

# AFFORDABLE HOUSING FROM A LAND VALUE PERSPECTIVE

By Albert S. Hartheimer, Lanesborough, MA

Presented November 2, 2000 at the Building on Our Heritage Conference on affordable housing, hosted by the Western North Carolina Housing Partnership)

Webster defines "afford" in this way: to have enough or the means for; bear the cost of, without serious inconvenience; and Webster defines "housing" in this way: to provide, or serve as, a house or lodgings for. So we are talking about providing places to live, the cost of which can be borne without serious inconvenience.

I spent all of my working life in Albany, New York. Albany is a 300+ year-old-river-front city on the westbank of the Hudson River. As you go west from the Hudson the land rises gently, then sharply, then gently again. The first housing in Albany was on the bank of the river. Next, those who could afford to, moved west, up the first gentle incline. There today you will find "Grand Street", a street lined with what were originally very lovely three and four story single family row houses. After a while people moved further west to a section called "The Pine Hills". I lived in a modest house in the Pine Hills when I was first married and then, along with many others, I built a house in the suburbs. As people moved to the suburbs, the houses no longer suitable for the avant-garde in the Pine Hills, became the affordable housing of those less wealthy and the housing on Grand Street was converted to apartments and used as affordable housing for the poor. And that's the way it is today.

In addition, more recently, in the fifties, new high-rise housing was built for the poor. Those buildings were destroyed by the tenants and for a long time stood as empty shells, then the government spent more millions rehabilitating them and, today they do house some of the poor. It would have been better and cheaper if the "Pruitt-Igoe" solution had been used, namely to blow-up the buildings and get rid of them entirely.

More recently, having learned that the poor do not want to be housed in high-rise buildings, the government has financed low-rise row houses, garden apartments and single separated houses. These have been more successful, but they all have, what to me is a great disadvantage, the effect of ghettoizing the poor. There have been many other programs with which you are undoubtedly more familiar than I am, of providing affordable housing. But the supply has never been able to catch up with the demand, and that's where we are now.

After World War II there was great demand for housing for returning veterans and others. Builders were anxious to build to satisfy this demand, but the banks were reluctant to take the risk of lending money to develop land in what was then the clean and green countryside. The government solved this problem with VA and FHA loan guarantees. Now, with the return of their money their money guaranteed, the banks were willing to lend. And lend they did, with a vengeance! People were housed, but along with the housing came the need for new roads, new schools, new water lines, sewers, electric and tele-

phone lines and now, fifty years later we are dealing with the very considerable problems of urban sprawl.

Because of the low density of population in the suburbs and the lack of people in the cities, mass transit is no longer economically feasible, so it is subsidized by the government or not available at all. We spend unconscionable amounts of time and money commuting to everything. The social fabric of the cities is being destroyed and not being replaced, in the main, and there are other problems. Now we are being bombarded with "solutions" to the problems of urban sprawl.

After expending billions of our tax dollars on an unending variety of programs we still have the problem of not enough "affordable housing".

Why is that?

It is because all of the solutions for the problem have been topical. If you don't have enough housing, build houses! If the banks won't lend money, guarantee the loans! And so it goes.

None of the solutions have recognized the economic root cause of the problem. And that's what we're going to discuss.

Now, however, I want to describe the typical small American city today. Usually there is a "downtown". Usually consisting of the City Hall, some banks, some office buildings, some museums, some institutional buildings like the YMCA and a regional hospital. There are also some stores, but the big department stores have gone to the suburbs and the "big-box" stores, Wal-Mart, Home Depot and the rest are nowhere to be seen. There are also some residences, most likely for the poor and some for the wealthy, but the middle class has fled.

And then there is vacant land, lots of it. In Asheville, there are about 4000 parcels of residential vacant land out of about 25,000 parcels, that's 16% of the total number of parcels and that represents about 13% of the total residential land value. There are also 500 parcels of commercial and industrial vacant land out of a total of 3500 parcels, about 14% of the total number of parcels which represents 8% of the total non-residential land value. That's a lot of vacant land. Why does it remain vacant in the face of the need for affordable housing? Probably the biggest factor is the low carrying cost of a vacant lot. In Asheville, on average, the annual tax on a vacant residential lot is about \$200. With a carrying cost so low, the incentive is to hold on to the lot with the hope that the city will recover and the value of the lot will increase.

Let us now consider the components in the cost of housing. There are three: labor, materials and land. According to Walter Rybeck (in "Affordable Housing--A Missing Link, Center for Public Dialogue, 1988): "Building materials in 1987 cost about 2.1 times what they did in  
(continued on page 11)

## AFFORDABLE HOUSING (continued from page 2)

1970, but the inflation rate for the same period raised prices to about 2.9 times their 1970 level. Similarly, wages for construction workers rose 2.4 times between 1970 and 1987." But the price of land in the same period rose about 5.7 times.

This is one result of a low carrying cost and, according to Rybeck: "This is why the price of a home has grown out of reach for so many Americans, particularly young families seeking their first house. Soaring land values are locking all but the very wealthiest out of the housing market."

In the publication *Incentive Taxation* (Center for Study of Economics, June, 1990), I read "A just released study by the Urban Land Institute reveals that the nationwide average price increase for residential land during the past five years was 51% while consumer prices increased only 26%".

The property tax is the principal tax levied by cities on real estate. It is a tax on land and buildings. These two taxes are totally different and work against each other. A tax on buildings discourages building. A tax on land encourages building. In Asheville, for the city tax, the tax on buildings is 78% of the total tax and the tax on land is 22% of the total tax. If you build a nice home in the city, one of your first visitors will be the tax assessor. The tax you will have to pay is the penalty for improving the city. The nicer the house, the higher the penalty.

A 1991 "Not In My Backyard--Removing Barriers to Affordable Housing" report to the President by the Advisory Committee on Regulatory Barriers to Affordable Housing said the following.

"In most places, the real property tax is a tax imposed on the combined market value and improvements of both land and buildings. The tax, however, discourages land development and rehabilitation, because they increase the value of the property and the tax that must be paid.

"An alternate solution for communities is to impose low tax rates on structures and high tax rates on land. This approach will raise the cost of holding land vacant (or leaving structures on the land unrehabilitated), will not penalize land development, and can result in more efficient land use, including increased affordable housing opportunities.

"The combination of the high cost of land and the punitive nature of the present property tax are the root causes of the lack of "affordable housing." No wonder the cities are in the shape they are today. No wonder there is not enough affordable housing.

To make housing more affordable we advocate the reduction of the tax on buildings and a simultaneous rise of the tax on land to yield the same or more revenue. We call this Land Value Taxation. It is also called the two-rate tax, incentive taxation and the split-rate tax.

We know, from studies of the twenty Pennsylvania taxing jurisdictions that use LVT, that every time the tax on buildings is reduced and simultaneously the tax on land is increased, that there is a spurt

of construction. According to Plassmann and Tideman (in "Analysis of the Effects of Two-Rate Property Taxes in Pennsylvania, 1997), "This means that, for an average municipality, an increase in the adjusted tax differential of 1 mill will yield an expected increase in the total value of construction of 1.58%". Much of this increase in construction comes from people improving their homes with the knowledge that the penalty for making improvements is being reduced.

Does this provide more affordable housing?  
Pittsburgh has used the two-rate tax since 1915, 85 years.

Recently, Lew Sichelman (L.A. Times, 6-4-00) said: "According to the federal government's latest tabulation, the average of both new and existing houses sold in 31 key markets nationwide reached \$200,300 during the first three months of this year. ... The San Francisco Bay Area ... remains the most expensive place in the country in which to buy a house. The average price there is now \$384,700. ... At the other end of the price spectrum, the average remains under \$150,000 in only two places: Pittsburgh at \$143,300 ... and St. Louis at \$145,100."

So Pittsburgh, the only sizeable city in the United States to use the two-rate tax, has the lowest cost housing in the country. A coincidence? I don't think so!

An interesting and amazing thing about the Pittsburgh experience is that the two-rate tax in Pittsburgh applies only to the city tax, not to the school tax and not to the county tax. It's impressive to say that for the city tax the tax rate on land is six times higher than the tax rate on buildings, but because of the much higher value of buildings, only about 57% of the city tax is from land. When you add the school tax and the county tax, less than 40% of the tax yield is from land.

So with a modest land tax applied over a long period of time, 85 years, the result is the lowest average cost of housing in the country. Imagine what would happen if the tax on buildings were eliminated and all of the city revenue came from the land tax. It boggles the mind to think about it.

David Roodman (in *The Natural Wealth of Nations*, 1998), wrote: "In the twentieth century, Melbourne, Australia, has been one of the best laboratories for the study of shifts toward land value taxation. Half of the 56 local governments within the metropolitan area eliminated the building tax between 1919 and 1986 and increased the land tax. Today, not surprisingly, districts that do not tax buildings have more of them. In fact, they have population and housing densities half again as high as those with conventional property taxes, even after controlling for distance from the city center, amount of industry, and other relevant factors; the difference is greatest for districts that switched earliest. And more construction within the city limits has reduced pressure for expansion beyond."

Johannesburg, South Africa has no tax on buildings.

The entire property tax is on land. Mason Gaffney, a highly respected land economist, a Professor of Economics at UC-Riverside, visited Johannesburg. This  
(continued on page 12)

is what he said about it (in a report to R. Schalkenbach Foundation, March 1992):

"The miracle of Johannesburg. Jo-burg is a Bootstrap City. It should have died when its gold mines played out, like a proper mining boomtown; instead it remains as the economic capital of its nation and half a continent. Johannesburg defies most laws of urban economics, e.g. that mines create no great cities. Explainers still cite the mines, but its mines have played out; it should now be a ghost town. It has no harbor, no water transportation, nor even any gravity water supply. It is, in fact, on a ridge top, the Rand or "reef", at an elevation of 5,000 ft. It has no sunburst of rail lines, like Chicago or Boston, "The Hub", except perhaps what it has attracted itself. It is "on the main rail line", Explainers say, but so are 1000 miles of other sites. The natural site lacks outstanding amenities, and certainly can't hold a candle to Cape Town. Jo-burg has no governmental economic base. Surrounding farmland is poor. Why Johannesburg? Why is it the largest city, the center of finance, industry, commerce, and international air travel?

"As a public finance economist I may overvalue incentive taxation, but Jo-burg has it. The property tax is on site value only, and at a high rate: they tell me it is 4%. This is what makes Jo-burg distinctive. Challenge and response: Jo-burg had to do something right in order to survive, and that is what it did. It not only survived, it became and remains Number One. Give me a better explanation and I'll back off. I haven't heard one yet."

Harrisburg, Pennsylvania started using the two-rate tax in 1975 with a very modest shift of tax off buildings, onto land. At that time it was known as a municipal "basket case", with over 4000 vacant structures. Since then it has shifted more tax off buildings on to land in several steps. Today the tax rate on land is 4.89%, the tax rate on buildings is 0.9618%. Today there are less than 500 vacant structures and Harrisburg is considered an up and coming city.

Mayor Reed in a 1994 letter to Patrick J. Toomey said the following. "The City of Harrisburg continues in the view that such a land value taxation system, which places a much higher tax on land than on improvements, is an important incentive for the highest and best use of land in already developed communities, such as cities." "Moreover, the same two-rate system tends to discourage real estate speculators and others who would be inclined under normal conditions to tie up land tracts that could otherwise be used for development purposes." "With over 90% of the property owners in the City of Harrisburg, the two-tiered tax system actually saves money over what would be otherwise a single rate system that is currently in use in nearly all municipalities in Pennsylvania." "I should note that the City of Harrisburg was considered the second most distressed in the United States twelve years ago" "Since then, over \$1.2 billion in new investment has occurred here, reversing nearly three decades of very serious decline." A coincidence? I don't think so!

Asheville would be a much more livable, alive city if it had no tax on buildings and taxed only land. There would be fewer vacant lots and more affordable housing. In order to reach this goal it is important that there not only be a good end result, but that it be

politically feasible at every step along the way to reaching the goal.

The study made by the Center for the Study of Economics entitled "Affordable Housing in Asheville, N. C.: Can a Land value Tax be an Answer?" provides the answer we need. It says that in a shift of tax off buildings and on to land, 70% of residential parcels would see a reduction in tax or no change. It also states that residential properties now pay about \$11,000,000 in property taxes. With no tax on buildings this drops to \$8,744,000, a reduction of \$2,256,000 or 20%, that is a very significant overall reduction for residential properties. Since these people are the voters and since the majority will pay less tax, their support will be forthcoming and it is politically feasible to shift to a land tax in Asheville.

What are the steps to be taken to implement land value taxation in Asheville? First, there has to be broad support for this idea at the grass roots. The public must understand the theory and practice of land value taxation. At the same time the city government, the Mayor and Council must understand and support the proposed change. Then, a state law must be enacted giving Asheville the option of shifting to a two-rate tax and then the Council must pass a local ordinance adopting the two-rate tax and setting the rates.

Easier said than done, but not impossible. The single biggest problem will be inertia, simple resistance to change. Everyone favors change when it applies to others. That's a given, but this is a common sense idea which, when properly introduced and explained, can generate public support. The experience in Allentown, Pennsylvania, where there were two referenda on this question, both of which won the support of the majority, gives us confidence legislation is passed, only a change in come that it can be done here. There's lots of support available to help you on your way.

There are many advantages to land value taxation other than the one's already stated.

No State or Federal aid is needed to implement this idea. After the necessary legislation is passed, only a change in computer programming is needed to change the tax bills.

This is a very progressive tax. We believe, in taxation, that the rich should pay more than the poor. The poor own or use very little land and will pay very little land tax. The middle class owns only the land under their homes and will pay modest amounts of land tax. All large and valuable tracts of land are owned by corporations or wealthy individuals, they will pay the most land tax.

This is an easy tax to collect and a difficult tax to avoid. Land is there for everyone to see. You can't put it in a Swiss bank account. You can't burn it down and you can't move it.

(continued on page 13)

## AFFORDABLE HOUSING (continued from page 12)

So what do we know?

We know that land has no element of labor in it, land is just what is found in nature and, therefore, in taxing land we are not taking the bread from anyone's mouth.

We know that every time the tax on buildings is reduced, somebody builds.

We know that every time the tax on land is raised, somebody builds.

We know that in Harrisburg, Pennsylvania, in the 12 years since the introduction of the two-rate tax, the number of vacant structures was reduced from over 4000 to under 500.

We know that in Pittsburgh, with just a modest land tax over 85 years, the cost of housing there is now the lowest in the country.

We know that in Melbourne, Australia the parts of the city that use the land tax have housing and population densities higher than those parts that use the conventional property tax.

And finally, we know that Johannesburg, South Africa, one of the cities in the world that does not tax buildings at all, has grown and prospered without any of the natural advantages that such large cities usually have.

Will this idea solve Asheville's affordable housing problems overnight? No it won't, but it took a long time to create the problems and it will take time to solve them.

Will it be easy for Asheville to change from a conventional property tax to a two-rate tax. No, it won't, but it can be done.

Will it work in Asheville? Will it help create affordable housing in Asheville? Yes it will, you can and I would bet on it.

I commend your interest in this idea and hope you will persevere until there is only a land tax and no tax on buildings in Asheville.

---

(editor's note: Albert Harthheimer is a retired architect. He is a member of the Boards of Directors of the Center for Study of Economics, of the Henry George Foundation of America, and of the Robert Schalkenbach Foundation.)

---