

THE VALUATION OF REAL ESTATE

IN MOST systems of taxation a considerable proportion of the revenue is derived from taxes levied upon real property (land and improvements taken together). In some cases the further step is taken of distinguishing between the value of the land and the value of the improvements. It is only in very recent times, however, that any serious attempt has been made to put the valuation of such property upon a scientific basis.

Students of this problem will welcome a comprehensive survey of methods of assessment in the United States recently made by Mr Joseph D. Silverherz for the New York State Tax Commission.* In this he reviews the methods adopted in every one of the United States, the results obtained are submitted to objective tests of accuracy, and general conclusions are drawn as to the best means to be adopted to secure equitable assessment.

The fundamental test of good assessment is the relationship of the assessed value to the market value as disclosed by actual transactions. The percentage of the assessed value to the market value is designated the "assessment ratio" of any particular property. By adding together the assessment ratios for a number of properties and dividing by that number we obtain the "average assessment ratio."

NECESSARY UNIFORMITY

It will readily be seen that if the assessment ratios for individual properties are close to the average assessment ratio, in other words if there is uniform under-assessment, the relative position of the taxpayers is the same as if all properties were assessed at full value. If, however, some properties are assessed at 50 per cent, others at 60, 70, and 80 per cent, gross inequalities occur. A convenient method of measuring the degree of inequality is provided as follows: the difference between the assessment ratio of any property and the average assessment ratio is termed the "deviation." By adding together the deviations of each property and dividing by the number of properties concerned we get the "average deviation." Finally by dividing the average deviation by the average assessment ratio we get the "co-efficient of dispersion" which gives a measure by which the goodness of the assessment can be tested.

Space will not permit us to review the results of the investigation in the various states. By way of illustration it may be mentioned that examination of 422 farm assessments in the state of Maine showed that the average assessment ratio was 30.29 per cent. The average deviation was 10.30. Hence the co-efficient of dispersion was 34.13 per cent. Individual cases, of course, showed much greater divergences. A few properties were assessed at 100 per cent of full value. Some at less than 20 per cent. To quote Mr Silverherz: "Instead of assessments being made uniformly, and everyone taxed equally according to the value of their property, as is the intent of the law, some assessments were found to be made at 20 per cent and others at over 100 per cent; and some tax payers were found to be paying two, three, four, and even five times as much as others." Another point that arises from the investigation is that on the whole the more valuable the property, the lower was the assessment ratio. "Properties worth less than \$5,000 were proportionally assessed on the average at approximately twice as much as those worth over \$45,000." Because of this "regressivity" the majority of the

taxpayers are being overtaxed to the relief of a minority of wealthy taxpayers.

EXISTING DEFECTS

The general conclusion is that the defects in present methods of assessment may be classified under five headings: (1) Complete escape of property from the tax rolls. (2) Rigidity, *i.e.*, failure to adjust the assessments to correspond with changes in actual values. (3) Inequality in the assessment ratios of different classes of land, *e.g.*, rural and urban. (4) Regressivity, *i.e.*, higher assessment of the smaller valued properties. (5) Inequality as amongst individual properties.

These faults are found to be wide-spread. The question then arises: how are they to be remedied. One method which has been generally advocated is state equalization, under which a state department is entrusted with the function of correcting the assessments. Experience has shown that this produced little result. Professor Carl C. Plehn is quoted as saying: "As everyone knows 'equalization' after the assessment has been made fails. It is predestined to fail. An audit after the cashier has run away with the funds is of interest for historical purposes only. It is a pre-audit that protects. It is equalization before, not after, assessment that is effective." Mr Silverherz himself says: "The whole system of equalization is a plant not worth cultivating, for it bears few flowers and attracts many weeds. It diverts attention away from thorough-going improvements, and offers little in return."

CORRECT PROCEDURE

The pathway of reform then is to devise means for ensuring that at the beginning all property is valued as nearly as possible 100 per cent of its full value. This necessitates the employment of fully trained and skilled assessors, employing modern technique in valuation. "Modern systems of assessment include four basic components: (1) tax maps; (2) a system of unit valuation for land; (3) a system of unit valuation for buildings, and (4) a system of compiling and analyzing indices of value."

For the purposes of land value assessment and taxation the third component is unnecessary, but it is interesting to observe that under a tax system, as in the United States, where land and buildings are equally subject to taxation, it is considered necessary to value land separately from improvements.

The following passages may be quoted relating to the other three components:—

"TAX MAPS.—Accurate and detailed tax maps constitute the basic prerequisite to any attempt at systematic assessing. For without a definite and accurate knowledge of physical dimensions, unit valuation is entirely out of the question. These maps usually contain the following detail: An outline of the blocks and lots within each block, drawn to scale; figures indicating length in feet and fractions of feet of each line bounding any lot; an identifying number for each block and an additional identifying number for each lot, and the names of the streets bounding the block." (This relates to urban land. For rural land other information is required.)

"UNIT VALUATION: LAND.—The basic method of modern assessment is to break down the value of properties into small comparable value units. For

* THE ASSESSMENT OF REAL PROPERTY IN THE UNITED STATES. By Joseph D. Silverherz. Special Report No. 10, State Tax Commission. Albany, New York, 1936.

standard 'average' parcels, the application is quite simple. With respect to land valuation, the usual practice is to consider a strip of land, located at or near the middle of a block, with a frontage of one foot and a depth of 100, 120, 125, 140 or 150 feet (depending upon the normal lot depth of the area) as the standard physical unit. The various blocks of a city are assigned front foot values, derived from analysis of sales and other value data." The assessor applies the unit values to calculate the value of each lot making due allowance for special factors such as abnormal depth, irregularity of shape, corner situation, alley influence, double frontage, etc.

"VALUE DATA.—It is possible for a city to adopt many of the components of unit valuation (*e.g.*, standard depth tables, corner formulae, and factors of value for building valuation), and then allow the system to stagnate by failing to keep the unit values up-to-date. This can be avoided by the continued collection, compilation and analysis of indices of value, such as sales, mortgages, appraisals of estates, etc. The method of the unit value system is a combination of analysis and synthesis. Available indices of value serve as representative samples to be broken down into value units applicable to all of the properties of a city. The larger and more representative the sample, the more easy is the task of establishing currently valid units, and the more justifiable will the assessments calculated thereupon be."

TRAINED ASSESSORS

In order that the best methods should be applied and should be well applied it is essential that assessors should have the requisite technical knowledge and equipment. "Only long-term appointive, well-compensated men can handle the job of assessing well." This involves that the assessment area should be large enough to afford to pay for competent service and provide the equipment required.

The view that assessors should be local residents and should be popularly elected is rejected. The assessor should be disinterested and should hold his post under civil service conditions. He should have variety of experience. The author recommends, and he quotes a large volume of argument in his favour, that the state should be the unit of assessment administration. (What the unit should be in this country is a matter which deserves careful consideration. Perhaps the county and the county borough.)

"LANDOWNERS' VALUATIONS"

It may be observed that there is no suggestion in this examination that the problem can be solved by the method of self-assessment, under which the property owner is made responsible for valuing his own property subject to some review by the assessment authority. The popular argument is that no one knows the value of his own property so well as the owner. There is no foundation for this belief. On the contrary, if he wishes to dispose of it he seeks expert advice, advertises it for sale, and then waits until he gets what he thinks is the highest offer likely to come. Moreover, if the owner does know, there is no reason to believe that he will communicate his knowledge to the taxing authority. On the contrary, his natural impulse is to put the value for purposes of assessment at the lowest amount which he thinks likely to be accepted. A further and still more fatal objection to self-assessment is that it means in practice that the small property is likely to be assessed at a larger fraction of its value than the larger one. The

value of the small house in the suburbs, for instance, is much more a matter of common knowledge than that of the valuable central office building or factory. Thus the result of self-assessment is to introduce regressivity into the assessment and to impose an undue share of the tax burden on the small man. When it comes to separate assessment of land apart from improvements the objections to self-assessment are still greater.

In concluding this review it will be of interest to note that among those to whom the author acknowledges his indebtedness for "much mature, practical advice" are Mr Lawson Purdy, formerly President of the Department of Taxes and Assessments of New York City, and Mr Philip H. Cornick of the Institute of Public Administration.

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