

ON JUNE 7 the voters of California gave their approval to the thirteenth of a list of referendum topics on their dual-purpose ballot papers. Proposition 13 thus passed quickly into law: the state government's main source of revenue, property taxes (roughly equivalent to British rates), was cut from \$12,000m to \$5,000m a year.

Proposition 13 was a popular issue. The campaigns for and against made it the biggest issue since Vietnam. The economic and theoretical arguments were lost in a groundswell of populist reaction by "Middle America" against government expenditure. Two camps were discernible. On the one side there were those of average and above average income who would not be affected by reduced government spending. They were led by Howard Jarvis and Paul Gann and made the running throughout the campaign. Opposed to them stood the state governor, Gerry Brown, a 1980 presidential hopeful, most government employees and the minority and underprivileged groups who rely on various state welfare services.

So, by polling day, Californian voters used the opportunity to declare their opinion on property taxes as a rather crude way of expressing their own interests and class and race prejudices.

Proposition 13 was put forward by Jarvis, a 75 year old millionaire and executive director of a landlords' association and Gann, a property speculator. Jarvis declared optimistically: "One result of this tax rebellion is that blacks and other minorities will get lower rents, taxes and utility bills. It's the best thing that ever happened to them."<sup>1</sup> He claimed their proposition was a move against government profligacy and that ill-defined old bogey "bureaucracy".

Proposition 13 campaigners made much of galloping property tax assessments: in the current property price boom a house valued at \$40,000 and assessed for \$800 tax in 1977 might well be valued at \$60,000 and assessed at \$1,400 in 1978. This rate of price rises has not been matched by increases in income and so ordinary people have been saddled with substantial tax rises on their houses. Jarvis and Gann skilfully capitalized on this understandable discontent and directed it not against California's rampant land speculation, but against the state government tax which happened to be the most accessible to mass political action.

That California's property tax has two component parts was conveniently ignored by Jarvis and Gann. The latest sale price of a property is used as a basis for its taxes and also those of neighbouring properties which might not have changed hands for some time.<sup>2</sup> But the sale price has two parts. These are the value of improvements (houses,

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By Keith Thomas

offices, factories) and, secondly, the value of the land. Unfortunately the two values, and the two separate taxes they give rise to, are seldom separated analytically and certainly were not during the Californian debate. While a reduction in taxes on improvements will benefit enterprise, the corresponding reduction in land taxation will ensure that over time those benefits accrue to the major land owners.

Oligopolistic corporations have been saved millions in property tax (Standard Oil pocketed \$20m., Bank of America \$13m. and Pacific Telephone \$8m.<sup>3</sup>) But most startling has been the response of the private landlords. Even Howard Jarvis was forced to admit only a fortnight after the vote that most had raised their rents by an amount equivalent to the property tax reduction<sup>4</sup> and the inquisitive Californian press could discover only one example of a fall in rents.<sup>5</sup> Here we have clear evidence, albeit in reverse, for the economic proposition that tax on land values cannot be passed on!

One way to demonstrate that tax on land values cannot be shifted is by pointing out that a landowner wants money for things other than taxes. If he can increase his rents to pay his taxes, why does he not do the same when he has other needs? Landowners take all they can now by way of rent and would take more if they could.

In California the across-the-board reduction in property taxation has left the relative advantages of all the sites unchanged. The tenants previously agreed to only a certain level of rents, knowing that property taxes were also payable. Now, with lowered taxes, property owners have immediately raised rents to take up the slack. This

may be expressed as follows:

	Before Proposition 13	After Proposition 13
Tax	300	100
Rent	600	800
Outgoings	900	900

Those who voted for proposition 13 did so only because Federal taxes, such as income taxes, were not accessible through constitutional means. House owners have had their property taxes reduced but their Federal income taxes will rise (taking more money out of their state) because property tax payments are deductible from taxable income. Ironically, proposition 13 will thus enhance the power of the remote Federal government at the expense of local government over which the Californians have some control.

Big corporations, which pay little income tax, have reaped two-thirds of the benefits. Their share of the windfall will increase over time because one of the Jarvis clauses ensures that when a property is sold, its taxes will be assessed on the new (inflated) sale price and not on the 1975 base evaluation of surrounding properties, producing inequalities between neighbours. Since commercial properties change hands less frequently than houses, the relative tax burden will shift further on to house owners.

There are two points which are relevant for Britain. Firstly, within the next year or so British populists, with an eye to increasing their share of unearned increment, will probably promote a similar idea in this country. Secondly, a White Paper is expected soon containing details of enabling legislation for the conversion of British rating from a rental to a capital basis. It is worth noting that it was such a system which proposition 13 opposed.

In California it is inevitable that disenchantment with proposition 13 will increase. Tenants are furious at their rent increases<sup>6</sup>; Californians have belatedly awoken to the fact that property taxes will continue at the old level but with two thirds of them under the new name of rents. The judiciary have been threatened with violence unless they reverse the tax and minority groups have voiced vigorous objections to the cuts in welfare programs.

The economic effects have been entirely predictable. California now offers a remarkable opportunity to promote the full case for land taxation: Jarvis and Gann have primed the pump.

## REFERENCES

1. *Financial Times*, 29 June 1978.
2. *Ibid*, 1 June 1978.
3. *New Society*, 29 June 1978.; *Observer*, 2 July 1978.
4. *Guardian*, 24 July 1978.
5. *Financial Times*, 29 July 1978,
6. *Christian Science Monitor*, 20 July 1978

SPOTLIGHT

ON CALIFORNIA'S TAX REVOLT