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# WHY PENALIZE BUILDING



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*Tafelberg*

# TAXATION, AS RELATED TO ARCHITECTURE AND THE PRACTICE OF THE PROFESSION

## INTRODUCTION

Recent and present paralysis of the architect's activities, and the collapse of the building industry, have prompted inquiry by this committee, into conditions which originate outside the architect's scope, but vitally affect his affairs. Cessation of building operations cannot be explained by anything inherent in the architect's function. Its causes must lie elsewhere. Certain it is, however, that the fate of the architect is inevitably bound up with that of a building project.

## BUILDING PROJECT

A building project embraces two general sub-divisions—structure and site. As to structure, there are two sets of problems, both of which fall within the province of the architect. One, architectural, deals with plan, design and supervision; the other, financial, deals with estimates, contracts and payments. As to site, there are also two sets of problems, but there is this difference between them: one, architectural, dealing with topography and landscape, falls within the province of the architect; while the other, financial, dealing with ownerships, leaseholds and taxation, falls within the province and responsibility of the client.

## INCALCULABLE FACTOR

Ownerships and leaseholds are definite factors; they are known and understood for what they are. Taxation, however, is a vague, incalculable factor, which, from all familiar signs, is generally regarded as a universal cause of social and governmental vexation. For this reason,

this committee undertook to examine effects of taxation—and rent which is involved with it—upon architecture and the practice of the profession.

#### FIRST PLAN OF INVESTIGATION

The committee's first idea was to compare effects of various forms of taxation upon the quality and amount of building. Information was obtained from several sections of this country and Canada, but it was found to be so devoid of any basis of comparison as to defeat that purpose. Discussion of it would have run to impossible lengths, and would have been of interest only to students of economics, as verifying suspicion that there is no scientific taxation anywhere fully in force.

#### PLAN ADOPTED

It was decided, therefore, to attempt analysis of taxation, as it pertains to buildings, from something like a scientific angle, with the hope that it would challenge thought upon the subject; that it would help rid the subject of some of the confusion which expedient methods now in vogue create; and that it would tend to remove the subject from the realm of uninformed opinion and place it in the realm of critical study, wherein the truth or falsity of the premises might find demonstration. That taxation has become an unbearable burden, the actual or threatened bankruptcy of cities is valid testimony.

#### THINGS TO FACE

In following this procedure, the committee realized that it would have to face, without prejudice, the unfuted statement that public improvements, even public virtues, enhance the value only of land. Also, the inconsistency of shrinkage of property values coincident with increasing population, as for example, that of Oregon the past year, reported by State

officials to be \$35,000,000. And, the more monstrous inconsistency, that whereas labor-saving devices have reduced the amount of labor necessary to produce essentials of living, they have not reduced the amount of labor necessary to obtain them, as index figures of commodity prices indicate. Through all the years of astonishing increase of efficiency of labor, due to improved machinery, these prices have kept going up, even while it has been made easier to produce these commodities.

#### BUSINESS STANDARDS

Since problems of taxation lie squarely in the field of business, the committee assumed that they should be subject to, and should be judged by, standards of business universally recognized to be sound. These standards require that all transactions be based upon a quid pro quo exchange—wealth of one kind for wealth of another kind—in which exchange both parties are satisfied that they receive the kind of wealth they want, more than the kind of wealth they give. How, then, do exigencies of taxation conform to sound business principles?

#### ARCHITECTS' ATTENTION JUSTIFIED

In connection with every building project, the architect should realize that his client either must have bought or leased a privilege to use some site, or he must do so. The measure of the annual value of this privilege is rent (not to be confused with rentals) which, capitalized usually on a twenty year basis, establishes its selling price. These facts justify attention of architects. They mean, that of the sum available for a building project, the amount paid for the privilege merely to stand a building upon the ground, reduces by that much the amount possible to put into the building.

#### SITE OWNER vs. BUILDING OWNER

Of course, similar consequences follow where site owner and building owner are the same person, but where loss in one pocket is made up by gains in another pocket, people are prone to overlook the causes of these losses and gains, which become clear where the pockets belong to different people. For clarity, therefore, in this report, the committee restricts the situation to one where site owner and building owner are different parties. It is proper, then, to inquire what a building owner receives in return for rent paid the site owner.

#### BASIS OF SITE VALUE

It is a plausible query, whether or not the average building owner has a clear idea of what goes to make a site worth the rent he pays for it. He knows in a way why he wanted the site, but does not analyze these reasons. If he did, he would realize that it was because at that particular location his tenants can enjoy individually and collectively created public advantages not to be enjoyed elsewhere, and that he can sell them these advantages along with the advantages of his building. No other location is exactly like his. It has possibilities in varying measure, of access to well-lighted, paved streets, parks, boulevards, schools and libraries,—to water, sewer and light services,—to transportation facilities,—to markets, banks, hotels, theatres, churches, stores and office buildings,—to health, police and fire protection; things necessary to the well-being of organized society,—which distinguish civilization from barbarism.

#### BASIS OF RENT

Did he ponder these things, the building owner would realize that these advantages were to be had at that particular location, because the requirements and desires of all the

people in pursuit of their happiness, had called them into being, with aid of labor, and of public and private funds, expended in every branch of industry. He would realize that it was the existence of these advantages, to be found in equal proportion nowhere else, that persuaded him to build at that location rather than elsewhere, and that it is for these advantages his tenants would pay him. Had he thought them not worth the price asked for use of the site, he would not have invested in a building at that location; he would have been under no compulsion to build there.

#### POSITION OF SITE OWNER

In other words, were none of these products of other people's efforts, both public and private, to be found there, the site would be valueless, because there is no known legerdemain whereby the site could be moved to another location where these same advantages might be had. Except for these fruits of community life, the site owner, as such, would have no power, though he have a legal right, to collect rent for the use of that site. He would be helpless to gather the wealth that comes to him as rent, unless his site be located where these products of the enterprise of a whole community are to be found.

#### TO WHOM RENT IS OWING

It is clear that the site owner does not own these public improvements. It is equally clear that he did not produce them. Yet, the privilege to use them is all that he has to offer the building owner in return for rent. Therefore, the rent he receives cannot, on sound business principles, be owing to him; it must be owing to those who produced the wealth embodied in these public improvements,—that is, the community as a whole. Rent is the public's natural income.

## RENT AND INTEREST

That he does, or can, collect rent, the committee found to be due—in addition to the fortunate location of his site—to common acceptance of the fallacy that rent for use of a site, and interest for use of capital, are the same sort of thing. If these were the same, they would be affected the same way by the same causes; but experience shows that they are not. For example, a tax on site values reduces the selling price of any site to which it is attached, because its payment reduces the net income from the site by the amount of the tax; but a tax on capital raises the amount that must be paid for the use of that capital,— that is, the higher the tax on a building, the more must be paid to occupy it. In other words, while taxes increase prices on labor products, they always reduce site prices. Rent adds nothing to total wealth, while interest is a natural increment of production.

## SITE OWNER RENT COLLECTOR

A building owner seeks opportunity to sell building accommodations, which are the result of the combined efforts of Labor and of Capital without the aid of the site owner; the site owner, as such, seeks a privilege to collect rent without contributing, as Labor and Capital do, to the wealth of the community. The site owner thus becomes the legal collector of community created values, although he could not claim to be the producer of them. What he receives is taken from wealth produced by Labor and Capital, and is measured by enormously increasing values of land.

## LAND VALUE ENHANCEMENT

George F. Nixon, former president of the Chicago Real Estate Board, was quoted in the Chicago Daily

News of March 8, 1930, as saying that the value of the metropolitan area of Chicago increased 1½ millions every twenty-four hours. At that rate, figuring rent at six percent, the people of Chicago, every day, must pay to their site title-holders, ninety thousand dollars more of wealth their labor and capital produces than they paid the day before, simply to breathe the air of that city. John A. Carroll, of the Hyde Park-Kenwood National Bank, speaking to the same Board, November 4, 1931, also is reported to have said that he knows of pieces of property in Chicago that increased thirteen thousand percent in twenty-five years. The City Affairs Committee of New York is quoted as reporting that the Eighth Avenue subway between Thirteenth and Forty-third streets, increased the values of sites along its route seventeen million dollars, not to mention those sites more remote.

#### SITE OWNER'S FUNCTION ABUSED

But, instead of requiring the site owner to function as official collector of individual payments for public benefits, turning them in to the government to be used to finance production of public benefits, he is, by long custom, and because of failure to analyze this situation, allowed to appropriate wealth that comes to him as rent, because his site happens to be in the midst of these publicly created benefits.

#### RESULTING PENALTIES

This, the committee holds to be a violation of sound business principles. Inevitably, it imposes a severe penalty; because, to make up the loss of rent paid the site owner, for use of public improvements he neither produced nor owns, taxes are levied on the private wealth of the very people who created the values in the site,

which the site owner is granted the legal privilege to sell.

#### PROPRIETY OF FUNCTION

Even children understand and realtors boast, that site values are created by the presence of population and the taxes it pays, and that these taxes are paid because they do provide streets, parks, schools, and all other improvements and services the whole community decides it needs. Why, then, should the building owner not insist that the site owner apply the rent paid him, to financing the things for which he receives rent, thus freeing the building owner from double payment of rent and taxes? Why should he pay for them once to the site owner and again to the tax collector? The answer seems to be, if sound business principles are to be adhered to, that if the building owner pays for these publicly created benefits in his rent, the site owner should supply them; if he pays for them in his taxes, there would seem to be no sound business reason for paying the site owner for them.

#### ENTITLED TO INTEREST

If the question be asked, Why is the site owner not "entitled to interest on capital invested" in his site, it is only necessary to point out that the terms so used involve a colloquial, not a scientific, use of language. All economists agree upon the mutually exclusive meaning of the terms, rent, interest and wages, as returns, respectively, for use of land, capital and labor,—to confuse which is to lead reasoning on the subject astray. Rent is not interest, because interest is return solely to capital,—and capital is wealth used in production. Land, again, is not wealth, because wealth is the creation of Labor and Capital, and no land was ever produced by Labor and Capital. Rent paid to a site owner for the privilege

of using a site is productive of nothing; what one party gains this way, the other party loses. This, certainly, is in direct violation of sound business principles; it fits perfectly into the ethics of poker, but men do not have to play poker, as they have to use land, to live.

#### SACRED RIGHTS

We hear much of the sacred rights of property. These rights are sacred and should be defended at all costs. Surely, men have a right to the things they produce, or obtain in exchange for things they produce. But these rights are no longer regarded as sacred, nor are they defended. All private wealth is subject to tribute through taxation. From his sacred private property the citizen pays taxes on buildings, automobiles, gasoline, incomes, inheritances, tangibles and intangibles of all sorts; he pays taxes on corporations, on his business, trade or profession, by way of tariff rates, excises, and a variety of fines, and, as the Washington State tax list has it,—after naming 155 separate items,—on “all other items of personal property”. Shortly, he is likely to feel the burden of a general sales tax on everything he buys; be he wholesaler, retailer or consumer, his tax bill will be obscurely pyramided with each separate transaction.

#### TAXES NOT CALCULABLE

It would be absurd to contend that any individual — tax assessors themselves included — is able to calculate what anyone pays for support of government. There is no principle of taxation anywhere in force upon which he could base a calculation. Did he think he had found one, a change of population by births, by deaths or migration, would upset it, if the next session of legislature or town council did not.

#### TAX IGNORANCE

From inquiries, the committee has reason to feel that the average building owner, along with the rest of American business men — among whom is to be numbered the architect — lives and conducts his affairs in profound ignorance of the amount of his contribution to the City, or State, in which he lives, to say nothing of that to the Nation. In the case of rent he knows definitely the amount he pays, and should be able to form an intelligent judgment of the value to him of what he gets in return; but in the case of taxes he can only guess, and knowing that he does not know, throws up his hands, calls taxation an unknowable subject and lets it go at that, making no effort to fathom it, simple as it may be.

#### IGNORED FACTOR

It is curious, that during the "late" depression, in fifty or more explanations of the never-to-be-halted "business cycle", not once were the economic factors, land and rent, mentioned by writers and speakers accepted as authorities in fields of commerce, manufacture, transportation, business and government finance, sociology, economics, statesmanship and the church. It were as if land did not exist, as if Labor and Capital could produce wealth without access to land. The effective trajectory of a shell could as accurately be calculated, were either its weight, velocity or direction ignored.

#### RENT AND BUSINESS PRINCIPLES

The committee has been led to wonder that this unbusinesslike payment of both rent and taxes should be allowed to continue. It would not violate sound business principles, were the building owner to make his full contribution to expenses of government in his rent, and to refuse, by legislative act, longer to pay tax-

es. He employs this very principle with respect to his own tenants. He does not charge them fares for rides in the elevators of his building, calculated upon "ability-to-pay", or upon the cost or amount of their office furniture; indeed, not,—rentals customarily cover charges for all building services whatsoever.

#### BUSINESS BLINDNESS

Upon reflection, the committee is surprised that the average building owner is content, year after year, to acquiesce in payment of both rent and taxes, when it is clear that it is to supply the community with the very things for which he pays rent that he pays taxes. He is hardly so generous, knowingly, as to pay twice for the same things, yet that is what he does when he pays with his taxes for making public improvements, and pays for use of them in his rent. But, he does not see this. He does not see the significance of the circumstance that, except in unusual instances, he complains little about rent, but does complain, constantly and vociferously, about taxes; or, of the fact, that while he decides the amount of rent he will pay, others decide the amount of taxes he shall pay.

#### BLINDNESS OF ARCHITECTS

No less blind do architects seem to the consequences to architecture, of this violation of sound business principles. Rent is fixed by competition between possible site users. A prospective building owner cannot effect savings in connection with rent. He can, however, and usually does, effect savings, both in the first cost of his building, and thereby in his annual tax bill, by making it as cheap as possible and still escape the risk of losing tenants of the class desired. To do so, he will resort to every legal skimping of space, light and air, to curtailment of every refinement, and

so endanger peoples' lives by flimsy construction, that, in self defense, cities impose building ordinances so detailed in character as to hamper the genius of the architect, and make him sometimes a subservient inventor of secret economies in violation of ordinances, that his client's building can be built for the money available, and he himself win a commission.

#### ART APPRECIATION

Pride, or some personal satisfaction, sometimes persuades a building owner to build better than he must, but as a "business proposition" he seldom does. In the circumstances, to complain of his niggardliness, or of his lack of "art appreciation", because he cuts the cost of his building, is unreasonable. He knows that the cost of every betterment will add to his annual tax bill, and reduce by that much his hoped-for profits. His tax becomes an annual penalty for building well,—indeed, for building at all.

#### TAX PENALTIES

Tax penalties for building well or otherwise, foster production of cheap, so-called taxpaying, or investment, buildings, and retard a natural improvement in architecture. Site owners themselves do not care what kind of buildings go up on their sites. What incentive to build, or to build well, is to be found in these conditions? Why should architects wonder at their lack of employment upon 80 percent of buildings—or 50 percent of the \$9,500,000,000 constituting their value,—built every year in this country without their services? How should they, when the very excellencies of plan and design they achieve but add to the tax load of the building owner?

#### TAX PAYERS

Where, to simplify matters, site owner and building owner are re-

garded as separate parties, it is evident that the building owner and his tenants actually pay all taxes levied against both building and site. There is no wealth produced at that location from which they could be paid; save that which comes from their own wages and interest. An unoccupied site does not produce wealth,—it affords, merely, an opportunity to do so. From their combined wealth, therefore, the building owner pays taxes levied on the building, while those levied on the site he turns over to the site owner, who simply does, or should, pass them on to the government.

#### SPECULATION

Where a site is bought for speculation, tax payments plus purchase price are the cost of opportunity to gamble. They constitute a bet that population will increase, that those engaged in business will need the site, that people will pay taxes to provide public improvements needed by them, — taxes which add nothing to their incomes but must become a charge against all they do or save, yet add value to the site. If he wins, the speculator will recoup both purchase price and tax payments, with interest, in higher selling price or rent, while users will foot the bills. If he loses, he must pay them from his own wealth, because an unused site produces no wealth from which to pay them.

#### GOOD SPORT

A good sport does not cry over the outcome of the risk he takes, and ask those from whom he would have taken winnings, that they restore him his losses, even in part, and others should not be allowed to do so successfully. That, however, is what real estate interests are now asking in seeking reduction, or elimination, of site taxes,—a tax juggling that

will increase winnings and lessen losses of speculation. It will encourage withholding sites from use, which is one kind of "hoarding" that escapes censure, although it enforces an unwilling hoarding of capital that otherwise would be expended in building. It, also, will increase the burden of taxation borne by buildings.

#### EXTENSION OF CITIES

A corollary of this unbusinesslike practice is found in necessary extension of cities far beyond essential requirements of population, to provide sites for those who would use them. In 1923, sub-division engineers in Los Angeles reported that 53 out of every 100 plotted lots were vacant, while, in 1929, according to the Illinois Tax Commission, nearly half the lots in Chicago were unimproved. Vacant sites augment the inconveniences, the inefficiency, and the cost of business and living, due to loss of time of citizens, and wear and tear of vehicles, passing these idle areas. They require increase, and lessen effectiveness, of police and fire forces, while unkempt sites work destruction of aesthetic and property values.

#### SPECULATION LOSSES

The committee found no data by which to estimate losses due to this evil, but they must be enormous, adding their weight to the crushing load of taxes industry must bear. Were public benefits paid for in rent, and were taxes abolished, an immense sum (variously estimated, per annum, at from 9½ to 13½ billions) would be available for productive purposes. That a large part of it would be expended in buildings, there can be no doubt; more, in fact, than the proportion now devoted to it. Since rent paid for use of sites is commensurate with accessibility to them of public benefits, it is clear that with buildings tax exempt, all

building owners would start even in the race for tenants; to win in competition with others, a prospective building owner would be obliged to build a better building. Indeed, since rent is payment for the kind of government and public improvements anywhere to be had — which add nothing to the value of buildings, but only to that of sites,—it is evident that to pay twice for these benefits makes building less probable, and good building more difficult.

#### CITY BUILDING

The committee observes, also, the destructive effects of taxation upon the execution of city, town and regional plans. It is not to be denied that parts of many excellent, comprehensive plans — altogether many and immense projects—have been executed, which have aroused popular interest in civic betterments, and have elevated public taste in city building. But, considering the time and money spent during the past forty years by plans commissions, city committees, professional organizations, engineers, city planners and architects,—the voluminous literature emanating from every branch of the press, and the many speakers engaged in “educating the public” on the subject, — the meager, compromised achievements, in proportion to populations and areas in this country, should shock the intelligence of architects.

#### WHAT HAPPENS

So long as tax funds pay for public improvements, and rent paid for their use is given away as the prize to be won by lucky site owners (who, a decade ago were reckoned as only one in 535 of the population) the idea that universally distributed benefits can come from present unbusinesslike methods, is mistaken. Affected site owners, naturally, will

fight for or against every proposed betterment. Their strifes may be followed in the press, in battles in city councils, state legislatures and the courts, in revealed or suspected bribery, while the public waits, often for years, for improvements desperately needed. Chicago was twenty-five years bringing Michigan Avenue to its present state, while neighboring streets have remained in rotten condition, and a like disorder has extended in all directions faster than any accepted method of correction could be applied. In varying degrees, the same thing is happening to every city, town and wayside in this country.

#### STREET CONGESTION

The committee noted another blindness to cause and effect, in connection with problems of street congestion, which were discussed before the convention a few years ago. It was seriously proposed to build more skyscrapers to control it; to regiment the lives of people who had to occupy them, to come and go at different times, even through the entire twenty-four hours,—indeed, to have them work and live in the same building and never, presumably, to come out on the street. And this, in truth, is the logical outcome. If private appropriation of community created values is to remain legal, people must live, move and have their being, not in ways that serve them best, but in whatever ways may be necessary to satisfy beneficiaries of that system.

#### EFFECTS OF SKYSCRAPERS

It is plain that a skyscraper tends to cause an influx of people to its neighborhood; that this increases the value of all sites therein; that this means an increase of site rents, which calls forth greater buildings, and higher rentals from tenants to pay these rents. These in turn bring an-

other influx of people, increased site values, higher rents, greater buildings and higher rentals, ad infinitum. That reasonable bounds are finally over-stepped does not alter the tendency nor the consequences.

#### PIONEER SKYSCRAPER

The effect of this process upon the pioneer skyscraper is to increase, from time to time, the rent it must produce by the only means available, that is, an increase of rentals from tenants, despite deterioration of the building from the day it was finished. Finally, so beaten in competition with greater buildings, it must give place to another, of capacity to yield rentals sufficient to make the increased double payment of rent and taxes possible.

#### UNBIASED CITIZEN AND SITE OWNER

Unbiased citizens, the committee observes, want street congestion done away with, — it impedes traffic, wastes time, makes for noise, dirt and confusion, — but site owners want more congestion. They rejoice over every new building, especially if it be big, in the neighborhood of their sites. They know that in proportion to numbers who frequent their neighborhoods, they can increase site rents; they can exact from building owners and tenants, all above what their labor and capital are accustomed to yield them; average prices of commodities, therefore, through any extended period of time, cannot come down. In the circumstances, site owners are not likely to favor plans to lessen, or to prevent, congestion,—it is their only hope of enlarging their gains.

#### CATASTROPHE OF 1929

Periodic vacating of buildings and decline of rentals should not too hastily be seized upon as evidence of decline of true site values and rents.

They are evidence of decline of asking prices of over-ambitious speculators. To architects who were observant of what was happening a year or two before the catastrophe of 1929, the acceleration in the rise of site prices and rents was the outstanding phenomenon. It forshadowed the climax. Prospective builders ceased to complain of 10 to 25 percent increase of wages, or of two to five points rise in interest rates, but began to complain of prohibitive 100, 200, 500 percent rise in site prices and rents. Strange to say, these prices were hailed by the press as signs of progress—of great and continuing prosperity.

#### BUSINESS CYCLE

When payment of both rent and taxes had so drained the pockets of industry that nothing was left with which to pay wages and interest, production ceased, unemployment and reduced consumption ensued, leaving warehouses glutted with goods people could do without, or had not the means to buy. Building was curtailed thereby, which meant that for every disappointed promoter, a contractor lost a job, some dealer an order for lumber, cement, brick, glass, and the many other things that go into a building; for workmen there was a building less upon which to seek employment, while on 20 percent of such enterprises some architect lost a commission.

Unemployable capital and saved wages filled the banks for want of locations where, after twofold payment of rent and taxes, profit could be had on labor and capital invested there. With this natural opportunity for employment of capital closed, it was put into stocks and bonds,—demands for such "securities" ran prices to absurd heights which could end in nothing short of complete collapse.

Then, the state we are in became manifest. Thousands of vacant sites held for speculative advances, and thousands of home-sites, were thrown on the market for whatever they would bring, to pay living expenses. In Detroit, last year, 134,000 such sites were reported to have been surrendered for tax sales. Vacancies in buildings multiplied and rentals declined until even hope of restoring inflated prices, and rents based thereon, vanished.

These sites naturally fell into the hands of those able to pay carrying charges, and to wait, until desperate need should drive wages and interest down in competition for the mere making of a living. So strong is this impulse, that men habitually pay a large part of the wealth they produce, for the mere privilege of retaining enough of it to live on. When this process has completely washed out speculative prices, and those having capital can figure wages and interest for themselves after rent and taxes are paid for site use, architects,—and business men generally,—may expect a gradual renewal of their activities.

#### CONCLUSIONS

The committee regrets that time does not permit submission to the convention of particular illustrations of effects of laws governing rent and taxes upon the practice of the profession. They would, however, tend simply to strengthen the view that, if natural and healthy improvement in architecture is to come, double payment of rent and taxes must cease; a legal stop must be made to private appropriation of public values, and public confiscation of private wealth; the public's rent must be used for public purposes, and private wealth left inviolate for private purposes; rent must be collected for govern-

ment revenue, and all taxation of whatsoever sort must be abolished.

#### RECOMMENDATIONS

The committee recommends that study of the subject considered in this report be pursued, with a view to verifying, or contraverting, conclusions herein set forth. Also, that a continuing committee be authorized to note the trend, and rate of variation, of site prices, rents, wages and interest, throughout the entire period of the ensuing "business cycle", and to report upon conclusions these phenomena suggest, that, if possible, the American Institute of Architects may be prepared to take an intelligent part, when the time comes, in preventing recurrence of the inactivity now being experienced in the building industry and the architectural profession.

Respectfully submitted,

#### THE COMMITTEE:

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