

Dear Senator Burdick,

Below is a letter I sent to Senator Haas concerning the upcoming discussion of tax reform starting on April 15th. I was advised by Nathan Howard to forward it to you and the committee administrator for consideration by the Finance and Revenue Committee. I will re-print it in its entirety without edit. Thank you for your time and for your consideration of comprehensive tax reform.

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Dear Senator Haas,

I am pleased to see your interest in tackling wholesale tax reform, as reported in the Oregonian on 4/9/13 ("Sales tax proposal kicks off discussion of Oregon's revenue future"). I am also delighted that you are not "wedded" to the concept of a sales tax, or any tax in general, but are genuinely looking for a root and branch discussion of taxes. As you said in the article,

"The goal is to ask Oregonians what they would do if we were a new state and we needed a new tax code. How would we write it? One thing I'm sure of, it wouldn't look like the one we have now."

Also, the article says that you are "lining up a slate of speakers that include business leaders, parents of school children, workers and others," for your hearings starting on Monday. As someone who is a parent of 4 children (two currently in school), a son of two school board members currently serving the school district to which I send my kids, and until recently tirelessly worked 60 hours a week at two jobs before a layoff knocked me down to 40, I am personally concerned with the symbiotic relationship government revenue and job growth have with each other. I have made the technical study of tax reform my number one priority and have evaluated all aspects of the various tax reforms, both proposed and not proposed. I want to submit my opinion to you via e-mail, since my voice is not able to be heard on the dates that are scheduled.

Since the main concern of your tax reform inquiry is to ask which reform would stabilize revenue and avoid cyclical budget shortfalls that hit school districts hard, I will address this first. Before any real solution can be gleaned, however, some key questions should be asked: Why is there a boom-bust cycle in the first place, and is there a tax policy that can stop the cycle (which avoids the question of which tax best weathers recessions)? If we can abolish boom-bust and put in its place steady growth via the tax system, this would be preferred. Fortunately, there is an answer. Boom-bust cycles have followed the same pattern routinely for centuries, and the common denominator is land speculation bubbles that pop. 2008's Great Recession, 1929's Great Depression, and the numerous Panics in the 19<sup>th</sup> century all saw rampant land speculation preceding the crisis. If land speculation can be stopped, recession and the ensuing budget contractions can be stopped as well. The way to stop land speculation is very simple, and only requires a shift in an already existing revenue generator, the real property tax. The real property tax is a tax on both the land and the structures built on it, and the reform of the tax that is needed is to shift the tax off of the buildings and focus all of the tax on the land portion of

the property. This is called a land value tax (LVT) and it is the reform that will end boom-bust in Oregon and provide ample revenue for social programs in a non-cyclical fashion.

Why will LVT halt the business cycle? The simple answer is that collecting a sufficiently high tax on the rental value of land precludes that value from accruing to private hands. Since the value is no longer going into private hands, speculating in property and driving prices up is no longer rewarded because the taxman would eat up the gains anyways. But why would people obtain land if they didn't obtain the asset value, you might ask? The answer is that they would obtain it for its intended purpose: its use value. People who are worried most about the loss of the asset value of land are people who are worried that they can no longer make an income on speculative asset gains rather than through using the land productively. People who wish to use land productively would welcome a reduction in the price of land, which means lower borrowing costs or a lower upfront cash payment to pay for asset gains to people who are choosing not to use the land anymore. The most complete example of LVT being used was Kiaochow, China while it was under German colonial rule from 1898 until the outbreak of WWI in 1914. The German colonies in Africa during the 19<sup>th</sup> century were plagued by disastrous land speculation that accompanied German investment in infrastructure. The imperial commissioner for Kiaochow had learned the lessons brought to light by Henry George about the dangers of land speculation and the use of LVT as the remedy and established a 6% tax on the value of land in the colony as its sole source of revenue. Not surprisingly, land speculation was non-existent in the colony and its main city Tsingtao developed into a modern city. LVT is also in use in milder forms in numerous Pennsylvania cities and the Asian tiger economies of Hong Kong, Taiwan, and Singapore, who use land-based revenues to provide ample social services without resorting to high income taxes.

Since I have demonstrated that an LVT would solve boom-bust and provide a steady income, I will move on to its adequacy as a tax base, because LVT is best combined with an abolition of all other major taxes (in Oregon's case, the personal and corporate income tax and taxes on non-land property). For starters, LVT is a tax that does not induce distortions in the economy, unlike income and sales taxes. This means that the loss of economic activity (called 'deadweight loss') that is currently being inflicted on the economy will be brought back as available for both private and public consumption. No less an authority than Nobel-prize winner Joseph Stiglitz, writing in his public finance textbook *Economics of the Public Sector*, notes that:

"... the burden of the tax on capital is not felt, in the long run, by the owners of capital. It is felt by land and labor.... in the long run, workers will emigrate... this leaves land as the only factor that cannot emigrate... the full burden of the tax is borne by land owners in the long run." "While a direct tax on land is nondistortionary, all the other ways of raising revenue induce distortions."

There are two main points to take away from this passage. First, a direct tax on land is nondistortionary and thus will stimulate economic activity currently being burdened with deadweight taxation. Second, he says that the burden of taxes on capital and labor are not felt by capital and labor, in the long run, but on land income. Eliminating taxes on capital and labor would then mean more income for land, and since the tax base is comprised of land income in an LVT economy, it should become clear that any tax revenue lost by abolishing existing non-land taxes will be recouped by the LVT, to the extent that LVT is implemented.

The truism that all taxes come out of rent (and tax decreases go back to rent) is because, according to Gavin Putland, an Australian researcher:

“In any tax jurisdiction, the supply of land is fixed. From the viewpoint of the taxpayer, the supply of land zoned for any particular purpose is also fixed, as is the supply of land within acceptable distance of any particular services, infrastructure, or markets. Yet access to suitably located land is essential to economic participation. Therefore land values, expressed as rent or as interest on purchase prices, are competed upward until they absorb the economy's capacity to pay. As that capacity increases — as it usually does — so do land values.”

The price of any object is determined by a function of supply and demand, and land is no different in this regard except for the one fact illustrated above: its supply is fixed. This means that demand alone is what sets the price for land, and demand is a function of how much money is able to be paid. It is analogous to the ideal gas law: if you hold the volume of gas constant (much like land's supply is constant), then increases in pressure (income) begets increases in temperature (land value), and decreases in pressure (income) begets decreases in temperature (land value). Thus, tax cuts on productive behavior lead to higher land value. The goal of LVT is to make sure that the increased land value is returned to the Treasury rather than captured by land owners. As an aside, this is why supply-side economics leads to more inequality. Lower taxes are not returned to the labor and capital owners that created the value. Rather, land owners, who provide no productive service, sop up the extra purchasing power returned to the producing class and leave them no better off. In the end, the rent must be paid, and it is just a choice of to whom: the government whose services give rise to most of land's value through access to police, courts, schools, and roads within its jurisdiction, or to the land owner, who provides none of those things but captures the value provided by those services.

In conclusion, a land value tax is the best tax reform for Oregon because it solves the two main problems besetting our current tax system: volatility of revenue streams and maintaining adequate revenue while not burdening any economic actor. LVT will abolish the dominant cause of boom-bust, land speculation, and therefore prevent volatility instead of reacting to it. LVT is also nondistortionary, so the maximum amount of economic activity can take place without disappearing due to deadweight loss. Finally, LVT will provide an adequate amount of revenue because it takes the maximum amount of revenue that the economy can bear. Any attempt to take more by creating a three-legged stool of income and sales taxes to go along with the LVT would be akin to Oregon playing tug-of-war with itself: an equal amount of revenue gained by the other legs would be taken away from the LVT leg, and in addition, jobs would be lost because income and sales taxes produce deadweight loss.

Thank you for your time and I hope that you consider LVT in your deliberation for a tax system overhaul.

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