

LAND VALUE TAXATION

AN INCENTIVE TO BUSINESS, HOUSING, JOBS
AND A STABLE REVENUE BASE FOR PHILADELPHIA

Prepared
by

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The tax figures on Philadelphia properties contained in this paper are not intended as conclusive for all properties in each class. They are selected cases from preliminary data used to illustrate, in local terms, the findings in other cities. Mr. Collins is conducting a detailed study of Philadelphia.

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LAND VALUE TAXATION: AN INCENTIVE TO BUSINESS, HOUSING, JOBS AND
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In recent years, the growing tendency has been to reduce the reliance on the real property tax in favor of wage, business, and other "nuisance taxes." The aim of such shifts is the often-stated desire to "broaden the tax base" and relieve the homeowner of an increasingly burdensome and unfair form of taxation. Not surprisingly, in Philadelphia, the wage tax now produces 42% of the revenue locally raised while the real estate tax supplies only 38%.

The questions of equity and distribution become as important a consideration when we propose to tax buildings less and land more as are the economic incentives for business growth, new housing and rehabilitation starts, jobs and revenue expansion.

Two facts regarding taxation should be initially recognized.

1. There are only two sources of revenue.
 - a) Labor created wealth or improvement values.
 - b) Community created land value.
2. Taxes are simply like pumps which draw revenue from one source or the other.

It is an undisputed economic fact that all taxes imposed on any product or human activity, by whatever name they are called, (such as the 4-5/16% net profits tax, 4-5/16% earnings tax, 2 mill general business tax, 4 mills on personal property, 4 mill mercantile license, 4-5/16 wage tax, etc to name but a few that we have in Philadelphia) will either cause their payers to leave town or increase the cost of

production of goods and services, reduce their supply and increase prices to the ultimate consumers. Clearly, the shift away from the real property tax merely disguises the increased amount of taxes being taken from the homeowner/consumer in the form of higher prices or spreads out the increases in smaller periodic deductions from wages enabling more to be collected with less resistance.

The reported loss of 3300 businesses and 130,000 jobs over the last eight years and a projected job decline of 2% per year for the next ten years must compel a serious re-examination of any practice that injects such deteriorating tendencies into the economy.

Authoritative information on the attitude of the financial community and from official studies of the City's economy identifies the wage tax, and by implication must include the other taxes listed above, which increase costs, reduce productivity and increase prices, as being largely responsible for the poor business climate, the flight of industry, and the loss of jobs in Philadelphia.

What is not as clearly understood is that since land is not an item of production, is inelastic in supply and fixed to its location, a tax on its value has no ability to alter the supply by productive or locational adjustment and thereby bring about an increase in price.

The next administration must use every tool at its disposal to reverse the physical and economic decline of the city while closing the gap between revenues and expenditures that it will inherit. Land Value Taxation offers the best hope for achieving those goals with minimum disruptions from layoffs, reduced services and unaffordable tax increases.

To quote the report of a conference on the Financial Crisis of our Cities, sponsored by the National League of Cities, U.S. Conference of Mayors, the National Commission on Urban Problems and others -

"Too few tax levyers seem to understand that the property tax is not just one tax; on the contrary, it combines and confuses two completely opposite and conflicting taxes, and it would be hard to imagine two taxes whose consequences for urban renewal and urban development would be more different."

"One of the two conflicting taxes fused and confused in the property tax is the tax on the improvement--the tax on what past, present, and future owners of the property have spent or will spend to improve it. And it must be obvious to anyone that heavy taxes on improvements are bound to discourage, inhibit, and often prevent improvements."

"The other levy confused in the property tax is the land tax--the tax on the location value of the site, the tax on what the property would be worth if the owners had never done anything or spent anything to improve it, the tax on the value that derives most from an enormous investment of other peoples' money and other taxpayers' money to create the community around it and make the location accessible, livable, and richly saleable. And it must be obvious to anyone that heavy taxes on the location cannot discourage or inhibit improvements; on the contrary, heavy taxes on location could put effective pressure on the owners to put their sites to better use so as to bring in enough income to earn a good profit after paying the heavier tax."

Philadelphia imposes a tax of \$6.175 per \$100 of assessed valuation on land and buildings combined. A property assessed at \$100,000 (\$20,000 land/\$80,000 building) is subject to \$6,175.00 per year in taxes. An adjoining land site of the same size, that is vacant or occupied by a structure so deteriorated that it may even have a negative value, will be subject to a tax of \$1,235.00 a year. As soon as it is developed to the level of its neighbor, the tax liability would jump by \$4,940.00 a year. Specific example: - Two adjacent warehousing sites in the 300 block of Market Street of approximately the same lot size. One assessed \$9,000 on land and \$900 on

building. The other, \$10,800 on land and \$31,900 on building. The former is obviously grossly underimproved and in fact may be unused. The taxes on that property is presently \$611. annually. if a warehouse comparable to its neighbors were to be constructed, taxes would soar to \$2,525.

Prof. Mason Gaffney, Chairman Dept. of Economics, University of California - Riverside, and formerly economist with Resources for the Future explains its impact in this way -

"If you compare the real estate property tax on construction with an excise levied once at the time of construction, the weight of the deterrent becomes plain. A 3% of true value tax, such as we have in Milwaukee and many other cities, is the installment plan equivalent of a 52% sales tax, that is, it costs the owner as much each year as a 52% sales tax would cost him if financed over the life of the building."

A tax of that magnitude falls like a dead weight on any prospective restoration or new construction in the city. Philadelphia's .06175 on 50% of market value assessment is approximately 3% of true value. Such conditions limit private investment to only the glamorous kinds in the most profitable areas (Gallery, New Market, Jefferson Hospital, etc). And even those must very often be encouraged by subsidized land.

The re-investments that are now concentrated in specific "fringe" neighborhoods of center city are also fair examples. The countless other neighborhoods of the city that are in various stages of abandonment, vacancy and deferred maintenance will only receive the individual and commercial investment necessary to preserve them when higher land and lower building taxes alter the arithmetic of ownership to make it affordable and profitable.

The need for a higher land tax is spelled out in the House of Representative's Committee on Banking, Finance and Urban Affairs Sub-Committee report on the City, chaired by Congressman Henry Reuss,

..."A high tax on buildings creates a bias against land use, as already pointed out. But a low land tax is the clincher. If land values are rising rapidly, or if landholders expect that they will, the low land tax encourages the waiting game. The owner figures the tax as a holding cost, one that is readily affordable if there is evidence that annual increases in land value substantially exceed the annual taxes on it. Some speculators cover the holding cost by what are known in the real estate fraternity as "taxpayers"-old stores leased to porno shops, ramshackle apartments, and most notoriously, surface parking lots."

"A high land tax, geared to the market potential of sites, would have the contrary effect, according to Philip Finkelstein of the Center for Local Tax Research. It would make it costly to hold valuable land in cold storage. Owners would be inclined to put their sites into use or to sell out to others in the market. As intensive commercial and industrial users find access to central city land, areas less suited to these purposes will accommodate various types of housing, or the kind of convenience village shops that too often are missing from residential neighborhoods."

In downtown Philadelphia on busy Market Street West, there is a row of obsolete two and four story structures in the 1900 block. One of those buildings, assessed at \$6,700, occupies a site assessed at \$91,400. The tax liability is approximately \$6,057. Assuming that the assessed value is 50% of market value as the assessor declares it to be, that land is worth \$182,800 and growing. The owner is content to earn enough to pay the taxes while he waits for an enterprising developer, or more likely, a redevelopment program to buy him out. The same is true of the surface level parking lots that preempt most of that area and so many other sites in center city.

The advantage of the land value tax over the wage tax as a revenue source was clearly demonstrated by studies in Pittsburgh prior to the adoption of a 48 mill increase in land tax in December, 1978 to help fill a \$23.2 million revenue gap. The 48 mills will cost the average homeowner \$62 a year while the equivalent wage tax for the same amount of revenue would have cost the average wage earner \$188 each year.

If Philadelphia sought to raise the approximately \$50 million deficit hidden in the recently announced budget, it would require either a .0368 additional tax on land, .0088 addition in the existing property tax or .006 addition to the wage tax. A homeowner in the neatly kept 3200 block of Carlisle Street in North Philadelphia (where incidentally, assessment is closer to 75% of market value than to 50% as it is supposed to be) with a property assessed at \$4,100, the land being \$800, would pay in land tax \$29, or with the existing property tax, \$36. However, on an assumed income of \$7,000, the wage tax would take \$42. a year. A home in the 1100 block of E. Johnson Street (E. Mt. Airy) assessed at \$13,000, land at \$1900, and with a conservative estimate of \$15,000 income: Land tax cost/would be \$70, with the existing property tax \$114, or \$90 on estimated income of \$15,000. When it is considered that such families are likely to have at least two wage earners, the wage tax appears even more costly. (Most wage earners may not be conscious of the higher cost of a wage tax because it is collected weekly from their paychecks and never seen. But the property tax is often paid in an annual lump sum that hurts. Perhaps some means should be devised to withhold the land tax from paychecks which would make it more palatable as well as more

equitable than the wage tax.)

Well improved homes, commercial and industrial property benefit from a land tax because most of their value is in the structure. Underimproved and vacant land rightfully bear the heavier burden. Two sites in the 2000 block of Market St. illustrate the point. A surface level parking lot, assessed at \$2,045,600, would pay an additional \$75,200 but only \$18,000 using the existing property tax method. Facing it directly across Market St. on a lot slightly less than half as big, is a multi-story office building with a total assessment of \$13,046,100, of which \$1,164,000 is land. That property would pay an astounding \$114,800 increase if the tax rate were on total value (compared to \$18,000 for the vacant lot). It would pay \$42,800 with the land tax, \$32,000 less than its land speculating neighbor.

The City administration already recognizes the effectiveness of lower land price to attract businesses and jobs. Industrially zoned land, owned by the City, has been available for purchase at as low as 10% of its market value for some time. The more affordable first cost could be achieved for privately owned land as well. It would require a land value tax high enough to discourage speculative holding to bring the price down. The current program does nothing about the continuing, high annual cost of doing business in the City. Government may not be able to bring about changes in industrial work rules, nor convince labor to moderate its wage demands in this inflationary period, but it can provide

compensating tax incentives by removing the tax entirely from buildings devoted to commerce and industry.

Pittsburgh, Pa. used the taxing tool effectively to secure the private rebuilding of its downtown in the 1940's. Its half as heavy tax on buildings than on land was strong inducement for major corporations to build there. The result was the development of the enviable Golden Triangle. (The 48 mill increase in the land tax last December now gives Pittsburgh a 4:1 land to building ratio.

In 1974 Harrisburgh made a tentative step toward heavier land tax and extended it in 1977. The land to building ratio is now 1.8:1.

Studies in Washington, D.C., Kansas City, Milwaukee, San Francisco, Newark, Wilmington and New York have all spelled out the wisdom of taxing land more and improvements less. Congressman Henry S. Reuss, Chairman, House Banking, Finance and Urban Affairs Committee, Ralph Nader, economist Alfred Kahn, Chairman of the Council on Wage and Price Stability and Kenneth Gibson, Mayor of Newark, N.J. have all said that taxing land more and buildings less would be better for cities.

Because it is a First Class city, Philadelphia may need legislative provision to enact full Land Value Taxation. But there is no real obstacle to its obtainment since it is already permitted in every other city in the State. It depends only upon the will of the administration.

Philadelphia is at a crossroad in its history. Bold, imaginative steps must be taken by those who care, to

arrest its decline and place it on a path to economic, social and spiritual vitality.

Recommendations:

1. Finance all deficits by an increase in the land tax rate only.
2. Exempt all new commercial and industrial construction on vacant land from building assessment.
3. Automatically exempt all expansion of existing plant facility from assessment.
4. Exempt all new residential construction and renovation in depressed or declining areas from assessment.
5. Institute a 4 year program to shift the property tax off buildings to land only.
6. Bring all land assessment up to 50% of market value.
7. Make the office of Real Estate Assessment a department of the City.
8. Require the assessor to publish a land value map annually and maintain the established assessment to market value ratio.

PROCEDURES FOR A PHASED INTRODUCTION
OF
LAND VALUE TAXATION IN PHILADELPHIA

In order to shift the property tax from buildings to land in four years, the present tax rate on buildings may be reduced by 25% each year and the revenue loss recovered by the appropriate increase in the land tax rate.

Using the formula below, with the current assessment figures, tax rate and revenue yield, the results over the next four years are shown in the table.

Assessed Value:	Buildings	\$4,297,127,800.	
"	"	Land	1,359,175,040.
"	"	Total	5,656,302,840.

City & School District
Combined tax rate .06175

Current Property Tax revenue \$ 349,276,690.

To continue producing the same amount of revenue each year and where:

LTR = Land tax rate
R = Revenue needed
BA = Building assessment (total)
BTR = Building tax rate
LA = Land assessment (total)

$$LTR = \frac{R - (BA \times BTR)}{LA}$$

LA

	BTR	REVENUE	LTR	REVENUE
1981	.0463	\$198,957,010.	.1106	\$150,319,680.
1982	.0308	132,351,530.	.1596	216,925,160.
1983	.0154	66,175,768.	.2083	283,100,930.
1984	0	0	.2568	349,276,690.