

Method For Determining Groundrent

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THOSE of us who believe in the validity, efficacy and justice of George's remedy, accept without question his fundamental moral postulate that every human being is equally entitled to the bounties of nature.

Groundrent, by definition, is the measure of the community's contribution to production. How much is the groundrent? Is it less, equal to, or more than public expenditures? Justice demands its collection by the community regardless of its amount, but it is certainly important for us to try to get an idea of its amount compared to current taxes.

Many Georgists and non-Georgists have attempted to estimate total groundrent in the United States, but the assumptions employed have not been generally acceptable, apart from the fact that the only data available are assessed valuations which are notoriously unreliable and involve errors that may be of the magnitude of 50% and more.

I propose to demonstrate a method which, as far as I know, is original and unassailable. I am indebted to William V. Burnell for a short-cut in the calculations but not for the principle involved. He is a past president of the American Society of Appraisers and he goes only part way with George. After we discussed some of his views he encouraged me to write an article for The Appraisal and Valuation Manual in which I used some of the short-cuts he had devised. These led me to the method I wish to demonstrate here.

The initial assumptions or "givens" for the numerical example (table 1) are:

1. The market value of the site is known to be \$25,000.
2. The market value of the building is known to be \$100,000.
3. The site is assessed at \$15,000 (60% of market value).
4. The building is assessed at \$60,000 (60% of market value).
5. The tax rate is 5%. This is equivalent to 3% of market value. (Although assessors are supposed to use the same percentage of market value for sites and buildings, this is not accurately or uniformly followed.)
6. TAX SITES ARE NOT SHIFTABLE; BUILDING TAXES ARE SHIFTABLE. These are essential links in George's reasoning and most economists accept these statements.

To determine groundrent, assume that overnight George's remedy goes into effect. The full amount of groundrent is due the city, hence the market value of the site falls to zero. The owner loses his investment in the site and his investment now is \$100,000—the market value of the building alone. There is no longer any tax on the building, a saving to the owner momentarily of \$3,000 (see line 5, table 1). But sooner or later the supply of buildings by new construction and renovation will be increased because of the tax saving. Income from the building will go down by \$3,000 because the effect of the tax saving is anticipated in the market place. The tenants will get the benefit of the owner's saving of \$3,000. (See table 2).

Just to check the algebraic formula for groundrent, namely $(t+y)$ times the market value of the site, substitute for t , the tax rate, 3%; for y , the yield,

Table I.

(1) Market value of site	\$ 25,000	(1) Market value of site	L
(2) Market value of building	100,000	(2) Market value of building	B
(3) Total	125,000	(3) Total	L+B
(4) Real estate tax on market value of site: at 3% of (1)	750	(4) Real estate tax on market value of site: at t% of (L)	tL
(5) Real estate tax on market value of building: 3% of (2)	3,000	(5) Real estate tax on market value of building: at t% of (2)	tB
(6) Total real estate tax	3,750	(6) Total real estate tax	t(L+B)
(7) Owner's yield on site at 9%	2,250	(7) Owner's yield on site at y%	yL
(8) Owner's yield on building at 9%	9,000	(8) Owner's yield on building at y%	yB
(9) Total yield to owner	11,250	(9) Total yield to owner	y(L+B)
(10) Total tax plus total yield: (6) + (9)	15,000	(10) Total tax plus total yield: (6) + (9)	(t+y)(L+B)

If, as we have assumed, the gross income is just sufficient to pay all expenses and charges including taxes and yield, we can call the amount on line (10) which is \$15,000 on the left and $(t+y)(L+B)$ on the right, the AMOUNT AVAILABLE for taxes and yield.

Table 2.

(11) Market value of site	\$ 0	(11)	O
(12) Market value of building..	100,000	(12)	B
(13) Total	100,000	(13)	B
(14) Real estate groundrent	R	(14)	R
(15) Real estate tax on building	0	(15)	0
(16) Total due city	R	(16)	R
(17) Owner's yield on site	0	(17)	0
(18) Owner's yield on building at 9%	9,000	(18)	yB
(19) Total yield to owner	9,000	(19)	yB
(20) Original AMOUNT AVAILABLE	15,000	(20)	$(t+y)(L+B)$
(21) Reduction in AMOUNT AVAILABLE because tax saving on building is passed back to tenants	3,000	(21)	-tB
(22) New AMOUNT AVAILABLE for groundrent and yield $(R + 9,000)$	12,000	(22)	$tL+yL+yB$
(23) Deduct owner's yield (18)	9,000	(23)	-yB
(24) Balance = groundrent = R	3,000	(24)	$(t+y)L$

9% ; and for the market value of the site \$25,000. The result is \$3,000 which agrees with the example.

The formula is applicable even if the site is vacant or poorly used. It must then be assumed that if the site were reasonably well used it would yield 9% to the owner after all expenses. Although actual yields today vary from about 6% per annum, depending on the financial responsibility of the tenants and the type of property (apart from speculative distortions), to 20% per annum — 9% is a reason-

able over-all figure.

In volume 2 of 1962 Census of Governments (U.S. Department of Commerce) the total imputed market value of local assessed real property in the U.S. is estimated to be \$970 billion. The land portion is estimated by others at 30% of this figure, or \$291 billion. Using the formula derived in this article, groundrent in 1961 is 12% of \$291 billion or \$35 billion. The land value estimate is undoubtedly low and in 1966 I would estimate that groundrent in the U.S. is at least \$50 billion.

Conference News in Montreal

AMONG the several press stories which appeared in both French and English in Montreal during the Henry George Conference July 26-30 at the College Jean de Brebeuf, there was a long interview with Ted Gwartney in the July 29th Montreal Star.

"Basically," stated the interviewer, Hal Winter, of the 26-year-old assessor of Southfield, Michigan, "his ideas, which are culled from the theories of the 19th century economist, Henry George, are that all building, including housing, should be exempt from any taxation.

"Instead, the land—all land—should be subject to taxation at its real value. This would be an effective curb on speculation, involving the buying of land and its subsequent resale at an inflated price. People wouldn't buy land if they knew they'd have to pay a yearly tax based on the true value as it rises from month to month.

"In addition, since the potential developer of property wouldn't have to make an excessive capital outlay for land purchase, much more could be spent on the actual building. Since the tax exemption would apply to commercial establishments as well, consumer prices would drop and there

would be more employment opportunities."

Initial steps in reassessing properties began in Southfield five years ago. As a result the population doubled and about 500 major U.S. corporations have built new office buildings there.

"But there's still a long way to go," the assessor said. "The state laws must be changed and, finally the central government in Washington will have to accept the plan before it can become really effective throughout the U.S."

Coming as it did at the height of the anxiety about the Detroit riots, emphasis was placed on Mr. Gwartney's belief that his taxation theories, if adopted, would cut income and sales taxes and high prices, and the slums "would disappear of their own accord."

On the following day many newspapers carried excellent reports on the banquet address of the Honorable A. W. Roebuck, long a firm believer in the principles of Henry George. As always, he delighted the audience with his masterful speech, being still keen, eloquent and mirthful at 89.

The September HGN will present his address and a further conference report.