



Thumbnail History of the Property Tax

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Thumbnail History of the Property Tax

1. Ancient Times

The oldest tax. Originally less a "tax" than a royal rent from the royal estate (hence "real estate").

Egypt, Babylon, Persia, China, and other ancient empires used it heavily.

Rome took the tax in the form of military service. This manned mighty armies, but is inherently regressive -- smallholders had to give as much as large holders, and the larger the family, the more you gave. This helped wipe out smallholders and cut the birth rate. Next to go was the Roman Republic itself. Cf. U.S. draft policy, French *corvée*, etc.

Later, in the middle east, Islamic empires, Byzantium, Turkey, in their days of ascendancy, used the proptax heavily, too.

2. Feudal times

The feudal system, with local variations, was nearly universal in Europe and Asia. When the central power was strong, land dues were owed to the King; when central authority weakened, they were used locally. In feudal legal theory, land is held from the King, subject to royal dues, often military service, in proportion to the value of land held from the King. William the Conqueror based dues on assessed values recorded in a cadaster, still known as The Domesday Book.

Modern property law still has this feudal basis. Land is held from the sovereign, subject to "servitudes", including taxation. Originally, all land was held subject to personal loyalty, or "fealty," to the King. This evolved into loyalty to the Crown as a symbol of the nation. The Church, torn between loyalty to Rome and the nation, held land subject to using rents for welfare purposes. Absentee alien ownership was impossible under this system. We, and every nation, retain remnants of this tradition, reminding us that land never can be as purely "commercial" as other property.

Over 900 years, feudal principles slowly eroded in England itself; but were exported to English colonies and former colonies in the form of the property tax.

3. American

a. Colonial Period

The proptax was the main tax, especially in New England. In proprietary colonies, the proprietor was expected to provide governmental services from his rents. William Bradford, of Plymouth Plantation, explained the system of equal land distribution, measuring by area, but using taxation to compensate for differences in quality of land.

Adam Smith wrote on the contrast of the egalitarian English colonies with the Iberian and French. The Dutch, while egalitarian at home, imposed the manorial "Patroon" system abroad, stifling development of the Hudson Valley for 200 years. The other great colonizer, Russia, exported serfdom.

b. 19th Century, westward expansion

As settlers moved west they needed public services, and paid for them mainly by taxing property. Call it "The tax that won the west." The resident settlers resented absentee speculators, and used this device to tax them, using state and county governments primarily, at first (and later, cities and school districts). This is the hidden fiscal basis behind the gunplay drama in traditional Hollywood horse-operas where settlers face off against cattlemen.

Taxing property was an element of native radicalism as per Jefferson, Jackson, Lincoln, and the lesser known Wm. H. Seward of New York (who became Lincoln's Sec'y. of State), but at the local level mainly. The opposition is exemplified by the patroon Robert Livingston, and his in-law Alexander Hamilton, in New York. Livingston pushed (in vain) for an income tax to displace the property tax, while Hamilton pushed for import duties and internal excise taxes. Hamilton, *consigliere* to the Patroons, maneuvered himself into writing much of the U.S. Constitution, where he got his way.

Ben Franklin, carrying Boston-bred ideas to Philadelphia, fought the tax-exemption of the Penn heirs in Pennsylvania, just as his contemporary Turgot was fighting such exemptions in France - but Franklin succeeded where Turgot did not.

The property tax on land has a developmental tendency: it was used to finance infrastructure. In the latter 19th Century, as cities grew and their needs grew, cities began to tax property heavily. The tax was used especially for public schools.

There are parallel histories in other Anglo colonies: Canada, Australia, New Zealand, E. Africa, Singapore, Hong Kong.

c. 20th Century America

From about 1920, the proptax has been gradually displaced by taxes on income, sales, and payrolls. State subventions and Federal Revenue-sharing help to replace it at local level. There was a revival of property taxation, 1950-78, followed by another fall. The forces that supported it in the past will undoubtedly revive again - it is too rich a tax base to leave unpreempted, and we cannot live forever on inherited infrastructure.

d. What level of Government uses the proptax?

1. Federal

The Founding Fathers assumed that the national government, like the colonial governments, would levy property taxes. The early Articles of Confederation, Article VII, had the national government levying on the states in proportion to the value of land in each one. The U.S. Constitution, drafted in large part by Hamilton and Madison, weakened that concept with the "Regulation of Apportionment," requiring the U.S. to apportion property taxes among states according to their populations - thus forcing a different ad valorem rate to be used in each state, creating enough rivalry and confusion to keep Congress from using the tax much. Congress used this power just five times, the last time being 1863.

To parry the demand for national taxes on property, Madison and Hamilton's strategy was also to divert the tax to the local level, where local particularism puts a natural cap on the rate. In England, much later in the 1920s and 1930s, Neville and Austen Chamberlain adopted the same strategy to undercut the then-strong campaign for a national land tax. While Chamberlain's main motive was to abort the welfare state, he also succeeded in weakening the armed forces and encouraging Hitler's aggressions, leading to the humiliation of Munich, 1938.

The force of local particularism was dramatized by Upton Sinclair's campaign for Governor of California, 1934. He proposed making California a redistributive welfare state. He got licked by fear of "swamping the lifeboat." Egalitarian policies generally cannot succeed at subnational levels. A more recent case in point is the movement for "Socialism" in British Columbia, 1972-76, and how it turned into snob zoning.

2. State

Until about 1930, many state governments relied on a state property tax. In 1920, for example, half of Sacramento's revenues were from this source. A major function of the State Board of Equalization was to force County Assessors, who are locally elected, to keep local assessments up to snuff.

There are various formulae to require wealthy school districts to share some of their tax base with poorer ones. One is called "power equalization." These are political compromises, and fall far short of complete equalization. To the extent that they do equalize, however, they amount to a state-imposed property tax. The same is true of "Mandated Programs" where the state requires each county to finance welfare services from its local property tax. In California, such programs have become almost moot since Prop. 13, 1978, because each county, straining and starved for revenues, keeps its proptax rate at the legal cap of 1%. In other states, however, the matter is a burning issue. New Hampshire and Vermont, for example, are in the process of

complying with court orders to find means to equalize school finance statewide.

We have seen that rail and utility property is state-assessed but locally taxed. We have analyzed the relation of this to fractional assessment, equalization, and the alliance of utilities with local property tax opponents.

3. Local (counties, cities, schools, and special districts)

Today, the property tax has been "devolved" mainly to local governments; and local governments increasingly receive "subventions" from state governments and Washington, thus substituting other tax bases for those on property. For better or worse, this has been a nationwide trend for 50 years now, resulting in soaring land prices and a huge gap between workers' gross incomes and their "disposable" (after-tax) incomes. Another result is local overzoning for retailers, to maximize local sales-tax revenues, and a 30% retail vacancy rate.

There is a peculiar drama in special districts, especially those serving water. Their land taxes are legally "benefit assessments," and not legally taxes, hence exempt from the Prop 13 cap. The voting franchise in water districts was originally democratic, but now may be restricted to landowners only, and often has been, a subject of intense litigation and current controversy. Landowner-controlled districts have pyramided power up to the MWD, a focus of the Southern California power structure.

Counties, cities, schools, and special districts.

Peculiar drama of special districts: "benefit assessments" are not legally taxes, hence exempt from Prop 13 cap; base is land only; franchise may be restricted and often has been, a subject of intense litigation and current controversy; pyramiding of power up to the MWD, a focus of the Southern California power structure.

4. Political Strategy

To parry the demand for national taxes on property, opponents like Madison and Hamilton diverted the tax to the local level, where local particularism puts a natural cap on the rate. Austen Chamberlain's campaign against the English land tax. Upton Sinclair's campaign for Governor of California and how he got licked by fear of "swamping the lifeboat." "Socialism" in British Columbia and how it turned into snob zoning.

D. Allocational Effects

Define "effects" of increasing the property tax. Always ask, "compared to what?"

1. Hold public spending constant and reduce other taxes.

Land tax is stimulating and developmental. An unusual "incentive tax" that motivates rather than drags.

- a) Fixed base
- b) No taxable event

Building tax:

a. In open economy is shifted to land (the Physiocratic model of Quesnay et al.), reducing in the process the capital-intensity of use. Sometimes reduces, sometimes increases labor-intensity of land use, as labor is substituted for capital.

b. In closed economy, reduces the RRAT but in a manner nearly neutral. The "Harberger" model, (although many others preceded him). This is currently often called "the new view" of property tax incidence, although "revived" or "exhumed" would be more accurate. It puts the supposedly conservative Chicago School (which Harberger represents) in the position of justifying heavy taxes on capital. This is not just an accidental deviation from the conservative stereotype, but is more consistent with Chicago's traditional effort to identify capital and land. Harberger in effect is treating the capital supply as fixed, just like land.

c. In partial equilibrium analysis, one form of capital is taxed while others are not. This reduces supply and tax is shifted forward, like an excise tax. These are called "excise tax effects." Models like this come from Musgrave and Netzer.

Tax on personal (movable) property

Much movable property escapes assessment. Uniformity is impossible; bias results.

2. Hold other taxes constant; increase spending.

Results depend on circumstances: how productive and useful is public spending? Are we short-changing schools and other people-services and falling behind other nations?

James Buchanan's view: all public spending is wasteful, so the best tax is the most destructive tax because it will raise the least revenue. (Curiously, Buchanan has spent his entire career teaching at tax-supported schools.)

Marshall's "onerous" vs. "beneficial" taxation, and its modern implications: tax property only for services to property, not to people.

Social dividend view: assert the public equity in property through taxation and spread the benefits around.

Feudal view: military spending is a service to property and property should support it. "Custer died for your sins," so don't just ask "what have you done for me lately?"

E. Distributional Effects

1. Allegations of regressivity

2. History of being regarded as progressive and "levelling." Bradford; Madison; Paine; Hamilton; Livingston; Quesnay; Du Pont; Franklin vs. the heirs of Wm. Penn; Patroons in New York, Patronos in California; resistance to organizing counties, incorporated municipalities, and taxing districts with universal suffrage; voter exclusion; Adam Smith, J.S. Mill, Henry George; Tom Johnson, Brand Whitlock, Newton Baker, cheap transit and civic revival, 1900-20; exporting tax ideas to LDCs after WWII; applications in Japan, Taiwan, Korea, Singapore, Hong Kong.

3. Contract vs. organic theory of government. "Benefits received" construed narrowly and broadly.

4. Maladministration: regressive assessment (e.g., timber in Oregon).

5. Balkanization. Low-tax enclaves in California. Fallacy of identification: enclaves of low income taxation in Wisconsin.

6. Concentration of property holdings. Dependence of high incomes on property sources. Especial concentration of unrealized "capital gains" which escape income tax but not property tax.

7. Regressive use of property. Slow sales by large holders. (Land/labor ratios rise with size of firms.)

8. Bias in partial inventories of wealth. Diversified large holders. Multi-national holders escape much income tax, but not property tax.

9. Allegations of forward shifting: Musgrave, Netzer.

10. High share of real estate is land: 45% of assessed value, probably 65% of true value (using building-residual method of separating).

11. Tax on capital not generally shifted forward, but downward. Still a tax on property.

12. Regression Fallacy. The Procrustean Bed of "income", a catchword that has obscured analysis for 50 years. The use of AGI as the criterion of "like circumstances", horizontal equity and vertical equity.

13. Defining income properly. AGI is after loopholes, and no index to real income. Property income in various forms largely escapes AGI, and property provides loopholes to shelter other income.

14. Property taxes are not proportional to rents but to capital values, which are progressive w.r.t. rents.

15. Appreciating land is most closely held of all assets, and free of all but property taxes.

F. Central Government and Local Incentives

1. Social dividends issued nationally or statewide tend to make local governments compete to attract people.

2. Kinds of partial social dividends: G.I. Bill; loans with per person limits; school aids based on ADA; HEW payments; social security payments (not taxes); cash payments (e.g.

Alaska); reapportionment according to population.

3. Competing for a fixed population is zero-sum, population-wise; but increases bargaining power of the movable population vis-a-vis holders of immovable property.

4. New move in Congress to assume more people-aids; shift more property aids to locals.

5. Negative social dividends: payroll tax; most of personal income tax; conscription; sales tax (except the portion shared locally); etc. Any exported tax based on population and/or activity acts as a negative social dividend. Marshall's "onerous" tax concept again.

6. Mandated county welfare spending, maximizes fear of "swamping the lifeboat." Turns local property tax into a "tragedy of the commons", one step removed. Kicking MediCal around.

7. The current imbalance: Feds subsidize land development while extracting negative social dividends. Result: exclusionary local zoning.

8. People-based revenue sharing formulae in other Federal states: Canada; West Germany.

G. Summary of rationale for property tax

1. Simultaneously progressive and incenting, resolving greatest trade-off in tax policy

2. Strikes surgically at non-functional source of economic power, exempts functional income. Implements the productivity theory of distribution and the Puritan ethic, at least w.r.t. labor. Exempt capital and it also implements the ethic w.r.t. saving.

3. Promotes intergenerational equity. Other taxes strike upward mobility.

4. If "Custer died for your sins" this tax makes us pay for our sins. (Alternatively, give it all back to the Indians and then tax it heavily.)

5. Is part of implied social compact -- or the actual Mayflower compact, as implemented by Bradford.

6. Promotes all three kinds of equity: functional; egalitarian; and market. And a fourth kind, too: interregional equity.

7. Penalizes cartels for holding excess capacity.
8. Is the effective seller motivation that keeps land markets from turning to glue. Moving the market reduces need for people to hold advance reserves.
9. Recoups for public the benefits of public works.
10. Moves landholders to respond quickly to new opportunities, e.g. from new extension of public works.
11. Offsets boom and bust in land markets (if assessors move quickly with the market).
12. Offsets major loopholes in the income tax.
13. Compensates those who missed out (or whose ancestors missed out) on the original political distribution of land by moving landholders to use land to: a, pay taxes; b, employ workers; c, produce goods.
14. An effective and indispensable part of "supply-side" macro-economics. Fights unemployment by promoting land use and investment.
15. Base is non-erosive, non-migratory.
16. Implements Haig-Simons by taxing unrealized capital gains, inherently and automatically.
17. Imposes a Performance Standard on landholders: "What have you done with the Golden Talents" which society has placed in your stewardship?
18. Does not discourage new investment (especially if capital is exempted).
19. Focuses on unearned income, which places one on a higher plane of well-being than the equivalent earned income since one has the leisure to enjoy it.

(More on this in "The Economics of Abundance," on reserve