

# Who Should Support Property Tax Reform Along Georgist Lines — and Why?

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NO TAX ON LABOR. NO TAX ON CAPITAL. The vision of Henry George! Unrealistic today. But the vision does challenge us to do what we can<sup>2</sup> — move in the direction Henry George advocated.

## **To a Better Life**

First, as to the “Why?”

Man-made capital is enormously valuable for human well-being. Housing, hospitals, factories, machinery, pipelines, refineries, computers, electric and telephone equipment, sports fields, streets, school buildings, and innumerable other types of man-made capital influence — improve — human life. The quantity is limited — but expandable. We add to it year by year. Quality varies; some is mediocre (slums), some superb (a modern surgery). More and better capital improves the quality of life.

Land also plays a vital role in human well-being. But the quantity of land is not expandable (with minor exceptions). Nature fixed the amount. For meeting human desires some land is better than others. Fertility affects agricultural output. In cities especially one sees that location can be excellent or poor for meeting needs. No two locations are exactly the same.

Property tax revisions that involve no net change in revenue can enable communities to (1) enjoy expanded quantity and improved quality of man-made capital and (2) induce land use that more fruitfully serves residents as consumers and businesses as producers.

The tax reform we propose would have other benefits, more than can be discussed on this occasion.

What is “the” Georgist Property Tax Program?

Henry George’s writings cover a broad range. And among persons who wish to see his wisdom utilized today, the emphases differ. On some elements there may be essential agreement. But moving from the general to the specific, disagreement arises. Much time can be spent discussing one or another feature — and the “whys” relative to each.

Economists speak of “one instrument for one goal;” two fiscal or monetary instruments are insufficient for reaching three macroeconomic policy objectives. Agreed. But ours is an economy with numerable interdependencies. The use of any major instrument will exert forces producing many results, promptly and over time, some large, some small, and with surprises. Changing the structure of property taxation will have a variety of consequences. Some proponents emphasize one probable result, others something different.

The concern here focuses on revenues from property tax as a way to pay for government, but matters of land use will get some attention. The starting point is today — not a century, a generation, or a decade ago. Lawmakers cannot be expected to act now as if unearned increments of the past could be captured for public purposes — as can many of those of the future. Past is past. What was done and not done limits us today. But a long future lies ahead in every country despite differences in circumstances today.

First, let me start with what seems to me to be realistically possible in the United States in the foreseeable future: (1) reduction in tax rates on buildings, equipment, and other man-made capital; (2) increase in rates on land to keep total revenue stable.<sup>2</sup> (The changes to be made in stages so that quite substantial totals would build up over, say, five to eight years without large shift at any one time.) Before many years the tax on buildings and other manmade capital could be low enough so that it would have minimal adverse effect on construction and other investment.

This is the prospect that should enlist, even enthuse, support for the proposal in the United States.

Conditions differ from one community to another. I do not urge that the changes alter the level of government revenue or spending. The issues involved can range rather widely. Everyone here, I expect, can suggest variants, good ones. But to include them

in the discussion here would be diversionary, distracting attention from the central issue.

Ideally, I believe, a (much) larger portion of government revenues “should” come from land rents (user fees). The highest marginal rates of income, consumption, and payroll (social insurance) taxes could be reduced with one or several of non-revenue benefits for society.

The possibilities in other countries depend upon many factors. Greater use of land rents could replace elements of revenue systems which must substantially and adversely affect human well-being. How well are the principles of land rent understood over the world? My guess is “most inadequately.” Margaret Thatcher in discussing her proposal to replace traditional rates on residential property with a community charge seemed not to distinguish between land rents and returns on man-made capital. (Ch. XXII of *The Downing Street Years*: “Any property tax is essentially a tax on improving one’s own home.” p. 664)

### **Beneficial Effects**

The changes in tax rates (total revenue unchanged) would:

(1) reduce tax obstacles to modernization, new construction, and acquisition of new machinery and equipment and

(2) put pressure on landowners to make more fruitful use of land where the market signals such possibilities.

Desirable results? Certainly.

### **Everyone a Potential Supporter**

Who should support the proposal? Everyone. Or almost everyone. The change would improve the economy — the community as a whole. Everyone is a part of the community and would share in benefits. But, in most cases, alas, without awareness of the fact. The fruits would be widely diffused, spread broadly, and not dramatically immediate but maturing over years. Real property is so large a portion of the community that any feasible tax change will take time to work its full effects, and some of them will not be identifiable as results of tax reform.

Exceptions to my “everyone” will appear. Owners of land in uses well below its potential would face higher tax bills in the immediate future. (More on this later.)

## **Homeowners (Owner-occupants) Should Support**

Homeowners have decisive voting power. In direct, immediate self-interest they should vote for the change. Most of them would benefit at once and more generally as time passes. Studies show that initially most homeowners will have somewhat lower tax bills, but usually the reductions are by only a few percent. What determines will be the ratio of land value to the value of structures. Typically the assessed value of land is considerably below that of residences. So the net effect of the reform will depend upon the relative changes of tax rates.

Over time the higher rate on the land would tend to be capitalized into lower land prices. The effects on structures of the tax change would depend upon a variety of factors — e.g., costs of construction and market changes in supply and demand for housing.

Homeowners will face conditions more favorable to expansion and modernization. The extent to which home improvements are in fact reflected in higher assessments will differ. So will owner perceptions of what will happen. But in any case, conditions become more favorable; human beings gain some freedom to obtain better housing because tax effects are less unfavorable.

How can recognition of such potential benefits be mobilized to affect attitudes when the proposal is under consideration?

## **Renters**

Persons who live in rental housing might well see no persuasive reason to favor or to oppose the tax reform. The net effects of tax revisions and changes in market conditions attributable to tax reform would probably exert slight net influence when leases come up for renewal. For renters as voters indifference is more probable than any significant support or opposition.<sup>3</sup>

## **Effects: Construction Encouraged**

Financing government from higher property tax rates on land and lower rates on improvements would have less — eventually perhaps no — deterrent influence on construction or on the purchase of new machinery or on the timing and size of holdings of business inventory. Computations of the weight of present taxes on man-made capital vary from locality to locality. In some communities tax rates are high enough for the present value of future property tax to be the equivalent of a sales tax of twenty to twenty-five percent or so.

Certainly the tax restructuring would tend to encourage additions to the quantity and quality of housing. Rental charges would fall as tax reductions encouraged increases in supply. Benefits would accrue to a minority initially but would gradually spread. Would increased supply tend gradually to reduce the prices of existing structures? Perhaps somewhat in some communities but the effects would more likely be “lost in the shuffle” of forces that affect housing prices.

The amount of new building would, of course, depend upon the availability of capital. What can happen in the first relatively few communities to act should not be expected for the whole economy. Always there are funds for some new houses — but for a large number the forces can be rather different. Pressures on capital supply would tend to raise interest rates (and thus, among other things, reduce land prices).

### **Businesses, Including Agriculture**

Most businesses would pay less tax. Biggest reductions would go to companies that use large amounts of machinery, equipment, inventory, and structures. The net effect would depend, of course, on the ratio of land value to the worth of structures and equipment. Competition would tend to pass the benefits to consumers or employees — with enormous variations in the speed and the distribution of change.

Electric, gas, telephone, and other public utilities with large amounts of man—made capital relative to land would benefit, perhaps greatly — except. The exception: For generations taxing consumers through utilities has had political appeal. Lawmakers would be tempted to make provisions that would permit relatively heavy taxes on utilities to be passed on to consumers as hidden burdens.

Farmers use typically much land relative to man—made capital including that which, embodied as investments in land, has become real property. The total real estate tax burden on farmers would depend predominantly upon government spending in the jurisdiction. My proposals would not, it seems to me, likely change the total taxes of farmers (assuming that local government spending is not also changed). But one can predict that the political influence of farmers would often be successful in pressing favorable treatment.

### **Effects on Land Use**

The quantity of land is fixed, and not all is used to best advantage. Henry George and many of his followers have emphasized the desirability of making more land available for higher and better — “higher and best” — use. An annual charge (tax or user fee) would create inducement to better use, as against (partial) idleness, of land. Land use

is important to human well-being in many ways. Think of commuters who drive, hundreds of times a year, through rundown urban areas to reach their homes.

Urban sprawl. The demands for streets and utility facilities! Society can overcome some of the disadvantages of fixity of the supply of land and its immobility by creating inducements to better use. By “better” one means use that reflects as fully as possible the many forces that result from human actions and desires to act in the market. A policy to induce better use would be a counterpart to increasing the quantity and quality of capital and labor.

Each community will have opportunities and problems specific to it. Is there a social or community concern if an owner chooses to sacrifice income by keeping land below its potential use? Yes. Why?

Land does differ from other property. Each location is a monopoly. It cannot be duplicated exactly. The productive process does not provide for the creation of new land in the way that competition so generally provides for overcoming exploitative industrial monopoly and speculative withholding.

The third-party neighborhood aspect of land does make it “different.” Any use, underuse, or non-use affects others; they cannot count upon market forces to create duplicates.

Speculation appears frequently and as an evil in Georgist discussion. And with land there is a difference from so many objects of speculation. The supply is inelastic. New land cannot be created (or only rarely). And substitutes for location are limited and perhaps more than just slightly unsuitable. The upside potential for price — well, a long history in many places records much optimism that merges into fantasy.

Over time much land has risen substantially in price. Speculators have profited from holding a naturally created resource in less productive use than people using their market power would have paid for.

Requiring owners to use more of the economic rent to pay for (local) government would increase pressure for earlier and fuller use of land as indicated by market forces.

The term “urban sprawl” lacks precision. But it does convey meaning in characterizing conditions in many places over the world. My time does not permit comment here. But as to the substance of this paper, one can assert with confidence that the tax reform proposed would contribute to reduction of the human loss and distress attributable to urban sprawl.

In this connection, two distinguishable public benefits could be attributed to the results of the proposal. (1) More of unearned increments would be used to help finance government. We are familiar with this argument. (2) Higher taxes on land would reduce price and the potential for dreamy pictures of higher prices; the tax change would also tend to enlarge the availability of land in the market. Speculative price increases would tend to be reduced. Lending institutions would presumably moderate the financing of land price increases.

Poor loans on land have caused no small amount of distress for the public, innocent (unconnected) bystanders, as financial institutions have been forced to reduce lending generally. Contractions in the banking sector forced by bad real estate loans aggravate and even cause business depression. The net benefits to the general public of more stability of land prices could be great indeed as against repetition of bubbles and busts of the past, at many times, in many places.

Yet “speculation” is also a term lacking precision or at least general agreement on its meaning. Some land development of a constructive nature seeks to produce rewards for the entrepreneur in the form of increments of value of land. I can offer little help at the moment except recognizing a complicating reality.

### **Construction Industry:**

Builders, Architects, Labor, Suppliers

The reduction of property tax obstacles to building would benefit a wide range of persons and organizations engaged in building. They would have self-interest in supporting the proposals. How much so? I cannot suggest magnitudes. A temptation to overestimate goes along with advocacy. But the direction of incentives provides solid basis for support. In local politics the focused influence of builders and organized labor can make a significant difference.

Because higher taxes on land would tend to be capitalized in lower land prices builders and buyers would need to pay, and to borrow, less to acquire land. But the total annual carrying charges would not be much changed. More would have to go to government and less to lenders because less would have to be borrowed. Formal debt would be smaller since the obligation to government for taxes is not capitalized into debt.

Developers should welcome any such easing of financing. They would need less capital to operate. Buyers of houses and other structures would borrow less and pay less interest but for the land element pay more to government each year.

### **Probable Opposition**

Guessing, as I must, about reactions can indicate possibilities. Probabilities. But magnitudes are unknowable — especially when the sizes of changes are unknown and must vary widely from place to place.

Owners of land that is in use well below its potential would face higher tax bills. If assessments do reflect value in possible as against actual use, taxes would go up. A few persons with rather much at stake can be expected to focus effort. Intense feeling can outweigh a widely dispersed total of many small interests. An old story in matters of the mobilization of public opinion~ Would owners see any offsetting factors? Complex considerations arise. Land on which building can begin without costly demolition or other obstacle might become more valuable as lower taxes on new buildings tip the balance in favor of construction sooner as against delay. Where existing buildings have several years of useful life ahead but are worth appreciably less than the land, the owners will probably be worse off until new development is feasible.

Higher taxes on land will tend to be capitalized into lower land prices. The total of effects will depend upon several conditions. The fact that capitalization will affect land prices by some multiple of the change in annual tax creates persuasive reason for gradualism. Discounting of the increases to take effect in the future will moderate somewhat their immediate burden.

From one community to another the amount of substantially underutilized land varies considerably. Underutilization of land imposes costs on the community, the humble and the leaders. Living is not so good as it could be. Most of the deprivations, of course, are unrecognized. But, to repeat for emphasis, they cannot be fully offset by market forces because of the inability of the market to create land or to duplicate location.

### **Support from Professional Economists**

Although I recognize that the subject has not been prominent in academic circles for years, I believe that professional economists rather generally support the principle of using land rent to help pay for government. A century ago, as Prof. Mason Gaffney has pointed out, mainstream economics merged land with man—made capital for theoretical purposes. The significance of pure rents as a source of government revenue then tended to be ignored or overlooked.

A survey of public finance economists in 1934 found that fifty-four percent favored lower rates on improvements than on land. In 1994 the figure was forty-four percent. If the possibility had been less generally ignored in professional discussion for decades, the conclusions today would, I am confident, have been more generally



favorable. Among economists aged twenty to thirty, two thirds (sixty-seven percent) were in favor, among Ph.D.s, the figure was forty-four percent.

In 1990 when a group of economists were solicited by telephone, quite hurriedly, for a letter to Soviet leader M. Gorbachev endorsing the use of land rents to pay for government, thirty supporters were enlisted readily. Seven Nobel prize winners endorsed the principle.

Rent-seeking (including more than land) has received considerable academic attention in recent years. This awareness must tend to alert economists to the attractiveness of land rents as a source of funds to help pay for community services. An educational, alerting effort would enhance awareness but hardly mobilize academicians to act in spheres of lawmaking.

### **Civic Leadership**

Ideas of merit, even great merit, do not implement themselves. People must act. Where general public interest is involved, civic leadership is called for. Putting into place policies for community affairs requires more than self-interest expressed through the market.

Sometimes one or a few persons or groups formed for other purposes will have enough direct interest to press a program. Typically, however, more is needed. Public spirit! The desire to help make a better community! Through a long history public spirited individuals have formed groups and pressed for action. Henry George was such a person. Success calls for a lot more than a good cause and the best of intentions.

Property tax reform would benefit the community as a whole. Most individuals, however, would receive only modest direct benefits. As members of the public they would benefit but in ways rarely identifiable. Individual benefits would rarely, I fear, be great enough to inspire the effort required to change government policies. Leadership has an indispensable role.

### **Concluding Comment**

Everyone would benefit. But where can we look to mobilize effort? Perhaps, somehow, organizations such as those in the Georgist movement can enlist and inspire the support that will lead men and women to do what is doable in utilizing old knowledge to yield new benefits.

Notes

1 Mr. Perry Prentice had for decades a leading role in the TIME publishing organization. He served for years as an active president of The Robert Schalkenbach Foundation. He drew upon unmatched experience with various elements of housing, urban planning, architecture, and building generally. Unfortunately, he died before he could complete a book that drew upon his long experience. But he did publish three articles in *The American Journal of Economics and Sociology* (1976). They have been combined in a single reprint, "Urban Financing for Jobs, Profits and Prosperity," which is available from the Schalkenbach Foundation, 149 Madison Avenue, Suite 601, New York, NY, 10016-6713. I owe a great debt to his work. This paper, however, deals with less ambitious reforms than assumed in Mr. Prentice's discussion.

2 See Steven Cord, *Twelve Formulas for Converting a One-Rate to a Two-Rate Property Tax* (Center for the Study of Economics, 2000 Century Plaza, #238, Columbia, MD, 1994).