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Two Municipal Revenue Sources Contrasted:

*The Land Value Tax and the Property Tax**

By DALE BAILS

FEW WOULD DENY that the market has failed to renew our cities fast enough. For this the property tax must shoulder much of the blame. The existing evidence indicates that the property tax is a deterrent to the rebuilding needed in metropolitan areas (1). In every renewal decision the property tax always favors old over new. The land value tax is neutral in this decision because it is unchanged by renewal; it is the same on the old as on the new. The property tax is not neutral because it rockets upward when the new succeeds the old. It weakens the new *vis-a-vis* the old by the amount of the tax increase. Measured in years, the fiscal deterrent to urban renewal retards renewal of individual urban sites by decades (2).

I

FOR THE SLUM LANDLORD, the present property tax contributes to making slum housing the most profitable form of real estate investment (3). The deteriorated condition of the neighborhood means that the entire parcel is assessed at a very low value, even though it is near or in the center of town (4). The slumlord is best off leaving his slum as is. Even if he merely did decent maintenance, his property tax increases. Anyway, his real objective is to sell the underlying land someday at a big, low-taxed gain. Under the land value tax, the landlord would be forced to eliminate his holdings of slum property; first, because his tax bill will increase as economic rent increases, implying that he will not experience any gain in land values; and second, because the current income from the slum rentals will not be sufficient to pay his tax bill. If land were more heavily taxed and buildings more lightly taxed, the slumlord's situation would be reversed. He would no longer get a tax break from his ratty buildings; for all buildings would be tax cheap. He would no longer find it tax cheap to hold his high value land for future gains; he would have to improve or sell to someone who would put up good buildings. Thus, by taxing land it is possible to tax slums out of existence. For proof of this one only need look toward the Australian cities of Sydney, Brisbane, and Melbourne where there are very few deteriorated properties and no slums at all as compared to the slums to be found in every American city (5).

As has just been shown, the property tax, as presently structured, encourages the misuse or non-use of land. It always favors old over new;

gas stations over apartments; parking lots over parking structures; billboards over offices; unused or underused land over improved land. This is a result of taxing owners of underutilized or unused land so lightly that they pay only a trifling share of the truly enormous cost other taxpayers must absorb to pay for the public improvement (6). All this means is that the owners who are using their land have so much the heavier burden to bear.

The land value tax is neutral with regard to the intensity of use of particular sites. The most profitable possible use of the land before the tax is imposed or increased continues to be the most profitable use. Note, however, the taxing jurisdiction does not insist that the land be fully utilized; the land value tax is a self regulating device. It is simply presumed that when a person pays the full economic value of anything, he will want to get his money's worth. By imposing a penalty on the underuse of land, via the land value tax, the speculative value of land is destroyed (7).

A large portion of the current prices paid for land is a result of the speculative withholding of valuable land from its most efficient use (8). That land prices have continued to soar is shown by one of the findings of the Douglas Commission; from 1955 to 1965, land prices have increased six times as fast as the index of wholesale commodity prices (9). According to *House and Home*, since 1950 land prices in urban areas have soared anywhere from 100 per cent to 3,760 per cent (10).

These figures give the impression that land is no longer available for use in urban areas. On the contrary, there is plenty of vacant land and underused land left close to and inside the major metropolitan areas. Harland Bartholomew, in his book *Land Use in American Cities* in 1965, surveyed 53 central cities and found that the undeveloped portion was approximately 29 per cent. Victor Gruen, retained in 1966 to replan downtown Fort Worth, found that the underused or derelict reservoir of land was large enough to provide space for a belt highway, parking garages for 60,000 cars, greenbelts, a 300 per cent increase in office space, an 80 per cent increase in hotel space as well as a new civic and cultural center (11). In May 1968 there were 14 million vacant lots, or an increase in ten years of over a million (12).

As a result of a high tax on land values, the withholding of land from its best use would become extremely expensive to the owners. The change to best use would depend upon the prior amount of speculative underuse, consumer desires, the changes in tax rates, and other factors which will differ from one place to another. However, the adoption of a land

value tax would almost completely halt the trend toward urban sprawl that is now taking place in all major cities (13). Lest this result be thought unimportant, consider the costs of urban sprawl that are directly related to the financial plight of cities. To fully understand why, the results of urban sprawl need clarification.

Urban sprawl is a new name for an old phenomenon; the inefficient use of city and suburban land. The problem has become particularly acute in recent years with the expansion and urbanization of the population. Modern cities are spreading at their fringes and decaying at their centers. Some decentralization and outward movement of industry and of the urban population is inevitable. But the form that this decentralization takes is not preordained. With present tax policies this form has been urban sprawl with its many disadvantages. There is profligate consumption of land for low density uses. This pushes back the boundaries of rural areas and makes natural open space even more distant. Then a city could be better off to disgorge much of the undigested outlying land it has gulped, even if it had no alternative use. Another disadvantage of urban sprawl is the limitation on housing choice in such a pattern of development. Basically, only one type of housing is available: the single family detached house on a large lot, increasingly distant from the center of the metropolitan area. Also associated with sprawl is the blighting of mile after mile of fine farming land. Sprawl negates the very reason for the existence of cities, which is provision for close, easy interpersonal contact. One of the most valuable, and most misused, natural resources is the tiny fraction of land surface best fitted by location to bring men together for cooperation, exchange, and fraternization (14).

An efficient city is one that maximizes ease of contact among individuals, giving people, in their character of both consumer and producer, the widest choice among alternative contacts with the least difficulty. Efficiency entails sharing the cost of common facilities. The most important consequence of sprawl is the idea that sprawl multiplies the cost of almost every municipal service. It multiplies the cost for roads to reach the sprawl-scattered homes at the rate of \$500,000 per mile (15).

The reason for this increased cost is what is known as economies of density. That is, most municipal services are operations whose unit costs not only fall as the patronage rises but also fall as a result of close congregation of customers. Along this same line of thought, sprawl multiplies the waste of time, the most scarce resource of all, and the cost of getting to and from places to work and play. A University of Pennsylvania study found that more money is spent driving to and from work

than is spent by these same people on their homes. A Stanford study found that commuters spend a third as much time getting to and from work as they spend working (16). Finally, when cities are allowed, encouraged and subsidized to sprawl all over the surrounding countryside, much of the pressure is released that would maintain central land values, and greatly defer the time when it is economical for central land owners to clear and renew their lands (17).

II

IN CONTRAST TO UNDERUSE, a claimed disadvantage of the land value tax hinges on its tendency to foster more intensive development. It is often claimed that raising the holding costs of land in low return uses would tend to force premature development and make it difficult to preserve open space in and around the large urban concentrations. Conventional wisdom in the study of public finance dictates that if open space is desired, public acquisition of such property is a more direct, hence desirable, method. The shift to the land value tax would make good city planning at once much more necessary and much more effective. At the present time, city planning is a negative power. It can keep property owners from doing what they ought not to do, but in a free economy it cannot compel them to do what they ought to do. The effectiveness of present city planning is best summed up by the following statement by the Douglas Commission:

Regulations do not build cities. Nor do they effect significant upgrading of deteriorating areas. Finally, they seldom effectively encourage imaginative urban design and too many times effectively discourage it (18).

The land value tax would give planners a positive tool for influencing private land use. When they designate an area for development and provide the necessary services, up would go the taxes payable, cash-squeezing the land owner into early attention to his new opportunities. Further, since high use zoning is exploited quickly, there need be no great surplus of it scattered about, as today.

Some, no doubt, will regard the land value tax as a form of government intervention, but there are limits to the planners' power. The city does not direct a land owner to put his land to a specific use; nor is there usually just one highest and best use of a given site to which every landowner will be forced. Whatever is the highest use in a neighborhood is supplied in abundance until the need for another one is no greater than the need for some complement. Thus an equilibrium generally prevails at any time, which affords each land owner several options. The land value

tax also gives public investment great leverage over private investment. Today it is the reverse. The land value tax lets city planners take the initiative. The city could extend roads and services in compacted increments and then raise the tax with synchronization resulting. Finally, the land value tax would allow city planners to plan for open space. Under the present property tax much of the open space is a by-product of land speculation (19).

There is a *prima facie* case that the property tax at the margin may be a deterrent to investment in real property in the large central cities. Other things being equal, it clearly provides an incentive to locate commercial and industrial facilities in suburban areas. The property tax is largely a tax on investment in buildings and land values in urban areas. Only if the property tax were confined to land values would it be neutral in its impact on the spatial distribution of economic activity. Within regions which constitute meaningful economic entities, typically metropolitan areas, there are wide disparities in property tax rates. These differences are both a consequence of and contribute to the location pattern of economic activity in metropolitan areas (20).

With a shift from the property tax to the land value tax, those communities acting soonest to cut taxes on improvements would benefit from attracting more of the flow of the economy's new capital. For the removal of taxation from improvements means that the net percent income in the land value tax community compared with the net income yield in property tax communities will be, at least for a time, definitely higher. Then too, industrial concerns would prefer to build new plants in the land value tax communities; demand for land in the non-land value tax areas would be less; and landowners in the non-land value tax communities would be poorer than if the land value tax communities had not adopted the new system (21). If it is said that land value tax communities are infringing and are inconsistent with neutrality and equity considerations, it must also be said that it is wrong or unjust for the people of any community to seek in any way to make their community so productive and prosperous that it attracts residents from other communities and thus lowers the demand for and the value of land in those other communities.

III

HAVING MET THE REQUIREMENTS of neutrality and equity, the land value tax will be analyzed as to its administrative feasibility. The administration problem of the property tax has been a central one with general agreement that the tax is frequently, if not usually, very badly administered.

According to Dick Netzer, a leading authority on the property tax:

The tax is simply not administrable. Practically the general property tax as actually administered is beyond all doubt one of the worst taxes known in the civilized world. These administrative defects are inherent rather than correctible (22).

The discussion of the feasibility of the land value tax includes the application of the canons of taxation, assessing land values and the adequacy of the tax.

One of the many invalid criticisms leveled at land value taxation is the claim that there is no meaningful way in theory, as well as in practice, or separating the value of the land from the value of the improvements on land if the land is not vacant (23). However, land is appraisable and in fact appraised constantly, separate from buildings for the following purposes: buying real estate on the eve of demolition; right of way acquisition; and allocation of real estate value between depreciable and non depreciable components for income tax accounting and fire insurance (24). Any one of these appraisals of land is at least as accurate as are present appraisals under the property tax. For proof of separation of improvements, look at the Australian system where they have been doing it for over 80 years. Not only do they accomplish the separation but they do it with much less argument and litigation than results in the United States (25). Even assuming that it is not possible to make an absolutely accurate separation of land from improvement values, does it necessarily follow that, because of possible danger of accidentally and occasionally taxing improvement values, it is better to deliberately and purposely tax all improvements all the time than to make an honest attempt to exempt them?

It is fairly obvious that the success of any system of land value taxation depends in a large measure on the adoption of some uniform method of valuing and defining land for taxation purposes. As this is not an examination of the techniques of valuation, the details will not be fully elaborated. However, it can be said that land value taxation can be placed upon a completely systematic basis. W. W. Pollock and Karl Scholz in their book, *The Science and Practice of Urban Land Valuation*, set forth the Somers System of valuation which is used in Fairhope, Alabama and Denmark and to a limited degree in Australia and New Zealand (26). The Robert Schalkenbach Foundation spent three years developing a complete Users' Manual for a pre-tested and debugged computed study program, which statistically analyzed assessed land and improvement values by property classification—land use, for example (27).

A question that is sometimes asked is whether a land value rate would be sufficient to defray the expenses of metropolitan areas. A categorical affirmative can be given only when an efficient valuation of the land of each city has been made. Practical experience in every country and city where the land value tax prevails has shown that the land values are equal to or exceed building values, hence providing a sufficient source of financing. There is no reason to anticipate any other result in the American metropolitan areas (28).

IV

IN THE PREVIOUS SECTIONS it has been shown that the land value tax, in theory, offers many advantages over the property tax. The following examples will show how it works and that it does work in actual practice. Pennsylvania has the distinction of being the first state to make provision for the application of a concrete plan for cities to tax improvement values at a lower rate than land values. The two second class cities, Pittsburgh and Scranton, have operated under such a plan for 40 years. Pittsburgh provides the best example of modified land value taxation in action. In 1913, the state legislature passed the law enabling the second class cities gradually to increase the tax rate on land value and decrease it on improvements so that by 1925 tax rates on land values were exactly double the tax rate on improvements.

The principal effect of Pittsburgh's Graded Tax, for that is what the law came to be called, were felt primarily in the first few years as landowners sought to make adjustments to the new tax. In 1913 and 1914, while the country underwent a sharp recession which hit with extra impact on the heavy industry that dominated Pittsburgh's economy, the city's building industry flourished. Many vacant or underdeveloped plots in Pittsburgh which were owned by large absentee landowners were suddenly developed.

There is no loss of revenue to the city through the graded tax. It simply brings about a shift in burden from buildings to land. Its effect is upon the respective tax rates on land and buildings. For the year 1953 the city tax rates were \$32 per \$1,000 or thirty-two mills on land and \$16 per \$1,000 or sixteen mills on buildings. The total taxable real estate valuation was \$1,065,173,432 of which \$414,326,522 represented the value of land and \$650,846,910 on the value of buildings. The Pittsburgh tax plan, as it now stands, is a moderate tax reform. While it represents a distinct departure from the practice prevailing in other American cities, its effects have been limited by reason of the fact that the owners of improved and unimproved real estate in Pittsburgh are sub-

ject to very considerable tax levies for school and county purposes over which the city administration has no control or jurisdiction whatever.

The relatively high tax on land values has definitely checked land speculation by making it unprofitable to hold valuable land out of use. The apparent tendency is to stabilize the value of land at a time when building values have been soaring. While the selling value of land has fluctuated, the average market value of land in Pittsburgh today is but little higher than the average value prevailing before the graded tax was introduced over 55 years ago. Pittsburgh's long experience has proved the soundness of the method employed and has also shown how successful political action under a gradual approach can be achieved. If the results have been less than some expectations, it is due simply to the limited scope of present legislation and not to any inherent defect in the method of approach. Pittsburgh is now attracting greater attention and more national publicity than ever before as a progressive and prosperous city, and is becoming a cleaner and more attractive place in which to live and do business. Vast building and rebuilding operations are in progress which will transform a large section of the Golden Triangle. Over \$50,000,000 is being invested in the development of the new Gateway Center and other great new office buildings, manufacturing plants and apartments are in process of erection (29, 30).

The oldest still existing and most widely known settlement founded on the principle of land value taxation is Fairhope, Alabama. The community was founded in 1895 and is located on the eastern shore of Mobile Bay in Baldwin County. The founders, a group of men from Des Moines, Iowa, decided that the land would be kept in the possession of their corporation, the Fairhope Single Tax Corporation, rather than being owned by numerous private individuals and corporations. The colony's original purchase was of 135 acres, and additions have continued since. Eventually outsiders bought up adjacent land that the corporation had been unable to afford. Today about 80 per cent of the land in the city of Fairhope is held by private owners, but the other 20 per cent of the city's area, about four hundred acres, is still owned by the Fairhope Single Tax Corporation, and leased on a ninety-nine year basis. Through the year 1956, at least one half the improvements in the city were located on the one fifth of the land owned by the Fairhope Single Tax Corporation.

The economic rent collected from the land is put into a fund from which state, county, municipal, and school district property taxes, real and personal, are paid for all land held by the corporation. Tax bills to the residents are made out separately by the various jurisdictions, but are all

sent to the corporation. One condition under which property taxes would not be paid out of the corporation fund was established during the 1930s. At that time the regular property tax bills were sent to the individual residents who paid their own bills and then secured refunds from the corporation. Though property values and, eventually, assessments went up during the 1920s corporation rentals were not raised in proportion; and the amount of the fund's annual surplus declined. The depression of the 1930s brought a decrease in actual land values; but because of the inherent tendency of tax assessments to lag behind changes in market values, tax bills remained at generally the same levels and the annual surplus continued to decline. The people of Fairhope were able to ride out the depression without the usual evictions, defaulted mortgages, business failures and unemployment.

In 1933, taxes for which the corporation was liable reached a high of 96.04 per cent of economic rent collected. Because the corporation did not succeed in getting the residents to resist overassessment by the taxing authorities, a new rule was adopted whereby individual property tax bills were refunded only up to the amount of economic rent collected from the leaseholder involved. This rule is still in effect; but it continues only as a matter of policy, not necessity. Even in its worst year, 1933, the corporation fund received more economic rent from land values than the total property tax assessments of state, county, city and school district. The payment required of leaseholders to the corporation fund is determined by using the Somers system of land valuation. At present, the annual surplus is far above what is needed to pay in full the property tax bills of every leaseholder. The resident's agreement to continue this limitation is based on a desire to have as much of a surplus as possible as a fund for use in community improvement endeavors (31).

One of the most successful uses of the land value tax was in California, in connection with irrigation. In 1887 the California Legislature enacted the Wright Act, now known as the Irrigation District Act, allowing for the formation of special districts within the state for the provision and financing of irrigation. Revenue to support public works is secured through assessments upon the land values in that district. The original 1887 act called for assessing all real property. However, in 1909 an amendment provided for the exemption of improvements from taxation in all districts thereafter created. Existing districts were permitted to come under the provisions of the amendment if they voted to do so. Most of them did and at present all active irrigation districts assess only land. All the land within a district is subject to assessment, including town lots.

The Modesto Chamber of Commerce in the Modesto Irrigation District issued a statement concerning the effects of irrigation financed by assessments on land values only. Included in that statement was the following:

As a result of the change (to land value taxation) many of the large ranches have been cut up and sold in small tracts. The new owners are cultivating these farms intensively. The population of both country and city has greatly increased. The system of taxation has brought great prosperity to our district.

Land value taxation seems to have continued to encourage the intensive use of the land. The pressure to use the land or to sell to those who will derives from the simple fact that if you are in a California irrigation district your land will be assessed if you use it or not. If the land is used only minimally or lies barren for a speculative rise, the owner pays the same number of dollars as his neighbor who makes a heavy investment in improvements on land (32).

The most recent city to adopt the land value tax was Southfield, Michigan in 1961. When Mayor James Clarkson took office, he wrote to the assessor requesting him to study implementation of land value taxation by providing exemptions to improvements and annual reappraisals of land values. When the assessor refused to comply with the request the mayor asked for his resignation. The mayor then recommended the establishment of a Land Division under the Assessor's Office to reappraise all the land in the city of Southfield annually. To accomplish the first reappraisal, the J. M. Clemen Shaw Company of Cleveland, Ohio, was hired. They did a complete reappraisal of land values throughout the city which resulted in an increase in valuation of land parcels amounting to \$45 million. With the reassessment program completed controversy ensued, which concluded with the Council instructing the City's Board of Assessment Review to remove the Clemen Shaw Company land reassessment program. A taxpayers suit instituted by the Federation of Homeowners Associations, representing the majority of homeowners in Southfield sued the city to maintain the assessments, and they won.

All assessments are now made on a uniform basis. Land that rises most rapidly in value is given priority in the reappraisal process. Appraisal of properties is based upon sales information that has been confirmed and adjusted for special conditions. Southfield has a large number of land sales, hence their appraisal has good justification. One of their eleven appraisers works fulltime collecting commercial land sales and reappraising commercial land values. Residential land values are reviewed annually, subdivision by subdivision, by the residential staff.

In their annual reappraisal Southfield contracts with a professional company, Computer Control Corporation, which specializes in performing municipal computer services on a fee basis. They have designed a program which allows the city to do a mass city-wide reappraisal in a period of three hours once a year, at a cost of less than \$6,000. The computer, in addition to doing the paper work of the annual reappraisal computation, also prints the assessment roll, prints a letter informing each person in the city of his property's assessed valuation, land and building, and prints a sales study which indicated errors in assessments and establishes reappraisal priority. During the first year, the city spent only 20 cents per property for preparing all the programs. The annual reassessment costs only about 6 cents per parcel.

As a result of adopting the land value tax, Southfield has become one of the fastest growing cities in America. It has doubled in assessed value over the last five years and tripled over the last ten years. In 1967 alone, 21 per cent growth was added to the assessment rolls. There are thirty-five high rise office and apartment buildings recently completed or under construction. Since 1960 over 3 million square feet of office space have been built in Southfield. This was 10 per cent greater than the amount of office space built in Detroit, the fifth largest city in the nation. Over one thousand new homes were built in Southfield last year, and the average house sells for around \$27,000. There was over \$75 million in new building construction in 1966. The beneficial aspects of Southfield's tax policy are best summed up by the following statement made in 1968 by the Southfield assessor.

Southfield's policy of assessing has differed from most other cities for six years now. There is an annual reappraisal of land values. Land is assessed on a basis of its full market value, whether it is being used, used poorly, or not used at all, zoned or not zoned property. Southfield has one of the most active commercial real estate markets in the nation. Real estate developers have been drawn to this city by the stability that land value taxation has created in the land market. A buyer of an unimproved site fully realizes that he will pay taxes based upon the market value of the site whether he builds or not (33).

A word of caution is necessary. To sell a program in which one believes, enthusiasm leads to exaggeration unless caution asserts itself. The change proposed would not pour huge sums into city treasuries. Nor will the land value tax build new structures, put all land to its best use, eliminate sprawl or renew our cities immediately. Nevertheless, the tax is economically sound and practically feasible and should be considered as an alternative to the property tax. It must also be pointed out that for

a problem so vast and complex as the urban crisis, there can be no one, no simple, no easy solution, and policy makers need all the tools economic theory can provide.

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* For the basic analysis underlying this paper, which I have tried to avoid repeating, see my paper "An Alternative: The Land Value Tax: The Argument for Continued Use of Part of the General Property Tax," *American Journal of Economics and Sociology*, 32 (July, 1973), pp. 283-94.

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Law and the Humanities and Human Interdependence

THE INTERRELATIONSHIP and interdependence of man with man and with nature is today no longer debatable. Even the new discipline, termed "the sociology of science," has as its core concept the interaction of researchers within a social framework.

The humanities have long known this, *i.e.*, that they cannot engage in tunnel vision and stand aloof from each other, that any such isolation is "unnatural," and that each discipline increasingly affects the other(s) and, in turn, is so affected.

The 18th century effort to compartmentalize the arts foundered because art and reality could not thus be stilted and stultified; so with the humanities—there is an enveloping wholeness which transcends any separatedness or total independence.

This rapport, even communality, creates ties, institutions and legal relationships or influences upon the law. These latter have, in past centuries and decades, been displayed in written documents, legislation, decisions, and administrative determinations.

For example, the break-up of feudal institutions and mores affected law, most notably as Austin showed, in the change from status to contract. So, too, the Industrial Revolution changed not only the social and economic face of western civilization but also its legal one, *e.g.*, the institutional relations involving property, power, and politics.

To illustrate "the seamless web" of history we need but seek understanding of today's employee-employer-union relationships in (at least) the social, political, and economic relationships of both England and America. And, especially insofar as law and legislation entered both as effect and cause, the necessary and intertwining relationships in this area were and are absent nationally, and now internationally.