabilize the property market and prevent property taxes from rising exorbitantly.

- ▶ In 2002, the center-right government tied the estate tax to the then nominal value of property.
- ▶ In 2003, an artificial ceiling on the land value tax was imposed. The change permitted an annual increase of no more than 7% on land values, which meant that the land value tax in most cities lagged behind the actual development of the housing market. Because of this artificial ceiling in particular, 90% of all land was not taxed on the basis of its market value in 2014.

The coalition government's settlement abolishes these defects. But the price of returning to the status quo ante is extremely high. To safeguard property owners from higher taxation, the rate of taxation will fall dramatically. The floor beneath the land value tax, which has hitherto been at 1.6% of the assessed value, is abolished, and the previous maximum of 3.4% was reduced to 3%. Municipalities have been instructed to lower the tax rate if their

expected total revenue from property taxes exceed the revenue they collected before the implementation of the new system of valuation.

Furthermore, current owners will receive a permanent tax deduction equivalent to the nominal difference between new and old taxation. If the value of their land/property increases, they will be taxed fully on the margin, but the fact that the deduction is permanent means that they will be undercharged for as long as they remain in their homes. Payment of increased taxes may be deferred, becoming a form of mortgage: a debt to the government which can be discharged from the proceeds when the property is sold. The debt is interest-free for increases 2017–2020, after which interest will be payable. But home owners can opt out of this scheme after 2020 and pay the increased taxes. *Why make a charge simple when you can make it complicated – and at a later date, using the complication as an excuse for abolishing it!*

The outcome of these initiatives means that the settlement will result in a very unequal taxation of land values between regions as well as between neighbours. Because the old valuation system, as well as the artificial limitations on property taxes, favours the large cities at the expense of the more rural locations, the largest deductions and the largest lowering of rates will occur in the municipalities of the largest cities. Copenhagen, in particular, is favoured over the other cities of Denmark.

We may suspect that the measures taken to curb the taxation of land and property are based on political fear of property owners. Commentators suggest that the possibility of repeal and reform is minuscule. But if this bias in fiscal policy does persist, it entails the risk of jeopardising a key building block of the social solidarity which has characterized Danish society for more than a century.

## Bibliography

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