Real Property—Not One Class But Two

by NOAH D. ALPER

WE ARE especially concerned with the taxation identified as real property in the Constitution of the State of Missouri. Natural site or land locations held in ownership through title, and improvements placed in or on the land, are very different kinds of property—yet we are compelled to assess and tax these different kinds of property as one class.

The general property tax was once the greatest single producer of income for both state and local governments, but after the 1920-30 collapse a trend was started to lower real estate taxes or eliminate them altogether. That trend is being seriously questioned and re-examined by economists and a 16-page special report in Nation's Cities in 1965, inquiring "Are Property Taxes Obsolete?" began with the premise that "reforming local taxes is at least as urgent as reforming taxes at the national level." The report went on to consider how taxes could be raised in a way that would help rather than hinder the right kind of urban development, with local governments assuming more responsibility for local needs.

It was explained in the report that "taxes on land tend to encourage, speed, or sometimes even compel improvements. The bigger the land tax the bigger the pressure on landowners whose property is under-used, to do something to increase its earning power or sell it to someone who will."

The greatest good can come to the great majority of our people by treating land and improvements as different classes of property and by taxing them at different rates, or preferably by taxing the location of land while exempting improvements from taxation entirely. I am sure it is an understanding of these principles that caused John H. Poelker, Comptroller of the City of St. Louis, in his appearance before the Commission, to declare that we should have different formulas for the taxation of land location and improvement values. He recommended that assessments on land be 100 percent of market value, while improvements be assessed at only 25 percent of their depreciated value.

Experience shows that when taxes on improvements are abolished and the revenue is raised exclusively from location value or rents, 80 to 90 percent of the people pay lower taxes on their homes. The effectiveness of this method is evidenced by the fact that in countries [Australia and New Zealand] where taxes were shifted from improvements to location rents, only the property owners were permitted to sign the petition and vote on it.

But are we in the U.S. sufficiently concerned about equality of property taxation? Studies show we are not. The report in Nation's Cities found that "gross inequalities in assessing are widespread, universally recognized, and tend to be taken for granted . . . Few officials feel under obligation to enforce the tax laws as written. The average assessor makes himself a sort of one-man legislature. He, not the state constitution and the state legislature, defines local taxing and borrowing power."

Because of actions lately taken by citizens toward full market value assessments, a number of states have been compelled to equalize assessments at full market value. This could mean

Noah D. Alper, President of the Public Revenue Education Council, St. Louis, was invited to appear before the Missouri State Tax Study Commission. His paper was distributed to all members of the Commission. This is a short version of his thorough and well documented presentation.

benefits for those who improve their land up to its use value, and penalties to those who hold vacant or poorly improved land.

The federal government gives grants in aid to states for use in ways that add location value to land privately held, yet it gets its revenue from non-property taxes. Presumably property taxes are left for local use, but local governments have largely substituted non-real estate taxes for real estate and other property taxes.

Our citizens, famed for having a government "of the people, for the people, by the people," are being "hooked" with higher prices of land and also of products and services, by reason of bad taxation. This greatly nullifies the ability of our free enterprise economy to lower prices and make more and better goods and services available for less.

Investors who seek profit in buying and selling real estate or in the construction of buildings have a direct interest in real estate taxes. Renters of homes, apartments and rooms are seldom so directly concerned even though they pay the taxes on the property they occupy or use in business, industry and utility services. Homeowners, however, become concerned when a proposal is made to increase real estate taxes. Such an increase is often suggested first to secure their backing for new taxes or an increase of existing non-property taxes. Yet in spite of their direct interest, few take the trouble to visit the assessor's office to see how their taxes compare with others in the neighborhood or in other locations, or to press for more equitable assessment practices.

Since the benefits of state-wide spending for general purposes cause higher land values, the proper sharing would be on the basis of location value taxation rather than on the market value of improvements. The difference is especially important since, as all economists know, the collection of this location rent is a direct charge against those who hold the title and the benefits of increasing land value. The use of this source lowers rather than increases prices of land; such a tax is therefore not shifted in higher prices of goods or services to people as consumers. Taxes on improvements, and on machinery, trucks, inventories and the like, however, do affect production, making it scarcer, and therefore such taxes are shifted in higher prices to the consumer.

The various governments constantly search for more taxes, or what political minded people and many economists refer to as new sources of revenue. Actually there are five direct and understandable methods which could collect the same volume of revenue that is now gained by the costly method of levying a thousand different "kinds" of taxes. It is hard to justify so many taxes when revenue can be drawn basically from only two sources (land and labor).

These five levies would include, the existing ad valorem tax to collect rent-on-land (which is not a tax), personal incomes, inheritance, gasoline, and fees for direct services. All these could be apportioned between the local, state and federal governments according to functions assigned to them.

Notice that three of these five methods for raising revenue were proposed in the Communist Manifesto of 1847 as ways of destroying the capitalist system of production and the distribution of wealth and services. The income and inheritance taxes, as the communists would apply them, would most certainly destroy capitalism. However, the use of the ad valorem, or rent-of-land tax, as it should be employed, taking less rather than more of the available rent-of-land, would make capitalism blossom forth as never before, and possibly destroy communism by free market competition.