

POVERTY, POLITICS AND PROFIT

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As sad as this state of affairs is for so many people in the United States, the absence of decent, affordable housing (as well as the corruption and fraud involved in the development of such housing units) is a symptom of a much deeper systemic problem caused by our tax system. For twenty years, from 1985 to 2005, I worked as a manager and market analyst at Fannie Mae. What became clear to me was the power of the property tax -- as structured -- to destroy communities. The mainstream property tax is a disincentive to the production of new housing or renovation of existing, older housing. The band-aid solution utilized by too many communities is to offer tax abatements on new construction. What this essentially does is raise the price owners of land can charge to developers, who can pass on the added cost to purchasers because the monthly escrow for property taxes during the abatement period is a small percentage of what the actual tax obligation will be when the abatement expires. Thus, the buyer/ mortgagor is able to qualify for a much larger loan than would be the case if the full property taxes were imposed.

Owners of land (and land speculators) benefit as well by the almost universally-low effective rates of taxation on vacant and underdeveloped land. The assessment of land, whether vacant or highly developed, is rarely kept current with rising - or falling - market values. The result is that land values in high priced markets are almost universally under-assessed, while in neighborhoods experiencing declining values the assessed value becomes a higher percentage of market value. One remarkable exception existed in the town of Greenwich, Connecticut, during the years when the city assessor kept land assessments current based on market data. The assessor, Ted Gwartney, reported several years ago that the assessed value of land in the city represented 70 percent of the total property values.

The economics are well-understood by analysts of land markets. Every parcel or tract of land has some potential annual rental value. This rental value is determined by many factors, but locational advantages are the primary determinants. A location may be highly desira-

ble because of nearness to natural assets, such as the ocean, a lake or river, a mountain recreation area, or other attractive characteristics. Locations in our towns and cities are highly desirable because of the public goods and services provided and paid for by broad-based taxation. Thus, land rental values have been viewed by economists as diverse as Milton Friedman, Mason Gaffney and Joseph Stiglitz as the legitimate source of public revenue. Taxing actual housing units, on the other hand, is counterproductive; and, one can argue, results in the confiscation of value produced by individuals. Mason Gaffney (now emeritus professor of economics, University of California) argued years ago, the property tax on property improvements is equivalent to an annual sales tax imposed on an asset once purchased. The optimum rate of taxation of housing units (and all other buildings, in fact) is zero.

Residents of higher-income, growing communities reasonably fear the introduction of high-density, publicly-subsidized housing. Although this appears on the surface to be a race-based problem, it is clearly caused by economic and class consciousness. Remarkably, in many suburban communities the result of opposition to affordable housing initiatives is that the adult children of residents are forced to move to ever more distant subdivisions and towns to find affordable housing. Because of higher and higher land costs, even individuals with well-paying jobs are required to commute longer and longer distances from home to work. In addition to contributing to the destruction of urban neighborhoods, the conventional property tax is a main cause of sprawling development. <<