

What is Site-value Taxation? (Part II)

MASON GAFFNEY

Concluding this review of various aspects of site-value taxation, which commenced in our last issue.

ELEMENT No. 4: Site-value taxation implies the inclusion of a "succession premium" (development value) in the tax base. The succession premium differs from capacity to serve in that the former is unripe while the latter is ready to go. I will refer to the capacity-to-serve premium as the "red premium" and the succession premium as the "green premium" to underscore this distinction. The succession of land from a lower to a higher use could and should take place in an orderly, peaceful fashion but rarely does. Zones of transition become "combat zones". Land value in these zones develops a green premium in anticipation of conversion. It is sometimes referred to as "speculative", but that is misleading, for "speculative" suggests that conversion to higher use is uncertain when in fact it may be more certain than a repeat of the present use. It is rather, simply, a green premium because the time is not yet ripe to change the use.

Including the succession premium in the tax base is often criticized on the grounds that it is inequitable, inconvenient and finally inefficient because it forces premature conversion to the higher succeeding use. Let us consider these points in order.

The equitable argument for including succession premia runs as follows. The premium is the discounted present value of future income and as such tends to increase yearly along a compound interest curve, growing like money in the bank. This annual increment in value is income. According to the Carter Commission, which was in the tradition of Professors Haig and Simons, unrealized accruals of value are and should be treated as current income. The annual accrual of value tends to be proportional to the value. So is the property tax. Therefore the property tax is pro-

portional to the income. Thus it is a way, probably the only practical way, of taxing that income at the appropriate time, which is when it accrues.

It is indeed the only sure way of taxing it at all. If we look at an alternative, like the Ontario speculation tax, it is levied only at the time of sale. That means that a person wanting land in the future could buy it today, hang on for thirty years, and finally realize its unearned increment by use, never becoming liable for the tax.

The anticipation of future taxes during the ripening period and thereafter will be capitalized into lower present values. This capitalization effect takes away a substantial part of the premium which is the tax base. In addition to being the tax base this premium is the market value on which interest is computed (either cash or imputed interest). Reducing this premium value therefore reduces the temptation of individuals to sell prematurely to developers, and the part of carrying cost which is interest.

Note, too, that if land is prematurely converted to a higher use, one of two things will happen, both bad. One, it may lose money for the first several years since the market is not yet there for the premature improvement, or two, it may be inadequately developed to meet the future demand in order to avoid problem no. 1, in which case it will soon move into a future where land taxes are based on a higher use than it is improved to meet. This is assuming that the assessor continues to increase the assessed value as the capability of the land increases with time. The only circumstance I can imagine in which assessment and taxation of a succession premium would cause premature conversion would be if the taxpayer anticipated, correctly or not, that the assessor was going to

freeze the land assessment at the low level corresponding to the premature underimprovement.

As to efficiency, we have discussed this in part in connection with inconvenience, but there is more to it. Site-value taxation, we have seen, has a developmental tendency. It strengthens the higher use *vis á vis* the lower use at every margin of decision, be it the extensive or the intensive margin; be it at the fringe of cities or on underdeveloped land that permeates the cores of every city. Thus it is conceivable that site-value taxation could encourage infilling as many of its proponents believe; or that it could cause additional sprawl as some others believe, including some of its earlier advocates. Harry Gunnison Brown, for one, has stated that cities may be surrounded by a belt of monopoly speculative landholdings which need to be broken through by taxation.

Some people believe that infilling is undesirable anyway while others see it as the only cure for urban sprawl which they regard as undesirable. From my observation, however, it is my judgement that under present circumstances the major effect of site-value taxation would be to encourage infilling and redevelopment of our older central cities. There is so much land there on the verge of renewal which would be pushed over the margin by the exemption of new buildings from the property tax and the application of fiscal inconvenience to landowners. In addition there would be an enormous synergistic effect from the replacement of older buildings by new.

Element No. 5: Universality and uniformity. The more comprehensive the tax base, both as to extent of jurisdiction and inclusion of different industries and land uses, the more it has the quality of site-value taxation. This



is a point of considerable uncertainty and evolution of position among advocates. To understand

why, let's go back to 1879. Henry George, writing in that year, did more than anyone before or since to advance the proposal, which is often identified by his name. He was not afraid to say, "Let us make land common property." And he clearly had in mind "making common" at the national level.

The proposal was much less radical and shocking in the context of his time and place than it might seem today because most of the land in the western United States was public domain or had only recently been so. Private land, as it existed then, had been alienated under conditions of considerable fraud so that its owners were in a weak moral position, and those were moralistic times. Some time later Henry George ended his career running for Mayor of New York, it is true, but then as Thoreau remarked, "The young man prepares to build a stairway to the moon but may end up merely repairing the woodshed." The woodsheds contemplated by George's successors grew ever smaller until the proposal became a limited gadget to improve the efficiency of municipal finance.

There was widespread application of George's ideas at the municipal level around the turn of the century, but universal ideals are not applied at the local level without considerable modification. City fathers have never regarded heavy property taxes, either on land or buildings, as a means of sharing property among the people of the nation or the world. Only growth oriented municipalities have found site-value taxation very attractive and nowadays growth has become a dirty word. In a less mobile society there was room for some redistribution of wealth at the local level but in today's circumstances that is increasingly without support. Site-value taxation of the degree contemplated by George and his early followers could only occur at the national level where it would have to be recognized as a redistributive measure, tending (as all taxes do) to make the taxable object common property.

One of the strongest arguments in favour of site-value taxation as opposed to general property taxation is that the latter cannot ever be uniform because some forms of

capital are much easier to conceal than others.

It is, on the other hand, relatively simple to draw a map or cadaster comprehensively including every square foot of land in the jurisdiction. If one accepts the principle of exempting capital from the property tax, uniform treatment of all land becomes an attainable objective.

Element No. 6: Frequent reassessment of property. In the normal course of events buildings and other capital depreciate with time in contrast with land which often appreciates. Any movement in the direction of more frequent reassessment, therefore, is a move towards site-value taxation and vice versa.

There is a tendency in many jurisdictions for the issuance of a building permit to be if not a taxable event an assessable event. New buildings, in any inflationary period, thus come on the rolls at inflationary price levels. If land is not reassessed annually it becomes seriously underassessed relative to new buildings. As to old buildings, practice varies. In some jurisdictions they are "factored" upwards from time to time to keep pace with inflation of replacement cost. Since land has no replacement cost this kind of factoring may omit land.

If land is not reassessed frequently then the assessable event in the life of land is likely to be subdivision or other improvement and what is called a land tax becomes a sort of increment to the tax on new buildings. Under site-value taxation the assessed value of raw land would increase annually with its market value so that actual subdivision would occasion no great jump, if any, in assessed values.

Site-value taxation has many faces. Few will like or dislike them all. It has its partisans on the extreme right, on the extreme left and in the extreme centre. It is a policy like many others that may be embraced or repulsed by degrees and in parts. We have never been without some elements of site-value taxation, since at least 1066 when William the Conqueror adopted it and set up in his Domesday Books an assessment roll and land registry. We have never gone as far towards

it as its partisans would like. But one way or another, we are all as citizens and/or as public servants going to have to think and make decisions about most of the elements in the site-value tax package over the near future and probably for the rest of our lives. It is a big elephant with many parts, and we will certainly handle it much better when we stand back and look at all its subsystems together rather than tickling the ear or twisting the tail.

* * *

Who's Stealing from Whom ?

DURING September seven towns received surprise visits from teams of wages inspectors to ensure that employees in low paid jobs were not being paid less than the statutory minimum rate for their jobs. This is the start of a "blitz" on low pay industries, reports *Employment News*, the Department of Employment newspaper.

Announcing the campaign, Mr. John Grant, Parliamentary Under Secretary of State for Employment, said: "... in many cases infringements may be due to misunderstandings. In those cases the wages inspectors are there to help put it right. But where deliberate underpayments are discovered, that is tantamount to stealing from the workers." It is difficult to see how the term "stealing" can validly be applied to an arrangement presumably voluntarily agreed between employee and employer. And if the enforcement of the statutory wage should make it uneconomical to employ some of the workers concerned, should they feel grateful to the Department for putting an end to the "robbery" albeit at the expense of their jobs?

This is not to approve of low wages but to condemn superficial and artificial methods of trying to raise them.

"Other towns may be subject to these blitzes at later dates," warns *Employment News*, so perhaps any workers who lose their existing employment as a result, could get jobs in the expanding Wages Inspection Industry.