Property Tax Relief Measures:
Answers to the "Poor Widow" Argument

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Introduction

Rising property taxes, it is often alleged, are driving people out of their homes. While parcels rise steeply in market value, and hence their assessed value, household incomes often increase only moderately, the result being that the burden of paying taxes for the support of municipal services and schools is deemed to be both onerous and unfair. Allusion is typically made to the "poor widow"[1] who, on a fixed income of a pension and/or social security is compelled to sell her home in which she lived for years and where she hoped to spend her remaining days.[2] Although pundits and politicians are often hard put to provide an instance in which this has happened, it makes for excellent copy, for what greater case of heartlessness can be offered for relief of property taxes! The National Conference of State Legislatures (NCSL) begins its 2002 Report[3] on Property Tax Relief for low income and elderly households by stating, "older Americans frequently live on fixed incomes and own their homes. [Therefore] in retirement the ratio of property wealth to income tends to rise as income falls, so the burden of property tax increases."

In truth, real property values, and hence taxes where assessments have been kept abreast, do cause households to feel an increased burden when contrasted with alternate tax regimes such as those on sales and income. But those other taxes also have their downsides. This paper is an examination of various solutions that have been proposed, even while maintaining the tax on real property. NCSL identifies four measures typically employed as a solution to the "poor widow" dilemma: property tax caps, the homestead exemption, the circuit-breaker program, and the deferral program. All are widely enough employed among the fifty states and the District of Columbia that clear lessons should be apparent upon examination. It appears, however, that no efforts have been made to do comparative analysis of their merits and liabilities or successes and failures; rather the studies that exist are for the most part statistical and enumerative. Studies are difficult because relief measures have been changing so frequently. The data on property values, tax formulas, thresholds and relief measures cannot keep up with continually changing economies of which they are apart.[4]

Because political demand for adjustments has become so frequent, this discussion does not pretend to be up to date in its tabulation of various state programs. It is directed more toward discussion of the administrative, economic, and moral issues inherent in their designs. It is intended rather to be an analysis and evaluation of such relief measures, and secondly to show how policies can be instituted that will accord with both the political demands for mitigation and the widely held principles of sound tax theory.[5]

Problems with the Conventional Real Property Tax

Modification of the real property tax as it now exists is difficult because it is fundamentally flawed at its base. Several polls show that it is the most reviled of all tax regimes,[6] and much of the criticism is warranted. This stems as much from its poor administration as from the conceptual design of the tax itself, but these flaws can be remedied with better understanding. With only slight modification and better management, this tax could be the most perfect tax of all.[7] Presently, however, it violates all the principles of sound tax theory enumerated since Adam Smith.[8] The property tax, as it now exists, violates

- the principle of neutrality, because it influences and alters decisions from what would occur in its absence;
- the principle of efficiency, to the extent that it, as well as other taxes, reduces market performance and economies by the "deadweight loss" it generates;
- the principles of horizontal and vertical equity: those in similar circumstances don't typically bear comparable obligations, nor are those in different circumstances treated in a uniformly commensurate way;
- the principle of administrability, insofar as its management is likely to be quickly affected by external forces, and because maintaining adequate and reliable records is so costly;
- the principle of simplicity, which leads to misunderstanding and opaque application, with the consequent loss of its legitimacy; and
- the principle of stability, which requires it to be continually jiggered and otherwise modified to provide adequate revenue on which governments depend.

Inherent in these downside effects is the distortion of locational decisions so that land use configurations do not unfold in optimal ways and lead those who must make such choices to second best alternatives. The tax creates centrifugal forces that foster sprawl development and lead urban cores to be underused and neglected.[9] It leads further to the adoption of costly public incentives to negate these tendencies, thus requiring measures that favor select constituencies and thereby raise the tax burdens on others to pay for them.

These liabilities' only saving grace, goes the argument, is that alternative revenue designs suffer from even more egregious flaws. Many tax designers maintain that all taxes have their defects, and we must therefore rely upon several revenue streams to ensure and stabilize support for public services. I have elsewhere challenged this claim, and I urge us to scrutinize the property tax more closely both in its dynamics and its impact.[10] If we are to fix the problems inherent in our tax structure, the property tax as well as others, we have to look at the economy systemically, not with *ad hoc* patchwork remedies as crises arise. The biggest problem stems from the belief that the economy would operate with maximum efficiency and productivity if only taxes didn't exert a leaden influence. In fact this is not true, because it is not taxes themselves that impose a drag and burden, but certain kinds of taxes, along with what classical economists call

rents. As with most other taxes, there is a close relationship between aspects of the real property tax and economic rent, suggesting that the best solution to restoring harmony to economic systems and approach optimal market exchanges is by removing the rent, wherever it may flow or come to rest. It is economic rent that figuratively "gums up the works," but which would allow markets to perform far more smoothly if it were completely removed by taxing it away.[11]

The Real Property Tax as a General Design

Understanding the real property tax is peculiarly difficult because its complexity and dynamics confound our conventional ideas about property, and is therefore typically underestimated. The most profound misunderstanding about real property stems from its misapprehension as an object, or as a "thing" similar to a car, a house, or a refrigerator. Some part of the tax is indeed imposed on "things," the part we call "improvements." That is actually the easiest component to understand. But the tax on improvements is both administratively and economically inefficient. So, for this among other reasons, many tax experts argue for placing the tax on the other component alone, the part on land, which is really the value of locations, and which is due to the presence of rent. This can be understood easily by considering the value as a site, ignoring any "earth" qualities. I prepared testimony for the Assembly Real Property Tax Committee on the challenges of assessment, and don't need to repeat that here.[12] Suffice it to say that assessment of land values is far easier to do than for the value of structures.

Yet one can understand why both land and improvements as bases for taxation should have come to be viewed *in rem*, (i.e., as things as opposed to being *in personam*, the other commonly understood base of taxes); after all, both have a solid form and a tangible quality that would appear for all practical purposes to be alike. To some observers, taxing real estate is the final and vestigial instance of the practice of taxing tangible objects, a practice that should be eliminated entirely along with the decreasing reliance upon *ad valorem* taxation of personal property. They would prefer to tax income, which is viewed as commensurate with one’s ability to pay. As noted, however, the land component of real property needs to be appreciated not as a "thing," but rather as a locational site, distinct from improvements that may attach to it. This gives land locations attributes that differ fundamentally from any objects that may attach to them. Rent, as linked to locations, constitutes an entirely separate and different potential base of taxation than does income as reflective of wage labor, or the value of things, which are capital.

Contemporary economic theory is not helpful in presenting a third base on which taxes can be built. This is because one needs to go back to 19th century classical economics (as opposed to the contemporary neoclassical school) to appreciate the significance of what was then called economic rent.[13] Rent is somewhat analogous to water, which flows through parcel sites, and in no way “resides” in the sites themselves. Furthermore, rent is reflective of the enterprise of a community as a whole rather than due to the efforts of any single titleholder. Better, therefore, that property parcels be understood not as the repository of value but rather as the *loci* through which value flows.

Rent constitutes one attribute among many that characterizes and reflects the value of real property. It helps that property law abjures use of the word "ownership" in preference to the term "bundle of rights" which refers to the privileges that attach to locations as they are defined.[14] Typically enumerated among the several rights that are linked to titles are the rights to sell, to mortgage, to bequeath, to lease, to use and occupy, to alter and install, and to subdivide and develop. The right to the retention of the ground rent is overlooked because its understanding is an artifact of classical economic theory. Market prices really attend to those privileges as they relate to the various uses to which sites can be employed, all of which create rent. To discuss this further would take us far afield of the concern of this paper, but is worth at least note in passing.

The critical component of the real property tax, the part that should ideally bear the burden, and indeed the part that actually improves the performance of the economy, is the tax on land sites according to their market value. A properly administered land value tax, as noted above, comports with all the textbook principles of sound tax theory, and indeed deserves the attention and understanding of students of fiscal policy far more than has been true in recent years. The market value of sites reflects the community enterprise of neighborhood communities and whole regions, and derives not from what any single titleholder does but rather from the economic vitality of the society generally. The flow of economic value, which is labeled rent, was understood well by classical economists as far back as Adam Smith,[15] and was given increasing clarity over the next century by Malthus, Ricardo, Mill, and Marshall. More than anyone, however, it was Henry George who constructed a comprehensive political and economic philosophy based upon the existence of rent that flowed through locations and reflected the level of market activity that those sites held.[16]

Rent, as a flow of economic value, is fundamental to an understanding of the market value of land sites. Absent a full understanding of rent, sometimes also called ground rent, site rent, or economic rent (to distinguish it from the contemporary vernacular use of the word), leads to confusion and misapplication of tax designs, and the consequent controversies that ensue in this regard. Attempts to design tax regimes that take into account not only the requirements of public funding but the vicissitudes of the economy and the circumstances of individual property owners has led to a succession of Jerry-built "Rube Goldberg" systems that invite criticism, and usually quickly fail on account of their inability to contend with changing times. Enumerating the ways that forces interplay between changing economic situations and formulas cast in fixed form allows one to visualize the problems inherent in current designs.

The first consideration in how multiple variables affect property taxation is the condition of the economy itself. The most easily identifiable impact on property value at any given time is the vitality and exuberance of the economy. Areas where activity is booming will have higher property values than those areas that are in the doldrums. The east and west coasts of the US have far higher property values than many locations interior, not just on account of the limitations of space on sites proximate to coasts and ports but on account of the manifold economies that feed the markets of those areas. New York City and its environs have been booming for the past two decades, in good

part due to the activity of the financial markets but due also to the other ancillary industries and other amenities that attract people. Where people want to be, site values are higher. Upstate New York State, on the other hand, has been dying for decades, because most of the industries that served to enrich that region for decades have moved or been made obsolete by a changing economy. It has yet to recover.

Moreover, it has become an article of faith that economies have periodic cycles, and that these phases are reflected more in property values than in any other sector. As this is written, observers are talking about a "bubble" in real estate values that may this time perhaps be more profound than any since the 1930s. Laws enacted to collect revenue from real property taxation are usually unable to accommodate to the rises, falls, and shifts in economic circumstances. In some instances, this is a virtue. Because the property tax is levied using an *ad valorem* formula (tax base times tax rate), however, it often fails more than other tax regimes to take into account changing factors and needs. This is not to say that doing so is administratively impossible; it is to recognize, only, that doing so is costly, and inadequate understanding of its nature leads inevitably to manifold problems.

A second important perspective comes from the significance mentioned earlier that the real property tax is really two separate taxes -- a tax on the value of landsites and a tax on the value of improvements. The improvements, as noted, typically depreciate in market value over time, even as the land values appreciate. For this reason, assessors are usually required by law to valuate land and improvements separately. Yet when governments fail to update the market value of property parcels frequently and regularly, disparities between actual market prices and assessed values quickly result. In any given area, even at a local level, distortions from one neighborhood to another eventuate with the consequence of shifting burdens. Comparability of parcels is often difficult, especially when judgments about the separate assignments of value to land and building components must be estimated. This becomes even more difficult for the assessment of property parcels that cannot be compared with market sales: residential parcels have a far more frequent turnover than non-residential parcels; as a consequence the standards for the latter are far more relaxed.[17]

This leads to still another consideration affecting valuation: the importance of timeliness in assessments. Some localities have been known not to carry out revaluation of their parcels on a comprehensive basis for decades, with all the distortions and loss of faith in their soundness that this entails. The state of Maryland has removed responsibility from local governments entirely, and placed the charge with professional state agency officials. Its office conducts revaluation for one third of all its counties each year so that no parcel has a valuation more than three years old. In fact modern computer technology has the potential for referring sales data over to assessment rolls and using formulas that could maintain a running valuation of every property parcel on a real-time basis. Instant reference to the market value of any and all parcels in any area would lead to the restoration of sounder valuation as well as greater assessment legitimacy.

Because one component of a real property parcel is continually depreciating while

the other is likely appreciating, it becomes a challenge to know what proportion of the market value to assign to each factor.[18] There are strong incentives, particularly given conventional political pressures especially by non-residential interests, to over-value the improvements and undervalue the land components. This advantages titleholders for purposes of bookkeeping and tax write-offs, even while it distorts comprehensive market forces and assessments.[19] Again, computer technology has the potential to overcome such abuses, but has been underused to date.

These above-mentioned factors are considerations that lead to questionable validity of valuations of real property at local government levels. It means that there will be unfairness and disparities from place to place, from time to time, and from titleholder to titleholder. Because so many state formulas feed into and are based on local assessments, the distortions are amplified when state school aid formulas, housing assistance, highway decisions, health policies, welfare aid, and other such instruments are implemented. The criticism of the real property tax stems as much from its poor administration as from lack of understanding of its design. But one should emphasize that these are technical and administrative problems and not at all inherent in the economics or design of the tax itself. Treatment of these concerns is addressed later.

The most important insight needed to appreciate how the real property tax works – at least for the land component – is the reciprocal relationship between the market value of land locations and the taxation of the economic rent that flows through those sites. The more the rent on land is taxed, the more stabilized the price of locations becomes; failure to recapture the socially created rent from land sites inflates the market price of sites and bidding up their purchase level to form distortionary bubbles in the whole economy. One way or another, rent streams flow through locations, to be linked to sites or to be collected in taxes. Leaving the rent untaxed allows it to be capitalized in the market price until it is ultimately apparent in a sale.

It should be emphasized again that leaving the economic rent to pass through locations raises their market price. So when titleholders ultimately cash out they reap the benefits of a windfall gain. As a corollary, the increase in market value of sites is subsequently reflected in higher assessments (if reappraisals are kept current), and, of course, in still higher tax levies. So it is that titleholders face the challenge of paying their property taxes on a regular schedule, even though they often don't experience the capital gain until later. The normal and expected return to owners is viewed as a sound investment payoff when property is sold, but meanwhile paying taxes evinces lots of "crocodile tears." This is not to deny that property owners, especially households, may experience stress when facing a large tax bill. Sympathy arises particularly for retired and elderly homeowners, who likely have substantially decreased income, just when home values, and hence taxes, jump. This dilemma, however, reflects simply a cash flow problem; no genuine loss of ability to pay the amounts due. There are available answers to this situation, and easily implemented.

Special Adjustments Applied to the General Design

Beyond the frequent criticism directed at the application of the property tax is the charge that the property tax is inherently unfair because it shows no relationship to the income of households and titleholders, and that it taxes people with comparable parcels differently. These complaints arise with little understanding of the factors that assessors take into account when making valuations, and show even further misunderstanding about ideas of fairness. Tax equity is usually measured by one of two criteria: on ability to pay or amount of use. Property tax revenues the public pays for use are sometimes referred to as "user fees," not taxes. But this is a distinction without a difference, because a tax that relates to the value of a location corresponds closely to community services rendered and is an ideal user fee.[20] Therefore the rent that flows through sites is a precise measure of its use value. Explaining this logic would allay many of the criticisms on the land component of the tax. But land value taxation is too little known or used in American states, despite its wide application elsewhere.

The assumption underlying all property tax relief is that homeownership constitutes a public good. It fosters family integrity and stability, facilitates a more active and involved citizenry, promotes activity and growth of the economy, and provides financial equity and security in a relatively innocuous and automatic way. More than any other element, it is the bulwark of the consumer economy, which is regarded as an unmitigated good. Housing is used as the bellwether measure of economic health.[21]

On the other hand, it entails an element of economic 'lock-in' that reduces the liquidity of capital and the mobility of populations, thereby distorting economically efficient use of housing as well as land use configurations.[22] It is just one more reason why the real estate market is far from having perfect competition. Inefficiencies abound, such as the way young growing families are denied the full availability of homeownership while empty nesters and elderly widows continue living in homes far larger than they really need or can use. An inordinately high proportion of earnings are dedicated to homeownership, land use configurations grow out of sub-optimal location choices, greater automobile dependency results, and a number of related disamenities make for distorted markets in site locations. Pundits note significant numbers of households have no adequate housing at all while a sizeable number have two and even three homes. Arguably there is as much unfairness imposed by these relief measures as there are instances of their alleviation.

Hardships that arise are then remediated on a patchwork basis. Special consideration is usually granted to primary homeowners who are elderly, disabled, veterans, low income, or who secure special privileges. The benefits and relief accorded are explained as much by special pleading as they are by justice and demonstrable need. Every state has at least one such modification of the basic property tax design, and most have more. Variously, the property tax burden is relieved for selected parties by methods like

- exemptions or deductions for those below certain poverty income lines,

- exemptions from the assessed values or from tax burdens due, and
- formulas for limiting the assessments or tax rates.

When such tax breaks are offered, sometimes by automatic eligibility, sometimes after special application procedure, states may then reimburse the local governments for revenue foregone. Some measures of this order are applied across the board and some are at the option of local governments. After giving relief to owners of residential property, one frequently then sees differential tax rates applied to non-residential property to induce economic revitalization there too. The result is a hodgepodge of measures that are as contradictory in their impact as they are ineffective.

The eligibility for such relief varies greatly. In fact the fifty states' ways of relieving aggrieved parties of treatment adjudged to be unfair differ so much that it is hard to compare these programs in any organized way. The NCSL study has constructed several tables of summary descriptions. But none of these tables and framework arrays can capture the variety of solutions and the permutations employed to adjust tax burdens. Nor is likely that they can or will be. The complexity of factors determining property value is beyond the anything snapshots can capture, and so are the remedies that are instituted in response.

The National Conference of State Legislatures identifies four measures typically employed as a solution to what is typically known as the "poor widow" dilemma: property tax caps, the homestead exemption, the circuit-breaker program, and the deferral program. At least half the states now employ one or another of the aforementioned provisions; several employ all of them. These measures of relief for financial hardship were initially envisioned for households with low income, or for those with special and extraordinary expenses like the blind and handicapped. But, politics being what it is, the relief has often been extended to reward preferred titleholders like veterans and clergy.

Property Tax Caps

The most simplistic measure devised to limit property tax burdens has been the use of caps on assessments, on rates, or on both. The most notable was California's Proposition 13, passed in 1978, and followed by measures in Massachusetts, Wisconsin, Oregon, Florida, and other states. Thirteen others have frozen assessments just for elderly households.[23] Counties in California are instructed by state law to revalue parcel only when ownership changes hands; otherwise any rise in assessed value is the lesser of 2% or the increase in cost of living. This means that some homes have not been revalued since 1978; and adjacent parcels can bear widely different tax burdens, thereby invalidating any hope of achieving equity. Because this was presented to the voters as a ballot initiative, there was no prior research and no legislative hearings for a measure with such profound consequences. Moreover, it was presented as an amendment to the California Constitution, which makes it now very difficult to alter, despite its limitations.

The greatest beneficiaries of this tax revolt were parcels that change hands infrequently, mostly non-residential properties, especially large businesses and industries.

Because the state is so large and because property values vary so widely, the cost of owning a home, especially in the coastal areas has skyrocketed. The greater the disparity between property taxes and the economic vitality of an area, the more the property values widened. The ceilings imposed have led to a shift of tax burdens to the state level, while at the same time starving many public services and programs of support. It is fair to say that no other single tax measure has so disrupted the performance of government as has Proposition 13.[24] For the moment, however, it remains the "third rail" of political discourse, and there have been no efforts to challenge its position.

The impact of Proposition 13's passage reverberated throughout the nation when it was passed, and other state efforts were initiated before too long. The next successful enactment, also by ballot initiative (although not a constitutional amendment) was in Massachusetts. The name of the initiative, Proposition 2 1/2, came from the assessment adjustments it imposed on all taxable property in a municipality. It stipulated that no property tax rate could exceed 2 1/2 percent of the assessed value of a parcel, and that no increase could be more than 2 1/2 percent in any one year. The tax applied to residential, commercial, and industrial parcels, as well as to the motor vehicle excise tax, and has been in effect since 1982. Five states now limit the growth in property tax revenues to no more than 3% annually: Arizona, Idaho, Massachusetts, Washington, and West Virginia.[25]

Other states' designs arise from similar sentiments. Measures to freeze property taxes take one of three forms: a freeze or annual ceiling on the increase of the assessed value of property parcels or a freeze on the mill rate of a tax, or both. A freeze on assessed values makes the whole valuation program essentially worthless; markets continue to operate and property taxes then remain fixed at whatever last point they were set at prior to the freeze, even if sometimes annually adjusted by a fixed percentage. A cap on the tax rate, regardless of background inflation rates or surrounding economic climate, leaves the land rent to flow through locations in ways that boosts their market price. As time goes on the injustices and differential economic permutations create even greater distortions in the tax regime. The result of such mischief is also to distort real estate markets, for taxes are never sufficient to brake values. Whatever inflation or surplus not otherwise captured by taxes is ultimately reflected in market prices. Failure to stabilize property prices results in higher site values and a greater gulf between the tax bases and actual aggregate real market values.

It is again appropriate to note the reciprocal relationship between the market value of locational sites and the amount of economic rent recaptured in taxes. Rent flows through a region in relationship to the vitality of economic activity, and taxes either recover that socially created rent or else leave it to affect the market value of sites. Leaving aside the questions of whether assessments are performed in a sound and timely manner, capping the taxes simply leaves rent in place to raise prices, thereby further increasing the assessed value when it is eventually recognized. Capping taxes actually exacerbates the problem: by allowing or ignoring the continual accretion of rent, it raises market prices far beyond what the normal recovery of rent in taxes would dictate. Arizona imposes a property tax cap of 1 percent on residential parcels, which of course

has sent home prices through the roof during the recent real estate bubble.[26] Many California communities today have experienced such enormous growth in real estate values that they are no longer competitive in attracting business, and are so out of proportion to reality that they sit at the top of the real estate bubble, until of course, it collapses.[27] Speculation feeds the process further until supply and demand finally offer the inevitable corrective.

The Homestead Exemption and Credit

As normally designed, a homestead exemption subtracts a specified amount from total property taxes due. This can be accomplished by subtracting a stipulated base amount from the assessed value of a parcel or from the tax bill itself. About half the states impose an upper income limit on eligibility; the District of Columbia, the highest, links to a household's adjusted gross income of up to $100,000. There are also instances where the taxes are applied as a credit against state income taxes instead of as a deduction (as is normally the case). Sometimes the tax applies only to municipal taxes; in other instances to school taxes as well (which are often levied separately). There are even instances where localities are reimbursed, totally or in part, from revenue foregone by state funding sources.

The most recent available (2002) count reveals that a total of 48 states and the District of Columbia allow homestead exemptions or credits of one sort or another.[28] A few states make eligible only narrow groups like veterans and the disabled, and some states allow localities to employ homestead relief as an option rather than offer it as a statewide program. Some 32 states allow some level of exemptions for homeowners of all ages, and with a ceiling set by income level. The remainder, most often, employ the provision for the elderly, with the threshold set at age 65. The age threshold can be as low as 61 (Washington) and as high as 70 (Massachusetts). Hawaii is unique in having both a phased-in age schedule and a sliding exemption. In most instances, enrollment is automatic, so that the benefit of tax relief is granted as a matter of course. There are instances, however, where qualifying homeowners must apply to obtain their benefit, or else to fill out income tax forms that depend upon their own initiative.

Arguments for the homestead exemption programs depend very much on the assumption that assessments are up to date and accurate. But assessment standards vary widely: instead of using 'full market value' for 'highest and best use,' the professional standard, some states mandate a percentage value or some other approach. Assessors don't always rely upon economically and technically sound valuation procedures. In fact law often requires them not to do so, for example, usually by making a distinction between appraisal value and assessed value. Even when assessors perform their job satisfactorily, administrative and political considerations may then call for levying differential tax rates on one class of property parcels versus another. This relieves favored titleholders of a portion of their tax, and shifts the burden to another class or classes. Of course, political decisions instituted in favor of homeowners lead to an increased burden on commercial and industrial classes – typically employers – and are disincentives to their expansion.

To a lesser and sometimes equal extent, the same problem of assessment gimmickry, disparities and inequities exists in just about every state and locality. The value of property parcels typically differs from one part of a state to another, even though the same formula is applied throughout. If the same formula applies statewide, it should be palpably obvious that a $200,000 home in Denver itself will be far more modest than one in more remote areas of the state. Colorado's homestead exemption of 50% for the first $200,000 of actual value is applicable if the resident has lived in it for at least ten years. Moreover, the state's assessors don't use the conventional standard of 'highest and best use,' but use 'actual value' instead. This means that a location that warrants more intensive use relative to its site value will likely continue to languish as a derelict or vacant lot, with little advantage except for speculative gain. Many urban officials, prompted by pressures to induce development in moribund neighborhoods, are induced to adopt other tax incentives like enterprise zones, tax increment financing, and various subsidies, precisely what speculators wait for to happen. This leads, of course, to economic lethargy and to burden shifting to other property taxpayers. Inequities such as these result in enormous potential tax revenue foregone. The homestead exemption, however finely tuned, can never be but a blunt instrument in satisfying the requirements of a fair and efficient tax regime.[29]

New York State is unique is its homestead design, and its complexity is somewhat baffling. Localities have the option of holding constant a percentage of the gross tax yield from residential parcels relative to non-residential parcels. The provision is employed when their governments have neglected to revalue property parcels for long periods, and then, having done so, face radical jumps in the tax burden on residential parcels. According to state law, localities may, if they then wish, keep the aggregate portion levied on homeowners constant by taxing them at a lower rate than others. This is done with the intention of reverting to a phased-in single rate in due course when presumably fiscal circumstances are improved and rates can be equalized once more. But that opportune time tends to fade into the distance.

This of course puts the additional burden on non-residential property owners, businesses typically. The extra load, which can increase over time since the split is held constant and businesses often leave, puts a city on a downward spiral from which it is difficult to extricate itself. Several major cities in New York State, among them Albany, Buffalo, Binghamton, Kingston, Niagara Falls, Poughkeepsie and Rochester, as well as many smaller localities, worked themselves into this box years ago, and have now experienced the consequences.[30] Some cities have even seen their businesses raze perfectly good structures rather than be saddled with burdensome taxes. General Electric tore down some serviceable buildings in Schenectady, and Kodak recently did the same thing in Rochester, all to reduce their tax burdens.

New York State localities can adopt the homestead option for both their school taxes and their municipal taxes. Besides this provision, which affects only about twenty five of its over 900 localities, there is a second measure known as STAR: School Tax Relief program, and then both a Basic and an Enhanced STAR program to boot.

Although administrative agencies and local governments now claim to have mastered the task of dealing with this complexity, there is no indication that any analysis of the equity issues has been addressed. The Basic STAR is available to anyone who owns and lives in his or her home and whose tax burden and income fall within certain specified ranges. The Enhanced STAR program is for senior citizens with (2006) incomes under $70,650. A further program is available for New York City homeowners. To further confuse things, a 'Middle Class Star Rebate program' enacted by the Pataki administration in 2006, allows additional relief on a phased-in sliding scale for homeowners with incomes below $90,000 upstate and $120,000 in the metropolitan New York City region. As this is written, further legislative tinkering seems to be in store in order to further relieve the burden upon homeowners, which will likely add even more complexity to a design of already 'Rube Goldbergian' dimensions.[31]

The New York Homestead Relief program and these others illustrate in graphic fashion the real difficulty with all such programs. Many distinguishing failures sum up their problems with the homestead exemption:

1) it relies upon assessment data which is seldom accurate for reason of being out of date, incompetently performed, or reliant upon inappropriate standards;
2) 2) it relies on formulas that fail to keep up with those market values and assessments;
3) 3) it fails to take into account disparities in property values from one part of a state to another;
4) 4) it fails to accurately comport with any standards of fairness –either one's ability to pay or one's benefit derived;
5) 5) it shifts the burden to non-residential properties which, in some cases, may find it more onerous than households.
6) Lastly 6), it has been an administrative nightmare.

In the final analysis, the benefits provided are not nearly as generous as might first appear. Yet the homestead credit and exemption programs survive because of limited understanding of land economics and of the dynamics of the real property tax. Political leaders can claim to have "done something," and mention the typical $300 state check homeowners receive in the mail.

Property Tax Circuit-Breaker Programs for Homeowners

Circuit-breaker property tax provisions adopted by various states are explainable by the metaphor that they employ. The circuit-breaker mechanism is an automatic shut-off when an electrical circuit is overloaded. Here, a tax burden similarly shuts off, by either a credit or exemption, as it relates to both real property taxes and income. It is intended to assist low-to-moderate income homeowners and, in two cases (Alaska and Oregon), to renters. Benefits can be based on an absolute threshold or a sliding scale. As of 2006, only four states provided for circuit breakers without regard to age, using income alone as a qualification.[32] But a full 34 states have provision for circuit-breaker relief, and just about all set the eligibility threshold at age 65.[33] According to the NCSL study, benefits range widely, from a modest $125 in West Virginia to $2,000 in North

Dakota, and phase out as income rises. Relief is granted sometimes by an initial exemption, other times by a rebate from state sources. Eligibility may pertain to other assets as well; in the case of Maryland the limit is $200,000. In some instances the administration provides for a rebate depending upon when state income tax is filed; in other instances, eligibility is determined by formula set beforehand.

At last count, the range of initial eligibility phase-in runs from a low of $3,750 (single) and $5,550 (joint) income in Arizona (West Virginia is not far behind with a threshold of $5,000) to a maximum of $30,000 in the State of Washington. Maryland and Massachusetts limit the benefit by the value of the home, the latter using an assessed value ceiling of $400,000. The mean maximum benefit of all 34 states looks to be approximately $600, but the high-cost states of New York and New Jersey allow credits from a household's state income tax payment, but cap them at a mere $90 and $75 respectively. This same New York formula applied in 2006 when a median arm's length residential sale was $630,000 in Westchester County, just north of New York City, and $69,000 in Chautauqua County at the western edge of the state.[34] Minnesota and Vermont have a benefit cap of $1,500 even though differential housing costs might not be quite so dramatic. All this description simplifies what are in some cases inordinately complex formulas, making it difficult for homeowners to know and understand how fairly the burden is being imposed. When floors and ceilings of eligibility become dated, as well as assessments, whatever results from legislative compromises for fairness or advantage is lost by a lack of simplicity and transparency.

Many of the same liabilities apply to the circuit-breaker program as exist with the homestead exemptions and credits. This broad-brush formula program invokes relief without regard to relative need. Given the variability of income and home property values, it is difficult to guarantee any uniform degree of fairness even within a state. Like other measures, an extraordinarily modest benefit in one region of a state can well be an inordinately generous windfall in another. And, as earlier noted, any exemption from taxation reflected by the land component of the levy is of course capitalized in the total market value of the parcel: the market price immediately rises to the extent that this burden of taxation is relieved. Depending upon the status of the owner and without bearing upon the value of the parcel itself, this is done selectively, and it constitutes a distortion reaching far beyond the owner, the parcel, and ultimately to the neighborhood itself. Far from being neutral, it means that tax programs affect decisions about ongoing uses of sites whenever the same owners retain title.

The first circuit-breaker program was adopted in Wisconsin in 1964, and twenty-five additional states adopted programs between 1970 and 1979. It has been all but impossible to link blanket adjustments in benefits to the sporadic and haphazard attention to local revaluation of parcels. Even though localities are frequently reimbursed for tax revenue foregone, the efficiency (and fairness) of the programs is compromised by reliance upon the homeowners to initiate applications for program eligibility. Even when percentages are employed in formulas rather than fixed amounts, it becomes difficult to incorporate any semblance of equity in such a far-reaching and broadly applicable program. Where renters' eligibility qualifies, any estimates of what proportion of a

tenant's payments constitute the tax component is largely a matter of guess. The difficulty in maintaining any integrity in the circuit-breaker program is most exacerbated by the rapidity with which assessments become obsolete, inflation factors alter income, and the corresponding formulas applied to them as well. It is no accident that the benefits of the circuit breaker have dropped drastically since most of them were first instituted.

The single universal feature of circuit-breaker eligibility is a homeowner's income; it has no way of taking wealth into account. And since economic rent, left untaxed on land sites, is capitalized in a parcel's market value, it results in an unrealized capital gain to the titleholder. The result is a two-fold gift: first the exemption from payment of a share of the property taxes, second, a capitalized rent flow increase resulting in a windfall gain when ultimately a parcel is sold. The upshot is that circuit breakers provide a solution to a misdiagnosed problem. If the programs were truly transparent and the public understood their real-world applications, it would realize that they represent a diversion to appeals for relief of a genuine predicament. Still, for lack of imagination of tax designers or due to an inadequate understanding of the economic dynamics of land markets, circuit-breaker provisions have been enormously popular. Given the recent run-up of property values in various localized areas, there will likely be enormous pressure for their expansion and for their further adoption unless more adequate relief designs are put forth.

Property Tax Deferrals

With a few exceptions, most of the existing deferral programs are limited to elderly homeowners. In these uncertain times some states' leaders have come to appreciate that many other households experience setbacks, but once recovered still manage to continue their tax obligations reliably. Because such arrangements constitute a lien on a home (perhaps in addition to a mortgage), there is often some discomfort when homeowners assume such an obligation. The burdens of opting for this provision can be stringent: In Florida, the amount deferrable is only that portion of taxes exceeding 5% of the applicant's household income, and in Texas any debt outstanding carries an interest rate of 8% per year, which discourages people from using it.

The District of Columbia allows qualified owners to apply for deferral each year only if the tax on their home is in excess of 110% of the preceding year's tax. States that address their concern exclusively to the elderly are generally more lenient in their designs. Those eligible must typically be at least 65 years old (although Washington sets the threshold at 60 and California and Oregon at 62). Two states – Arizona and South Dakota – hold out the eligibility till age 70. The total amount that can be deferred also varies widely, up to $40,000 in Massachusetts, $50,000 in Virginia, and $60,000 in Minnesota. Michigan indexes its cap to inflation and Wisconsin sets its cap at 150% of poverty level.

While homeowners in eligible categories may defer payment of their tax duties, their relief is only temporary. They are deferred so that they can continue occupying their homes without any pressing concerns about tax payments. Whenever the homes are

ultimately sold or transferred, the lien, including interest, must be satisfied. In one sense (although not in others) this design functions somewhat as a 'reverse mortgage.' But the terms are typically far simpler and more generous than reverse mortgage arrangements in most instances. A total of twenty-five states and the District of Columbia now employ some system of property tax deferral. “Deferral programs,” says the NCSL study, “are the most cost effective method of alleviating the concern that elderly homeowners might lose their homes because they cannot afford taxes.” It is cost effective to both homeowners and to governments. Unfortunately records of program use are lacking, but the general impression is that it is not as widely used as might be. One can surmise that the elderly regard their home, likely their most important possession, as their financial security. They may want to pass their asset, typically accumulated over the course of a lifetime, to their heirs free from encumbrance. One can also assume that children would tend to resist the use of this relief provision as they stand to gain when a title is ultimately transferred. To them it constitutes a windfall gain, and who doesn’t enjoy a windfall!

Part of the explanation for the reluctance to employ deferral options may stem from the unwillingness, and perhaps even the inability, to appreciate the distinction between earned and unearned gains. The bald fact is that Americans have come to regard the windfall wealth of rising home value as much as an entitlement as they do earned wealth, sometimes more so. The real estate industry urges people to regard their home as an investment. Even though a lifetime depreciation of a house might reduce its value to a fraction of its replacement cost, the land appreciation typically more than compensates, and is regarded as a rightfully acquired capital gain. The distinction between structures and land values is ignored, and society and government make little effort to bring that distinction to light. We have witnessed, particularly in recent years, an enormous dependence upon unearned income by large elements of the population, and no effort is made to identify how much of this income is passed-through economic rent.[35] In reality rent is windfall income, created by the community, and ought to be understood as such, morally speaking. The increasing dependence of so much of the American population on unearned income, much of which relies on the capture of such rents, has led to the use of new economic language. People are said to live in an economy of finance capitalism, in contrast to an earlier era of industrial capitalism.

Nonetheless, one must appreciate that when one segment of the population is relieved of its tax burden, others must take responsibility for assuming it. The abstruse dimensions of other property tax relief measures fail to make clear where justice and fairness lie in the total scheme of things. With deferral owners of residential property are not relieved of their tax burden; they still shoulder it fully. They are simply given the privilege of deferring it until they move to other quarters, die, or otherwise cash out. The provision for its use also makes clear that the burden is linked not to the person of the titleholder but rather to the property parcel. This distinction is critical for its message in making clear the moral dimension of a tax regime.

It is sometimes argued that the instrument known as a “reverse mortgage” can accomplish the same thing. Recent figures show that an increasing number of seniors are making use of this option where it is allowed. One advocacy website cites the increase in

numbers since it was first authorized. US government records show that the total number of policies contracted was only 157 in FY1990, but was 107,558 in FY 2007.[36] Earlier experiences showed that exorbitant interest, points, and penalties, a matter of less concern often victimized seniors with property tax deferral instruments.[37] Perhaps the increased popularity of reverse mortgages is due to their closer government regulation.

The potentially distorting effects of property tax regimes on behavioral choices have been alluded to earlier, beyond family and parcel use itself. Whereas the homestead, circuit breaker and tax freeze programs all have profound consequences for and upon the wider community, and upon land use decisions and configurations, deferral programs in contrast are likely to have a very limited impact. Real estate prices in deferral programs still maintain the same integrity they would have absent their use. Tax burdens are still incorporated in pricing structures, much as in deferral's absence.

A final concern is the impact upon a local community's fisc. The deferral option in no way shifts the tax burden onto others or excuses an elderly homeowner from his obligation, even if payment is delayed. The arrangement is a financially neutral transaction. If a peculiarly large number of applicants were to be involved in the tax schedule at a program's inception and was onerous to a local government, there is no reason why a state might not be able to offer transitional aid. But no transition difficulty has been reported in any of the 24 states offering a program.

Uniqueness of the Real Property Tax and the Georgist Alternative

Further discussion of the pros and cons of each remedy for the “poor widow’s dilemma” requires more exploration of the real property tax itself. The real property tax to a land economist is really two separate taxes: the tax on the land value and the tax on the improvement value. Land must be treated separately because of the limited supply elasticity (i.e., the fixed amount) of land available, in contrast with the variable supply of structures that can be produced. The tax on land value comports with all the principles of sound tax theory; it is the tax on improvements that is so problematic.

It is impossible to deal with any modifications of the real property tax without first restoring its integrity. The present failure to adequately adapt real property taxes stems from their unique character, as well as from the fact that contemporary neoclassical economics gives no special place to land as a factor of production. Recapturing the rent from locations rather than letting it attach to those sites actually increases the efficiency of economic performance, even while it provides revenue for the support of government services. Taxing improvements, on the other hand, makes no sense whatsoever, from any perspective. It discourages titleholders from improving their sites to the full extent that their locational value warrants, and it penalizes them for maintaining them in good order. When a parcel is built upon or added to, the current property tax increases, a perverse incentive which discourages the behavior that policymakers should be encouraging. A bit of reflection should make it clear that taxes on improvements should be eliminated entirely.

If first the property tax were modified in ways that conformed to the principles of sound tax theory, it would then be easier to make modifications that address concerns such as those faced by the reputed "poor widow." Otherwise, any relief or adjustments run afoul so many of those basic tenets, and create so many other difficulties of both a technical and ethical nature, that the challenge remains unresolved. Addressing the matter *de novo* helps in framing the problem in a way that makes a solution both easy to understand and to implement administratively.

Examining the application of tax theory as it is applied in classical economics makes clear that taxing "land," in any of its forms, has no downside effects; it is indeed the perfect tax. It is totally neutral with respect to its influence upon behavioral choices, efficient insofar as there is no "excess burden" (a fancy word for productivity loss and economic drag), equitable to the extent that one pays according to one's ownership and use of sites,[38] simple and comprehensible in that the public can appreciate it, and administrable because of the transparency and certitude of land values. The major distinguishing reason for the advantages of taxing land is the existence of economic rent, a phenomenon that is essentially ignored in contemporary economics. Rent is the economic surplus that flows through and links to any location that has a market price. It connects to places that have an inelastic supply, especially land sites. Restoring the special place of land in economic theory would solve many of the problems associated with both tax design and administration as well as for larger economic policy discussions.

There was a time when one could argue that discerning the relative value of the land component versus the improvement component of a site was impossible. Although assessors have always regarded this as a bogus argument, modern computer applications and full command of sales data, as well as the ongoing redevelopment inherent in teardowns in many areas, have put an end to this purportedly insurmountable obstacle. In the aggregate, the land value of urban localities is typically between 30 and 50 percent, sometimes even higher. In some particularly noteworthy high-traffic or especially productive locations, the aggregate land value of cities reaches well above 70 percent of total real property value.[39] Although some people assume that a land value tax can be passed forward, this is not so, because the rental price to tenants for office or apartment units is necessarily set by the market and not by the overhead costs of the landlord. So also with imputed rent of homeowners. Improvements, in contrast, are elastic, especially in the longer term, and taxes on improvements, therefore, are susceptible to being shifted both forward to tenants and even backward to the building industry.[40]

Although not typically mentioned as a consideration in evaluating tax policies, one more criterion should be considered as important to any review of the real property tax, and that is its effects upon land use configurations and upon the environment generally. Land, being a limited resource, needs to be husbanded and used with care. Tax regimes should be designed so that they at least do not confound rational land use policies, and if possible even facilitate them. Current tax programs give little thought to such matters, and the consequences are to be seen in the rampant development of sprawled communities, the evisceration of urban centers, and the profligate use of energy and raw materials far beyond what prudence and ecological consciousness promotes.

Indeed taxes on real property as they currently exist actually foster foolish development, and it is adequately demonstrated that shifts to land value taxation alone go far toward reversing the centrifugal tendencies of sprawl as they are so ubiquitously practiced.

The utilization of economic rent as the basis for public spending has both an economic and a moral foundation. The recapture of rent in the form of a land value tax restores a clear moral dimension to both economics and to tax policy, and is the only tax regime that is morally sound. It makes land value taxation more clearly comprehensible and justifiable to the average person than any other regime of raising revenue. Inasmuch as economic rent is socially created value, it is returned to society for the support of social services. Rent is far from a trivial component of our economic system. Although our own US government statistics preclude it from being adequately calculated in ways that measures it in full, it has been so identified for the Australian economy, where the land portion of real estate totals at least 29 percent.[41] Suffice it to say, therefore, that even if substantial amounts of rent is recaptured for support of public services and in lieu of taxes that tap other revenue bases, the remaining rent attached to land sites would still appreciate property parcels.

Were every bit of economic rent from land sites recaptured in taxes, site values would, of course, fall to zero; there would be no flow of rent to sites and there would be none to be capitalized in the market prices of land components. Only the stock value of improvements would have a marketable price. Full implementation of a tax regime based on the recapture of all economic rents would obviate the need for taxation of people's wage labor and other capital resources. Nowhere in the world is so much land rent recaptured at the present time. But no more than a small fraction of rent taxation is necessary to supplant the current local property tax regimes in any case, much as proponents of land value taxation regard it as desirable. But without reducing reliance on sales taxes or income taxes or hotel occupancy taxes, much can be gained at the local level by increasing the collection of land rent while decreasing the tax on buildings, i.e., remaining revenue neutral. But smart state and local leadership will examine the merits of going further, reducing sales taxes and/or local and state wage taxes and collecting a larger share of local land rent. Gradual tax shifts in some twenty Pennsylvania cities that are now shifting from the conventional property tax to a land value tax – a phasing out of taxes on improvement values and a replacement increase in the taxation of land values -- still leaves the bulk of economic rent to flow through sites and appreciate their market value. It has also provided marked improvement to the economic vitality of those places.

Despite the strong public sentiment for the protection of windfall gains, people pay much more in other tax revenues than they would likely reap from cashing out on their home appreciation. This is because there is so much inefficiency inherent in those tax regimes.[42] In reality, the proportion of the nation's population and households that are "winners" in the property investment sweepstakes is quite low, even though the proportion of households that own their own homes is currently over 65 percent. We nonetheless read frequent stories about people investing in homes and even "flipping" them to get rich in astonishingly short time periods.[43] (At the moment, we are seeing stories of the households who have not been so lucky, who over-extended themselves

with sub-prime mortgages, and are now hoping to have a stable place to live.)

One typically also hears much more from well-situated winners who are threatened with loss of their property than we are from those who either are safely ensconced or never got into the game. This accounts for public policy measures that provide relief to those who feel so threatened. But for every long-term property owner that walks away with a lifetime's benefit of increased rent attached to a land title, there are just as many - if not more - young households or emerging businesses that are prohibited from acquiring a property because of exorbitantly expensive prices. In this sense, a title to a socially created stream of rental benefits constitutes a monopoly privilege to an unearned windfall gain for a lucky few. Yet, American culture has learned to see land speculation as common sport, if not as an entitlement, and has done so since its historic beginnings.[44]

One must go back to classical economic theory, and to its culminating figure and exponent, Henry George, for an appreciation of the importance of land. It meant at that time, and before, all natural resources -- air, water, mineral wealth, and, today, by extension, the electromagnetic spectrum, airport time-slots, and any other elements that have a market value not created by human hands or minds. The primary exponents of this tradition today are the remaining carriers of the classical economics heritage. The Georgist tradition sees considerable unfairness, as well as inefficiencies, in the real property arrangements that have evolved in the US and are taking hold in other societies.

In Henry George's moral order, calculated effort to capture elements of common wealth was tantamount to theft. It was the moral equivalent of owning slaves.[45] He viewed decisions by society to tax the effort of people's own minds and muscle as equally repugnant. He interpreted the rampant land grabs prevailing during his time and earlier as an historical aberration. His knowledge of Biblical history and his reading of practices led him to see that the classic source payment for the privilege of using land and other natural resources was economic rent, deliverable, of course, in labor, in goods, or in money, but always only as rent payment. One of his most eloquent speeches, delivered on May 8, 1887, to the Anti-Poverty Society when running for the Mayoralty of New York City, was "Thou Shalt Not Steal."[46] To George, the rightful and natural source of tax revenue was the economic rent yield from land, and he argued for and looked to a time when his tax reforms would arrive.

In contrast to the prevailing neoclassical economic tradition today, classical economics was all built on three factors of production – land, labor, and capital. Neoclassical economics sees nothing particular or special about land as a production factor, and therefore conflates it with manufactured items (essentially tools for further productivity) into a single category of capital. In classical economics, land cannot be "owned" as one might own a car or a pencil. As an element of nature it can only be used, and the meaning of its possession relates to its use and not to the rights inherent in fee simple titles. The importance of this cannot be underestimated, as land, then, is not regarded as wealth. Elements of nature, rather, are the common heritage and birthright of humanity. Only our own creations reflect our wealth, and come about only as the

products of labor and past capital. To Georgists, our house may be wealth but the land is not, a gigantic difference. Based on neoclassical economic premises, the NCSL Report has considerable difficulty as it unfolds in explaining and justifying the relief options that it describes. A high proportion of land economists subscribe to the Georgist tradition, and find great difficulty, therefore, in addressing the problems of real property taxation living within the framework of neoclassical economics.

The distinction between stock and flow in economics is particularly important when discussing economic rent, for the reason that real estate parcels are typically marketed for their stock value, whereas the land rent on those sites constitutes a flow. Economic rent or land rent is reflected in the value of site locations as the local and regional economy's surplus. All the value of market enterprise flows through locations and is capitalized in their market value. Absent its capture and diversion to interests bent on aggrandizement in what is known as "rent-seeking" or in taxes other than on land sites, the site value is ultimately reflected in market price. Directly recapturing the added value from site rents in the form of land taxes can stabilize real estate prices and obviate the need to tax people's labor and capital goods. Adherents to the Georgist economic tradition employ the physiocrats' acronym ATCOR – all taxes come out of rent – to explain this. South African Georgist Godfrey Dunkley prefers to say, "All taxes are at the expense of rent." Taxing rent directly, or land as the source of rent, avoids all the downside effects that are associated with other taxes, while at the same time stabilizing prices and the economy itself as no other tax can.

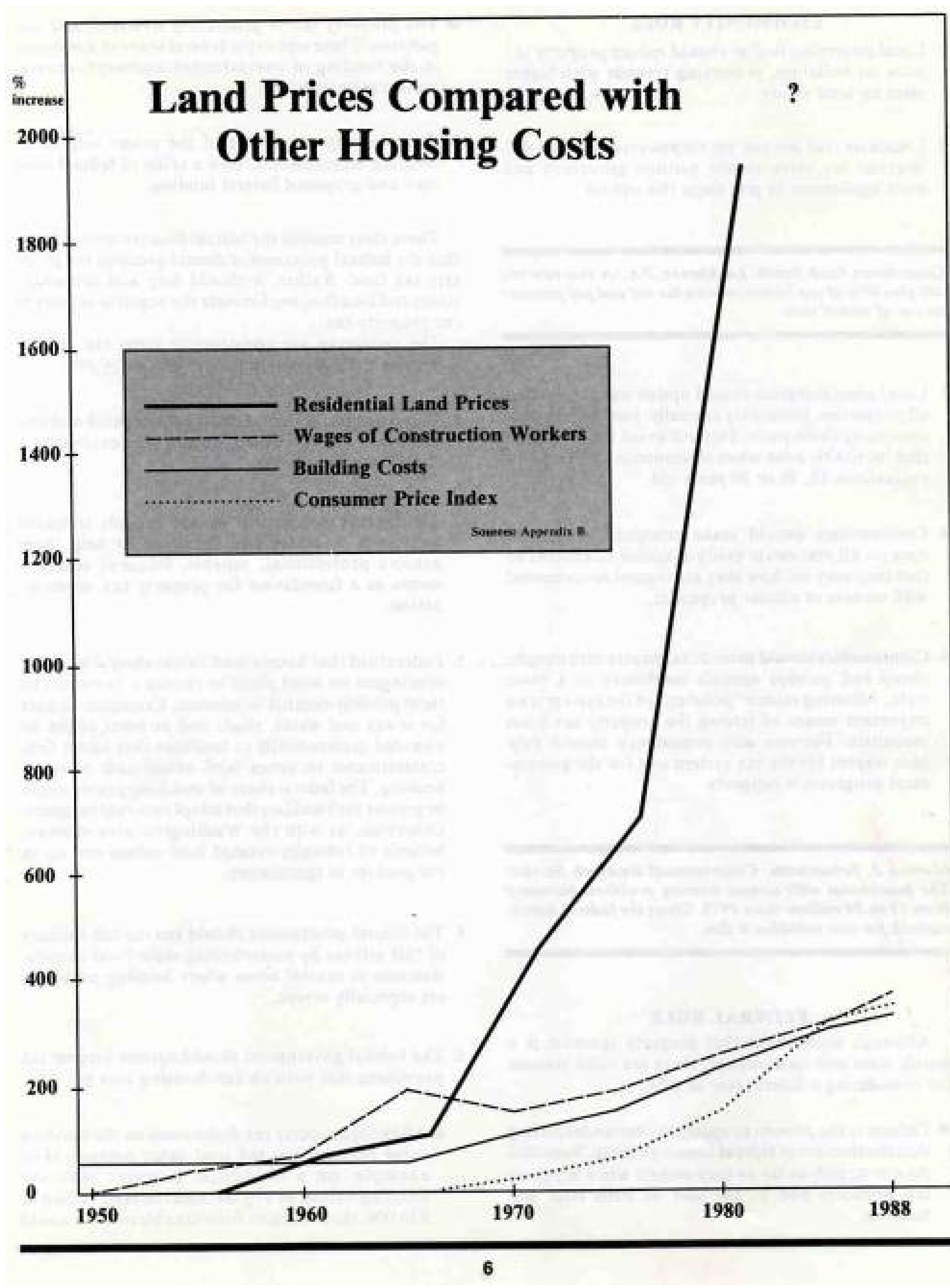
Georgist economists, and indeed many others, have long argued that land value taxation is the best solution to fiscal challenges, especially for local government finance. As policy stands now, however, the two components of the property tax are like a train with an engine at each end. The tax on improvements exerts a penalty upon those who would improve their sites, while the tax on land values provides an inducement for titleholders to build to the full extent that carrying costs warrant. Eliminating the tax on improvements would remove all the downside consequences of the property tax as it now exists. Doing so would foster development in high-value locations and thereby reverse the centrifugal forces of sprawl development. This would lead to an increased supply of housing and commercial office space, and in precisely those locations that are economically and, with proper zoning, environmentally desirable. With all the tax relief to residential property owners likely to eventuate under a regime that shifts gradually to a land value tax over time, the animus against taxation at the local level could well abate. Not only are most homeowners likely to see their overall burdens reduced, it would lead to positive results in the financial health of urban configurations as well as more support for public services.

Some adherents in the Georgist tradition abjure the word *tax* totally, and employ the word "ground rent," to refer to the revenue collected from the public for the privilege of using parts of nature. Others talk about taxing economic rents. It is a trivial point. The important challenge is to restore a moral basis for economics and taxation that has disappeared in the course of the neoclassical heyday now passing. As this paradigm collapses, recovering the tradition of classical economic theory is a task of the first order.

There is no better approach to achieving this than by tackling the questions of taxation. If Georgist approaches are to be part of this reconstitution of the field of economics, matters involving the specter of poverty, respect for nature, and their relationship to democratic systems will surely follow. One sees a renewed interest in this tradition worldwide, as other tax regimes are revealed to be unworkable or have greater liabilities.[47]

The Georgist solution offers a well-founded starting point in designing a sound structure for property tax adjustments where warranted, because it comports most perfectly with sound tax principles. A land value tax is neutral insofar as behavioral choices are not altered by its imposition. It is efficient because it imposes no excess burden or deadweight loss (often described as productivity loss and economic friction). It is equitably progressive because only individuals or households that own land pay any tax at all. Middle class homeowners for the most part own only modest parcels under their houses and farmers' holdings are where land is cheap. High value parcels in urban cores are typically owned by institutions and wealthy people and end up shouldering most of the burden. A land tax is simple enough to be easily understood and transparent enough for all to see. It is stable because land values are less subject to periodic cycles and abrupt changes than are taxes on other factors. And it is easily administered and certain because the parcel values on which it is based are readily assessed relative to other parcels and to sales records. No other tax provides such an elementary and feasible beginning from which to make further analysis. Despite its century old explication as a coherent paradigm, it owes its strong rebirth to the advent of computers and easily available data. The results of recent interest in and simulation of Henry George's claims shows that he was right: that taxing land value is a win-win-win for all elements of the community.[48]

With a soundly conceived tax on the land value of parcel locations, implementing a stopgap adjustment to relieve households that have for whatever reason become unable to pay their taxes is an easily included amendment. What has come to be known as the deferral option addresses the needs and expectations of both the titleholder and the community, in ways also that encourages an efficient housing market, efficient land use configurations, easily administered relief without undue government intrusion, equitable outcomes for all parties, and stable revenue streams.



Land Prices Compared with Other Housing Costs
% increase
2000
1800
1600
1400
1200
1000
800
600
400
200
0
1950
1960
1970
1980
1988
?
Residential Land Prices
Wages of Construction Workers
Building Costs
Consumer Price Index
Source: Appendix B.
6

[1] The reference to the poor widow is intended to be metaphorical. This could, of course refer just as well to a widower, an indigent family, or any other householder threatened with loss of a home when not able to make tax payments.

[2] The "poor widow" argument has a venerable history, traced even to the Bible; see Luke Chapter 21: "When he looked up he saw some wealthy people putting their offerings into the treasury and he noticed a poor widow putting in two small coins. He said, 'I tell you truly, this poor widow put in more than all the rest; for those others have all made offerings from their surplus wealth, but she, from her poverty, has offered her whole livelihood."
http://www.biblegateway.com/passage/?book_id=49&chapter=21

Elizabeth Cady Stanton, frequently invoked the "poor widow" argument in her political campaigns: "If all those magnificent cathedrals with their valuable lands in Boston, Philadelphia and New York were taxed as they should be, the taxes of women who hold property would be proportionately lightened...I cannot see any good reason why wealthy churches and a certain amount of property of the clergy should be exempt from taxation, while every poor widow in the land, struggling to feed, clothe, and educate a family of children, must be taxed on the narrow lot and humble home."
http://htomc.dns2go.com/atheism/cookie.41b

The poor widow rose again in a veto by Governor Billings of Vermont in 1925: "And now upon a plea to help out the poor widow who owns a few shares of bank stock, all the well-to-do bankers who are perfectly able and ought to pay as much tax as the owner of real estate and tangible personal property, and who can easily sell their bank stock when the taxation burden gets too heavy, are to be given a gratuity in a reduction in 50% of their tax so that when extra taxes are to be raised in their towns to build roads and school houses and to pay debts which are getting to be quite a municipal burden, the man struggling to pay for his real estate or business must absorb all of the extra burden. This seems to me to be unfair."
http://vermont-archives.org/govhistory/governance/Vetoes/pdf/1925BillingsH254.pdf

Winston Churchill, when arguing for land taxation in the House of Commons in 1909, was exasperated by the poor widow objection, i.e., that it would evict her from her home. In defending land value taxation, he responded with classic Churchillian eloquence: "When we seek to rectify this system, to break down this unnatural and vicious circle, to interrupt this sequence of unsatisfactory reactions, what happens? We are not confronted with any great argument on behalf of the owner. Something else is put forward, and it is always put forward in these cases to shield the actual landowner or the actual capitalist from the logic of the argument or from the force of a Parliamentary movement.

"Sometimes it is the widow. But that personality has been used to exhaustion. It would be sweating in the cruelest sense of the word, overtime of the grossest description, to bring the widow out again so soon. She must have a rest for a bit; so instead of the widow we have the market-gardener - the market-gardener liable to be disturbed on the outskirts of great cities, if the population of those cities expands, if the area which they require for their health and daily life should become larger than it is at present." Speech in the House of Commons, 4 May 1909, in response to Mr. AJ Balfour, Leader of the Opposition. http://www.earthsharing.org.au/node/32

[3] National Conference of State Legislatures (NCSL), *A Guide to Property Taxes: Property Tax Relief*. Denver, 2002, p. 1. http://www.ncsl.org/programs/fiscal/fpproptax.htm

[4] Other recent compilations of property tax relief programs are See, *State Tax Policy for Senior*

Citizens, Second Edition, Denver: NCSL, 1994; David Baer, "State Programs and Practices for Reducing Residential Property Taxes," Washington: AARP, May, 2003; David Baer, "State and Local Property Tax Burdens in 2005, Research Report," Washington: AARP, 2007; Donald C. Richards, Property Tax Relief for Senior Citizens. Wyoming Legislative Service Office Research, July 14, 2006, downloadable at http://legisweb.state.wy.us/LsoResearch/Researchlisting.aspx; and Virginia Municipal League Tables (n.d., 2005?) at www.vml.org/LEG/05PropTxIndx.html;

[5] These criteria are amply set forth in the classic public finance text by Richard and Peggy Musgrave, *Public Finance in Theory and Practice*. The fifth (and last) Edition, McGraw-Hill, 1989—sets forth in Chapter 12 the "Requirements for a 'Good' Tax Structure, which is generally followed in all the later texts. The virtues of land taxation are given considerable attention in these later texts. See, for example, Harvey Rosen. *Public Finance, Fifth Edition*. New York: Irwin/McGraw-Hill, 1999), pp. 486-495; and Neil Bruce, *Public Finance and the American Econom*y (New York: Addison-Wesley, 1998), pp.622-630.

[6] Richard L. Cole, John Kincaid, "Public Opinion and American Federalism: Perspectives on Taxes, Spending, and Trust: An ACIR Update," Publius, Vol. 30, No. 1, *The State of American Federalism*, 1999-2000 (Winter, 2000), pp. 189-201.

[7] Several Nobel Prize-winning economists have endorsed land-value taxation, even given their neoclassical economic predilections. See among other places: http://www.urbantools.org/research-and-studies, "Can a Site Value Tax be an Answer?"

Milton Friedman: "I share your view that taxes would be best placed on the land, and not on improvements."
Paul Samuelson: "Pure land rent is in the nature of a 'surplus', which can be taxed heavily without distorting production incentives or efficiency." A site value tax can be called "the useful tax on measured land surplus."
Franco Modigliani: It is important that the rent of land be retained as a source of government revenue. Some persons who could make excellent use of land would be unable to raise money for the purchase price. Collecting rent annually provides access to land for persons with limited access to credit."
Robert Solow: "Users of land should not be allowed to acquire rights of indefinite duration for single payments. For efficiency, for adequate revenue and for justice, every user of land should be required to make an annual payment to the local government equal to the current rental value of the land that he or she prevents others from using."
William Vickrey, 1996 Nobel Prize Winner, also endorses site value taxation: "It guarantees that no one dispossesses fellow citizens by obtaining a disproportionate share of what nature provides for humanity."
James Tobin: "I think in principle it's a good idea to tax unimproved land, and particularly capital gains (windfalls) on it. Theory says we should try to tax items with zero or low elasticity, and those include sites."
James Buchanan: "The landowner who withdraws land from productive use to a purely private use should be required to pay higher, not lower, taxes."

[8] I have summarized much of this thinking in "Principles of Sound Tax Theory as they have Evolved for 200 Years and More," http://www.progress.org/cg/battprincip02.htm. This enumeration is repeated, with corroborating citations, in the author's article, "Who Says Cities are Poor? They Just Don't Know How to Tax Their Wealth!" at
http://www.wealthandwant.com/docs/Batt_WSCP.htm, and in Note 3, of the author's article, "Painless

Taxation" at http://www.cooperativeindividualism.org/batt-h-william_painless-taxation.html. The latter was his submission to the President's Advisory Panel on Federal Tax Reform on April 24, 2005.

[9] See H. William Batt, "Stemming Sprawl: The Fiscal Approach," Chapter 10 from the book, *Suburban Sprawl: Culture, Theory, and Politics*, edited by Matthew J. Lindstrom and Hugh Bartling. Rowman & Littlefield Publishers, 2003. http://www.wealthandwant.com/docs/Batt_SSFA.htm

[10] It should be acknowledge here that there are some students of tax policy who, steeped in the neoclassical economic paradigm, still hold to the view that all revenue streams have some downside effects and that no tax is "perfect." Ironically, most of these same students are quite willing to subscribe to the list of criteria that is employed here. For my discussion of this, see 'The Fallacy of the Three-Legged Stool," originally published in State Tax Notes, Vol.35, No.6, 2 February 2005, pp.377-381, and online here at http://www.wealthandwant.com/docs/Batt_3legged.html

[11] See Fred Foldvary, "Efficient Taxes," Editorial, at www.progress.org/2006/fold473.htm
And Colin Clark, "Land Taxation: Lessons from International Experience," abridged and presented from Land Values, edited by Peter Hall, The Report of the Proceedings of a colloquium held in London, March 13-14, 1965, under the auspices of the Action Society Trust, at www.cooperativeindividualism.org/clark-colin_land-taxation.html.

[12] H. William Batt, "Testimony on Equity in Assessment Practices," New York State Assembly, February 6, 2007, http://www.wealthandwant.com/docs/Batt_Assessment.htm

[13] Mason Gaffney and Fred Harrison, *The Corruption of Economics*. London: Shepheard Walwyn, 1994. For my account of this, see my 1995 article, "How the Railroads Got us on the Wrong Economic Track," originally published in Torch Magazine, and now online at http://www.wealthandwant.com/docs/Batt_HTRGUOTWET.html and elsewhere.

[14] See, for example, Barron's Educational Series: *Dictionary of Real Estate Terms, Sixth Edition*, Jack P. Friedman, et al. (editors). 2004; also at www.answers.com.

[15] See Adam Smith, *The Wealth of Nations*, (1776) Bk.5, Ch.2, Pt.2, Art.1. : "Ground-rents and the ordinary rent of land are, therefore, perhaps, the species of revenue which can best bear to have a peculiar tax imposed upon them."

[16] Henry George, Progress and Poverty, 1879, and Robert Schalkenbach Foundation since. A short version has been published for the contemporary reader and available from the Schalkenbach Foundation, edited by Bob Drake, in 2006.

[17] The official handbook of The International Association of Assessing Officers states (p.547) that "the chief measure of uniformity [in aggregate analysis] is the coefficient of dispersion (COD), which, depending on the nature of the properties involved, should not exceed 10.0-15.0 for residential properties, 15.0-20.0 for commercial properties, and 20.0 for vacant [i.e., rural] land." Joseph K. Eckert, et al, Property Appraisal and Assessment Administration, Chicago: IAAO, 1990.

[18] One effort to deal with this challenge is a recent paper from the Bureau of Labor Statistics by Robert Poole, et al., "Treatment of Owner-Occupied Housing in the CPI," December 2005.

[19] See Michael Hudson, "The Land-Residual vs Building Residual Methods of Real Estate Valuation,"

Remarks to the New York University Real Estate Institute, October 25, 2000, online under articles at www.michael-hudson.com.

[20] Walter Rybeck, "The Property Tax as a Super User Charge," in Lowell Harriss (ed.), The Property Tax and Local Finance. New York: Academy of Political Science, 35(1):133-147, 1983.

[21] Yet, ironically, the Consumer Price Index does not include the cost of housing; the only measure even close is the Index of Real Estate Prices.

[22] See, for example, Nada Wasi and Michelle White, "Property Tax Limitations and Mobility: The Lock-in Effect of California's Proposition 13," February, 2005, NBER paper # 11108.

[23] The 2006 Wyoming Legislative Research Memo counts "at least 13 states" that have adopted some kind of "property tax freeze" program apply only to elderly homeowners. Among them are Arizona, Arkansas, Georgia, Illinois Louisiana, New Jersey, New Mexico, Oklahoma, Rhode Island, South Dakota, Tennessee, Texas and Washington.

[24] See, for example, Peter Schrag, *Paradise Lost: California's Experience, America's Future*. New York: The New Press, 1998; Daniel Smith, *Tax Crusaders and the Politics of Direct Democracy*. New York: Routledge, 1998; Arthur O'Sullivan, et al., *Property Taxes & Tax Revolts: The Legacy of Proposition 13*. Cambridge: Cambridge University Press, 1995; and David Sears and Jack Citrin, *Tax Revolt: Something for Nothing in California*. Cambridge: Harvard University Press, 1982.

[25] Connecticut Voices for Children, May 2007, "The Governor's Proposed Property Tax Cap: The Wrong 'Cure' for Connecticut's Relatively High Property Taxes," at www.ctkidslink.org.

[26] The March 3, 2006, issue of *Mortgage News Daily* carried the story that "Phoenix-Mesa-Scottsdale, Arizona [is] the top ranking Metropolitan Statistical Area (MSA) in the country with an annualized appreciation of 39.67 percent and a 7.77 rate for the quarter. Other markets with high annual appreciation are Naples-Marco Island, Florida (38.89 and 9.49 percent) Cape Coral-Fort Myers, Florida (36.19 and 7.19 percent) and St. George, Utah (35.27 and 8.21 percent). Of the twenty top MSAs in the county 10 were in Florida, four wholly or partially in Arizona and three in California. One year ago 14 were in California, four in Florida and two in Nevada."

[27] The *North County Times* (December, 26, 2007) reported "San Diego's home prices tumbled more in October than those in any major metropolitan area in the nation, according to a new report."

[28] The Institute on Taxation and Economic Policy estimates the number at "more than forty states." www.itepnet.org/pb12home.pdf

[29] The NCSL 2002 Report offers an illustration of the complexity involved in real property tax administration, especially comparing state to state. It illustrates with the comparative cases of California and Louisiana:
"The degree of property tax relief provided by homestead exemption and credit programs varies tremendously from state to state. The tax reduction depends upon the dollar amount of the exemption provided and the assessment ratio used to determine the taxable value of the property. In Louisiana, for example, each homeowner receives a $7,500 homestead exemption, while California homeowners receive a $7,000 exemption. Louisiana's program is much more generous, however, because the state uses a 10 percent assessment ratio to determine the taxable value of the home. A $100,000 house in

Louisiana has a taxable value of $10,000, so the $7,500 homestead exemption effectively exempts $75,000 in actual value from property taxes. California's assessment ratio is 100 percent, so its homestead exemption is worth $7,000 in actual value.
"After the homestead exemptions are calculated in the example above, the taxable value of a $100,000 house in California becomes $93,000, while the taxable value of a $100,000 house in Louisiana becomes $2,500. This represents a significant difference in benefit level because these are the amounts to which the property tax rate is applied when calculating the total tax bill."

Even tax law professor Susan Pace Hamill's survey, done with sixty-five research assistants, makes no attempt to summarize them in tabular format. This is the most recent compilation with exhaustive documentation, concerned primarily with matters of equity, simply describes each state's tax regime. See. Susan Pace Hamill, *As Certain as Death: A Fifty-State Survey of State and Local Tax Laws*. Durham, NC: Carolina Academic Press, 2007. Connecticut Law School Professor Richard Pomp compiles a frequent update of changes in state and local taxation on a comprehensive basis, including relevant legal cases. It too is chary in its effort to summary trends and patterns in a comprehensive manner. See. Richard D. Pomp and Oliver Oldman, *State and Local Taxation, Fifth edition (2005*), Hartford, CT: University of Connecticut Law School.

[30] For the most recent list of localities currently employing its Homestead option, see the New York State Office of State Controller's Annual Report: Overlapping Real Property Taxes, at http://www.osc.state.ny.us/localgov/orptbook/2004taxrates.htm.

[31] For further information on New York State STAR program, see www.orps.state.ny.us/STAR.

[32] This is the figure of the Wyoming Legislative Study dated 2006. An earlier NCSL study (2002) lists Iowa, Maine, Maryland, Michigan, Minnesota, Montana, New Jersey, New York, Vermont, Wisconsin, and Wyoming.

[33] The Circuit-Breaker eligibility threshold exceptions are as low as 55 and over for households with dependent children, 61 in Washington, and 62 in California, Maine, Montana, and Nevada.

[34] Data from the New York State Office of Real Property Services, at www.orps.state.ny.us/sales/resmedian.cfm

[35] Michael Hudson, President of The Institute for the Study of Long-Term Economic Trends (ISLET), a Wall Street Financial Analyst, Distinguished Research Professor of Economics at the University of Missouri, Kansas City, has estimated the proportion of capital gains that constitutes passed through economic rent is roughly 80 percent.

[36] See Residential Reverse Mortgage, a commercial agency, at www.reverseny.com. See also the National Reverse Mortgage Lenders Association, at www.reversemortgage.org, and the website for the US Department of Housing and Urban Development, at http://www.hud.gov/buying/rvrsmort.cfm .

[37] "More San Diego seniors jumping on reverse mortgage train," Mon Jul 28, 2003, *San Diego Daily Transcript,* "Reverse-mortgage market zooms forward: Plenty of new products are emerging, but consumers still need to be wary," *Marketwatch*, June 21, 2007; "Owning a home: from money faucet to drain," by Froma Harrop, *Creators Syndicate*, July 06, 2006; "Cash poor and house rich: Reverse mortgages can unlock money for those in a pinch," by Bruce Mohl, *Boston Globe* March 21, 2004;

"A mortgage tailor-made for seniors," Robert Bruss, Tribune Media Services, November 1, 2002; "Living Large On a Mortgage Of Last Resort: Tool Designed to Cover Basic Needs Of Retirees Is Used Increasingly For Second Homes, Luxury Items," by Kelly Greene, Staff Reporter of *The Wall Street Journal*, April 26, 2005; Page D1.

[38] Despite frequent claims to the contrary, the progressive nature of the real property tax becomes particularly apparent when looking at who pays: typically about half the burden is paid by commercial and industrial parcel owners, while farmers' land is so remote that it usually has inconsequential market value. Tenants pay no tax on any land component of their rental, and share the incidence of the building component with builders and landlords. Only two empirical studies have ever been done on the subject, but both concluded that the real property tax is mildly progressive. See Peter Mieszkowski, "The Property Tax: An Excise or a Profits Tax," *Journal of Public Economics* 1 (April 1972): 73-96, cited and discussed extensively by James Heilbrun, "Who Bears the Burden of the Property Tax?" in Lowell Harriss (ed.), The Property Tax and Local Finance, *Proceedings of the Academy of Political Science*, Vol 35, #1 (1983), pp. 56-71; and Henry J. Aaron, *Who Pays the Property Tax: A New View*, Washington: the Brookings Institution, 1975. These are reprinted and further discussed in Dick Netzer and Matthew P. Drennan (eds.), *Readings in State and Local Public Finance*. Oxford: Blackwell Publishers, 1997, Chapters 7 -- 10. See also Harvey S. Rosen, *Public Finance, 2nd Edition* (Homewood, IL: Irwin Press, 1988), pp. 483-489; Mason Gaffney, "The Property Tax is a Progressive Tax," *Proceedings*, National Tax Association, 64th Annual Conference, Kansas City, 1971, pp. 408-426. [Republished in *The Congressional Record*, March 16, 1972: E 2675-79. (Cong. Les Aspin.) *Resources for the Future, Inc*., The Property Tax is a Progressive Tax, Reprint No. 104, October, 1972], online at www.schalkenbach.org/library/progressivet.pdf .

[39] This is currently the case in Greenwich, Connecticut, the "gold coast" of that state. Other outstanding examples are Jackson Hole, Wyoming and King County, Washington.

[40] See Harvey S. Rosen, *Public Finance, 2nd Edition* (Homewood, IL: Irwin Press, 1988), pp. 483-489; or any Public Finance textbook.

[41] See, for example, Terry Dwyer, "The Taxable Capacity of Australian Land Resources," in Australian Tax Forum, January, 2003. www.prosper.org.au/Documents/TaxableCapacity.pdf; See also Steven Cord, "How Much Revenue Would a Full Land Value Tax Yield? Analysis of Census and Federal Reserve Data," American Journal of Economics and Sociology, Vol. 44, No. 3 (July, 1985), pp. 279-293.

[42] Harvard Professor Martin Feldstein calculates that that:
The efficiency loss from current income taxes is more than 30 percent. If Social Security taxes are included, there is a 50 percent efficiency loss. A 10 percent increase in taxes would raise revenue by only $21 billion, while reducing efficiency by $44 billion. The study finds that these conditions are aggravated because of the progressive tax structure of the U.S. tax code. *Review of Economics and Statistics*, November, 1999.

[43] The rising value of property parcels results in what economists know as the "wealth effect."

[44] Only in recent years is this history coming to be appreciated. Several recent books have probed the matter in depth. Among them are Andro Linklater's *Measuring America*. New York: Walker Books, 2002; John C. Weaver, *The Great Land Rush and the Making of the Modern World, 1650-1900*. Montreal: McGill-Queens University Press, 2003; Robert J. Miller. *Native America, Discovered and*

Conquered. Westport, CT: Praeger, 2006. This writer's review of these can be accessed by searching by www.askhenry.com.

[45] Henry George, Progress and Poverty, Boo VII: Justice of the Remedy, Chapter 2. at http://www.schalkenbach.org/library/george.henry/pp072.html

[46] Thou Shalt Not Steal," by Henry George, www.wealthandwant.com/HG/George_TSNS.html .

[47] See, for example, Samuel Brittan, Columnist "A Tax Idea that Can't be Buried," *London Financial Times*, April 15, 2005; "The Disappearing Taxpayer," (Lead Editorial) *The Economist*, May 31, 1997; John Petersen, "What'll Be Left to Tax?" (Lead Columnist) *Governing Magazine*, 1997, among many others.

[48] For a review of current studies of land value taxation at the local and state level, as well as corroborating endorsements, and accounts of ongoing legislation, see www.urbantools.org. For a list of various organizations worldwide that are linked by common adherence to Georgist views, see www.progress.org/cgo/. The common search engine through which resources on just about any subject (or name) can be accessed is www.askhenry.com.