PROPERTY TAXATION

Statement to the Ways and Means Committee, Hew Hampshire State Legislature by C. Lowell Harriss, Professor Emeritus of Economics, Columbia University; President of the Robert Schalkenbach Foundation, Inc.; March 2, 1994
Views expressed are the speaker's and not necessarily those of any organization with which he is associated.

"How," I have been asking myself, "might I be helpful?" Not, certainly, by presuming to comment upon issues quite specific to New Hampshire! But thoughts about the economics of property taxation can perhaps be useful.

Although the property tax is familiar, the economic realities it embodies are not all recognized as fully as possible. With better understanding, Americans can, I am convinced, make fundamental improvements. That is, looking beyond revenue, we can get better non-revenue effects.

Any tax does more than yield revenue. It also affects the ways in which people invest, produce, consume, support philanthropy and the arts, and so on. Per dollar of yield to the treasury, different taxes and tax structures can have a variety of results. Some will be more desirable -- or less unwelcome -- than others. Property taxation offers unique possibilities.

In an economic sense "the" property tax is not one but two taxes. They differ fundamentally. One is the portion that falls upon man-made capital. The other is the tax upon land.

To a business or an individual an investment in land may seem much the same as one in buildings or machinery. But for those concerned about the economy of a community or a state the difference is profound. The quantity of land has been fixed by nature (with minor exceptions). In contrast, the quantity of man-made capital depends upon human actions. The amount of housing, equipment, and so on that will become available in an area as time passes can vary greatly. New funds for such capital will go where prospects seem best. The higher the prospective property tax, the less.the attraction for new capital.

The amount of housing and other man-made capital in a community in the near future will not be materially depleted if the tax rate rises next year. But over time the capital that means so much in life must be adversely affected by heavier as against less burdensome property taxation.

Not so, land. The quantity of land will not be reduced by an increase in tax. Land will not move. The quantity of land actually made available for (most) productive use may be enlarged by tax pressure on owners to pay tax in cash.

If time permits and if you wish, we can discuss the isssues more fully because there is more to say. In their policy decisions, lawmakers can make constructive use of the fact that "the" property tax is not a homogeneous entity. It falls on two distinctly different kinds of property. The higher the tax rate on housing and other man-made capital, the smaller the net (after-tax) benefits. Human well-being will suffer. In contrast, the larger the supply of man-made capital and the better its quality, the better we, our children, and theirs can live. But the tax on land will not reduce the supply.

The potentials for human betterment seem to me great enough to warrant determined efforts to restructure property taxation. The logic seems clear. Governments can change the balance of incentives to favor construction and to induce better use of land. States and communities (if given authority) can begin with rate differentiation.

Present taxes on man-made capital are more burdensome than may seem. Rates of 2 percent, more or less, seem low when compared with income, payroll, and even sales tax rates. But property taxes fall, not on income but on capital that produces income (including housing). And one to two percent on capital value will usually be quite a large portion of the fruits of capital, the benefits produced.

One can think of constructing a new building and the property tax that will be due on it year after year. Then one can estimate the present value of that stream of taxes. That amount will probably be several times the sales tax on normal purchases. Incentives to build must suffer. But the land is already in existence.

If more revenue is needed in New Hampshire, one may hesitate to increase burdens on man-made capital. But is that the only choice? Is there not another? Cannot most or all of the added revenue be obtained from land values without more depressive effects on man-made capital?

The distinction I am emphasizing is not some recent intellectual discovery. But it is one sadly neglected in American taxation (except for some communities in Pennsylvania). I have brought along some copies of an address which goes into the subject a bit more fully.