

A conversation with Richard England on March 27, 2014

Participants

- Richard England – Visiting Fellow, Lincoln Institute of Land Policy; Professor of Economics and Natural Resources, University of New Hampshire
- Alexander Berger – Senior Research Analyst, GiveWell

Note: This set of notes was compiled by GiveWell and gives an overview of the major points made by Richard England.

Summary

GiveWell spoke with Richard England as part of its investigation of US tax reform. Conversation topics included: trends in US municipal tax codes, property tax policy, and the political landscape around tax reform.

Pressure for tax reform

The modern US tax code at all levels of government is badly in need of reform. The code is now very complex, producing high compliance costs. Economists have produced a lot of research showing that current tax policies produce some negative incentives. For example, tax policies can inadvertently discourage investment.

While there are strong economic and political incentives for reform, the political environment makes fundamental tax reform hard to achieve. The last sizable tax reform was in the 1980s and was limited to the federal level.

Many municipalities depend on property taxes for revenue. However, in some major US cities, property tax rates are so high that they are causing major efficiency losses. For example, some studies suggest that in some instances tax rates are high enough to cause measureable increases in unemployment and one recent study indicates the rates in a few cities are so high that they are already reducing the cities' tax revenue (i.e. they are over the maximal revenue collection point on the Laffer curve).

For example, Philadelphia has struggled in recent decades to cope with its very poor municipal tax policy. In addition to substantial property taxes, Philadelphia also taxes payrolls and gross receipts (rather than profits). This combination has led many employers to move beyond Philadelphia's borders into surrounding areas.

Detroit faces similar problems with its tax code. On top of its other fiscal difficulties, its property tax system has contributed to the spiraling drop in property investment. Though many properties are delinquent, the city often does not bother foreclosing because market demand is so low that

foreclosure would not produce much revenue. Professor Mark Skidmore, a visiting fellow at the Lincoln Institute from Michigan State University, is currently studying Detroit's economy and tax policies, exploring where the largest problems lie and what solutions might be possible.

Land value taxes as an alternative

On the local level, land value taxes are one of the better options for raising revenue. Where many other forms of taxation are philosophically controversial or produce recognizable drawbacks, there is a consensus amongst tax economists that land value taxes create negligible efficiency loss. Taxes on various forms of commerce can discourage those forms of commerce, but land is a constant; taxing it does not reduce the supply of it in the economy, it only influences how it is used. There is also the older argument that much of the value of a given parcel of land is a result of social construction. Land next to civic improvements or other beneficial developments is worth more, so the public is somewhat justified in recouping some of that value from the landowner.

Pennsylvania is one of the few parts of the US to experiment with a land value tax. Pittsburgh and a number of other small cities have made use of it for decades. Most other states have avoided it due to the technical challenge of accurately assessing the land value for each individual site. Some Pennsylvania cities currently use a two-rate property tax system; a higher tax rate is levied on the land value with a lower property tax rate on the value of buildings and improvements. While eliminating property taxes entirely with land value taxes would likely be impractical in major urban centers, a two-rate tax system may be easier to implement.

Effects of land value taxes

Shifting taxes from a property value basis to a land value basis creates more of an incentive to spend on maintenance and property improvements. Though not enough on its own to transform city centers with serious urban decay, some see this as a potential tool for urban renewal. In cities with a high proportion of neglected rental properties, moving to land value taxation can incentivize property improvements and new construction.

Though there is no clear consensus on the effect that a land value tax would have on trends in population density, there is some indication that it creates enough incentive for urban construction to keep economic activity anchored in cities. Some serious research on this subject has been done but not enough to completely settle the question. While it cannot negate urban sprawl entirely, there is some reason to believe that the combination of both lowering taxes on urban building values and lowering taxes on rural-use land (forestland and farms) outside metropolitan areas would increase density.

The tradeoff is that properties that have a high ratio of land value to building value would see a big increase in tax liability. This, in turn, would reduce the market value of the property as a whole since

new buyers would face higher taxes going forward. Land itself would trade for lower prices, as would developed properties in locations with very high value. Tax reform based on land value would likely be opposed by people with high investment in this kind of real estate.

Historical issues

Property value and land value taxes have historically been implemented entirely at the state or local levels rather than at the federal level. In previous eras, federal presence in most jurisdictions was very small compared to today, and assessors would have required understanding of local market pressures in each and every jurisdiction being taxed. Centralizing the assessment process would have been impractical. Even at the local level, the official assessment process has a long history of corruption and abuse.

Federal limits

It is unclear whether a federal land value tax would be constitutional; property tax laws are usually governed by applicable clauses in state constitutions, often calling for uniform taxation of land or property. Some states also have amendments that allow for different “classifications.” For example, almost all states have adopted a policy of use value assessment, in which rural land is taxed very lightly. Most states are committed to taxing farm and forest land proportionally less than other forms of land.

Defining "land" to include mineral resources

Professor Mason Gaffney, an economist at UC Riverside, publishes periodically on how natural resources like oil and gas ought to be brought into the land value rubric.

Exploring Pigovian taxation of can yield similar tax incentives. Professor England published a piece a few years ago endorsing state gas taxes in the New England region as a way to encourage energy conservation. Since the region has no local petroleum sources or refineries, everything is imported. He proposed rebating most of the resulting revenues to motor vehicle owners, limiting the overall increase in expenses at the pump, while creating an incentive to conserve.

Georgism

In the 1870s, politician and economist Henry George made a case for land value taxation:

- He claimed a portion of society was growing disproportionately rich through real estate ownership. Modern advocates usually adapt this claim to the more general one that wealth now accumulates through ownership rather than contribution.
- He made a populist argument that land value taxation would be fairer and promote a more egalitarian society than other kinds of taxes.

Though a number of small groups exist that advocate Georgist policies, most are highly ideological and attribute immense benefits to a land value based tax system, beyond what many economists would consider demonstrable at this time.

Challenges in advocating land value tax reform

A major challenge in mobilizing support for a land value tax is making the argument for the tax clear and persuasive to the public. The underlying rationale is that current municipal tax systems discourage construction and maintenance by taxing improved property more highly, discourage employment and small businesses by taxing wages and receipts, and drive higher-income residents out of cities by taxing personal income. Land value taxes offer tax revenue without these harmful disincentives. While this is a reasonable argument, it focuses on areas of policy that do not usually receive large amounts of public attention, and which most of the public does not understand well. The benefit of restraining urban sprawl may appeal to environmentalist voters, but there are usually relatively few such people in urban centers, where this kind of tax reform is most needed.

While the benefits of tax reform are diffuse, persons whose tax liability is most likely to be increased (or, relatedly, asset values harmed) by this kind of reform will be quick to realize it and will be strongly opposed to reform.

Technical problems with how land value can be properly assessed are also an issue, but one which can be overcome. Well-trained assessors are needed, requiring stricter guidelines and uniformity in training, but advanced methods for proper assessment already exist.

And, of course, local conditions might make land value taxation an ineffective approach in some cases.

Potential funding opportunities

Research

- A better understanding of the political economy issues surrounding tax reform is important; research is still needed to form a clear understanding of why the US has not seen wider adoption of land value taxes. A chapter in the Lincoln Institute's recent anthology on land value taxation examines the international experience with land value taxation, especially in British commonwealth countries where land value taxation has been much more widely used, but there is still a need for better understanding of the underlying political obstacles.
- Further research demonstrating the ways in which existing municipal tax codes harm the local quality of life can help make the case for comprehensive tax reform. This includes exploring

negative impacts on small businesses, larger employers, and disincentives for landlords to maintain and improve rental properties.

Political Education

- Raising awareness about the difficulties faced by municipalities seeking to improve their tax code can make reform easier to achieve. A series of case studies on individual cities could be part of the political education. The Lincoln Institute has a series of DVDs exploring the political economy of Portland, Cleveland and Phoenix, examining struggles to construct better tax systems.
- The Concord Coalition is a nonpartisan group working to raise awareness of the national debt and the value of tax reform in addressing it.

Ultimately, any action on this kind of tax reform will need support in state capitals rather than a federal initiative.

Others to talk to about these issues

- Robert Schalkenbach Foundation
- Concord Coalition

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