

Testimony to the House Revenue Committee

HB 2509, March 19, 2003

Kris Nelson, Legislative Director
Common Ground OR-WA
Portland

Chair Barnhart and Committee Members:

Since Oregon voters passed Measures 5 and 50, widespread economic distortions and inconsistent property tax obligations have been documented. Our study of Salem's early experience with property tax limitations and use of maximum assessed values showed that tax burdens have shifted off of rapidly-appreciating properties and onto properties with slower-growing or decreasing assessed values (1). Statewide, the effect has been to transfer tax burden onto residential properties.

Because Measure 5 tax limitations have caused local levies to go uncollected, the disparate provision of voter-supported services has created widespread frustration and calls for remedial action.

The proposals we have seen thus far to address these tax discrepancies do not provide adequate tax relief. Reset upon sale, either to real market value or a countywide average, could take up to 30 years to reach turn-over of housing stock. Fixing compression alone leaves out the underlying unfairness of Measure 50. How can we permanently fix these problems while maintaining a check on unlimited growth in property taxes?

Considering the 80-plus years of success in ^{some of the} nearly 20 Pennsylvania and Hawaii cities using the two-rate structure that reduces the rate on improvements and compensates with a higher rate on land values, several advantages can be expected if Oregon adopts this model (2):

1. Similar to the Enterprise Zone, cutting the improvement rate removes the penalty for investing in capital improvements. This has been found to lead to increased building permit volumes, infill development, an increase in housing supply, higher lending activity, increased employment, and an expanding tax base (3).
2. Adjusting the rate on land assessments upward has been shown to cause no deadweight loss, or drag on the economy, unlike income or sales taxes. In fact, studies have shown this drag effect costs about one-third of the revenue collected in these other taxes (4).
3. Economists explain that land taxation is capitalized into the price of land; this has an inflation mitigating effect. The result is a more stable real estate market and reliable tax revenue stream.
4. When improvement assessments become less important, and because land is assessed on an area basis, property tax appeals have been found to decrease. This had led to fewer staff and greater productivity in assessment departments.

According to accepted economic theory, value created in property legitimately belongs to the source of that value. Improvement value stems from private investment on specific parcels. So owners have the legitimate right to retain most of the building value which they have created. Land value accrues from public investments and actions like up-zoning, as well as natural amenities, location advantage, and population growth. The community is justified in collecting its legitimately created value in land.

Land value taxation is a self-perpetuating way to fund urban infrastructure. When cities up-zone or expand urban growth boundaries, elevated land tax revenues from newly developing locations can be used to fund local infrastructure, which further boosts site values, which in turn raises added revenue to fund more infrastructure. At least eight Nobel economists verify LVT's record of providing incentives for urban revitalization, as well as its ability to raise sufficient, reliable, broad-based revenues.

Then what are the core issues we need to assess to provide a smooth transition from the woes of Measures 5 and 50 to a local option land value tax? A task force would study several questions, including:

1. How can relief measures best be designed for homeowners that experience large tax increases resulting from the return to real market values? Phasing-in the two-tiered tax rates over five to ten years will minimize precipitous increases; a tax deferral until sale would also afford relief. Another option is to consider a homestead exemption on land value up to a reasonable amount.
2. What would be the revenue-generating effects of land value taxation on overlapping taxing districts? Depending upon the overall assessment ratio of land to improvements, some districts might experience a decrease in revenues, and others an increase compared to an equal rate tax.
3. How would revenue growth limits instead of rate limits work most effectively? Similar to Washington's use of local revenue caps, might local entities adopt statutory limits based on the rate of inflation or some other index?

The longer we delay tackling such questions, the greater the opportunity costs to struggling communities that could unleash productivity gains clearly available if the two-rate incentive tax system were available. We ask you to support this bill as the means of bringing about proven prosperity for businesses, homeowners, and local government.

Thank you for your consideration.

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- 1: "Tax Shift Sequential to a Land-Based Property Tax System in Salem, Oregon," Gihring, Tom, Ph.D., Nelson, Kris, MBA, The Geonomy Society, 1999.
 - 2: <http://www.urbantoolsconsult.org/upload/LVT%20Jurisdictions%202013.pdf>
 - 3: <http://www.urbantoolsconsult.org/Tax-Reduction.html>
 - 4: "Testimony Submitted to the Assembly Standing Committee on Libraries and Educational Technology," Batt, William H., Ph.D, *GroundSwell*, November-December 2012, Beloit, WI; <http://commonground-usa.net/gsrecent.htm>

TAX SHIFT SEQUENTIAL TO A LAND-BASED PROPERTY TAX SYSTEM IN SALEM, OREGON

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Tom Gihring, Ph.D.
Housing & Planning Consultant
Seattle, Washington
tagplan@comcast.net

Kris Nelson, MBPA
Geonomics Consulting
Portland, Oregon
krisjn@earthlink.net

ABSTRACT

The Portland based Geonomy Society conducted a study of *tax shift* in the Salem metropolitan area, with the aim of illustrating how a reform of the state's property tax system might be implemented. Measure 5, Measure 50, and the Enterprise Zone program all place limits on the growth of individual assessments as well as caps on tax rates. The cumulative effect of these tax initiatives approved by Oregon voters since 1990 is a shift in tax burden from some classes of property onto others. Reforming the property tax system would first correct the assessed value distortions caused by tax limitations currently in effect, and secondly introduce a graduated land-based tax system that targets land rent as the legitimate source of local government revenue.

The study design employs a two-step tax simulation process. First, individual property assessments are changed from the current taxable values to true market values, allowing an examination of tax burden and revenue shifts that accompany a departure from the normal practice of applying uniform tax rates to current full market values. Secondly, a split rate **land value tax** is applied to the true market land and building assessments. Differential-rate tax outcomes are compared to conventional tax outcomes to ascertain the direction and amount of tax shift that would occur in a transition to LVT. The data base consists of 70,000 tax lots, with land use, location and valuation variables provided by the Marion County Department of Assessments.

Study results reveal the disproportionately high tax burdens that accompany current property tax limitations: on central business district developed parcels, lower value locations, and residential properties in general. A change to true market assessments and land-based taxation is shown to be less punitive to owners who undertake substantial capital investments—who put their land into production or use land more intensively. The greatest benefits accrue to multifamily and smaller lot residential properties, as well as centrally located fully developed sites. Conversely, LVT tax simulations demonstrate upward tax shifts associated with vacant and underutilized sites, especially those in central locations.

Owners of all real estate, including owner-occupied residential properties, realize land rent as long as site values continue to rise. Land rent capture rates as well as the land price-dampening effects of LVT are simulated by extrapolating observed home price increases over a hypothetical holding period and modeling the tax effects on speculative gains.

The study questions assessment practices that tend to adjust building values on developed sites roughly in proportion to land value increases, and devalue "excess" land on large-lot parcels. Both practices weaken the incentive effects of LVT. The question could also be raised as to whether industrial and some commercial sites are undervalued, thus shifting added tax burden onto residential sites.

Pennsylvania Jurisdictions that employ Land Value Taxation (LVT)

Millage Rates as of January 2013

Jurisdiction	Land Tax Rate (mills)	Building Tax Rate (mills)	Tax Ratio	Aggregate Property Tax Rate (mills)	Year Established
<u>Aliquippa School District</u>	188.000	29.500	6.3729	60.530	1993
<u>Aliquippa City</u>	81.000	11.400	7.1053	24.900	1988
<u>Allentown City</u>	50.380	10.720	4.6996	17.520	1997
<u>Altoona City</u>	369.015	0.0	369.015	47.84	2002
<u>Clairton City</u>	33.000	3.5	9.5	7.500	1989
<u>Clairton School District</u>	75.000	3.100	24.1935	22.000	2006
<u>DuBois City</u>	82.000	2.000	44	18.370	1991
<u>Duquesne City</u>	18.50	11.5	1.61	10.3	1985
<u>Ebensburg Borough</u>	25.00	7.500	3.33	10.500	2000
<u>Harrisburg City</u>	30.97	5.16	6.0	9.630	1975
<u>Lock Haven City</u>	22.16	4.55	4.9	7.58	1991
<u>McKeesport City</u>	16.500	4.260	3.8732	7.000	1980
<u>New Castle City</u>	26.497	7.792	3.40	11.18	1982
<u>Pittsburgh Business District</u>	4.374	0	4.374	N/A	1997
<u>Scranton City</u>	92.2636	20.065	4.6	28.500	1913
<u>Titusville City</u>	53.510	13.35	4.0082	18.333	1990
<u>Washington City</u>	100.630	3.500	28.7514	21.620	1985

Sample Pennsylvania Cities Using Land Value Taxation

(1) The contiguous cities of Allentown and Bethlehem in eastern Pennsylvania are very comparable as to size and economy. In 1997, Allentown started taxing buildings less than land; Bethlehem did not. Allentown's new private construction & renovation thereupon grew by 32% in dollar value in the three years after the shift to land value taxation as compared to the prior three years. That was 1.8 times more than Bethlehem's increase in private construction & renovation during the same time period, even though Bethlehem (but not Allentown) received much federal grant money in the prior three years. These figures come from a study of building-permits on file in the Allentown and Bethlehem city halls by Benjamin Howells (science researcher and one-time Allentown Councilman), William Kells (science-oriented businessman) and Steven Cord (professor).

(2) Washington and nearby Monessen (both in southwestern Pennsylvania) are roughly comparable as to size and economy. After Washington started shifting some of its tax off buildings onto land in 1985, its new private construction & renovation increased by 33% in dollar value in the three years after its two-rate adoption as compared to the prior three years. But during the same time, nearby one-rate Monessen's new private construction & renovation actually decreased by 26%.

(3) Connellsville, Pa., saw its new private construction & renovation jump 3.46 times in the three years after it adopted a two-rate LVT property tax as compared to the prior three years. This jump over-shadowed the modest 1.07 increase in new private construction & renovation of nearby one-rate Uniontown during the same time period. The two cities are quite comparable, although Uniontown is the county seat and is somewhat larger (economic development plusses).

(4) Aliquippa, Pa., after the closing of its large steel mill, shifted some taxes off building onto land values in January 1988. Result: most residents paid less taxes and its new private construction & renovation jumped 97% in the three years after the two-rate switch as compared to the three-years-before. Nearby Ambridge, comparable except that it is closer to the Pittsburgh International Airport and enjoys brisk tourist traffic at its Old Economy Shaker Village (both economic plusses), experienced a 30% decline in private building-permits issued during the same period of time. Nearby Beaver Falls, also comparable except that it is less hilly than Aliquippa and is the county seat (again, economic plusses) experienced a 7.2% decline during the same time period. In July 1993, the Aliquippa School District adopted a two-rate building-to-land property tax. Its new private construction & renovation thereupon spurted: for 1994-95, it was 2.3 times greater.

(5) In 1989, Clairton, Pa., an industrial suburb of Pittsburgh, was under direct state fiscal control, officially labeled "financially distressed." It took the advice of the prestigious Pennsylvania Economy League and adopted two-rate LVT. Building assessments were taxed at 2.105% and land assessments at 10% (instead of both at 3.7%). During the three-year period after the switch, its taxable building permits were 8.5% more than in the three years before (based on building-permit records in Clairton City Hall). This is to be compared to the 5.8% decline in all U.S. building permits issued during the same time. (The Clairton School District made a major tax shift from buildings to land. Results so far: as predicted, higher building permits)

Economic Incentive Effects: Penn. and Other Cities Using Land Value Taxation

(6) Oil City, Pa. adopted two-rate LVT starting in January 1989. Its private construction & renovation increased 58.2% in the three following years as compared to the three-years before, while its nearby one-rate but otherwise comparable neighbor, Franklin, experienced a decline of 12.2% in the same time period.

(7) Pittsburgh, Pa. increased its land tax rate (but not its building tax rate) in 1979 and 1980; its building-permit issuance then became 3.57 times higher than in the previous years of 1974-1978 (source: Pennsylvania Economy League 1985 study, p. 16 chart) despite a steady decline in its steel industry. Compared to this 3.57 increase, U.S. office-building permits increased only 1.6 times (neither increase adjusted for inflation). In 1984, Pittsburgh again increased its land tax but not its building tax. In the following two years, its new construction & renovation increased 6.2 times faster than U.S. construction & renovation (sources: City of Pittsburgh building-permit annual reports and table 1194, U.S. Census report C30), again despite the continuing decline in Pittsburgh's steel industry. Pittsburgh's 1985 building permits increased 2.29 times over 1984; in 1986, they were 2.38 times greater than in 1984 (source: Pittsburgh Bldg. Inspection Dept.).

(8) Godfrey Dunkley, an economist and mechanical engineer, extracted statistics from the official Municipal Yearbooks of the government of South Africa. He compared 1959 building assessments to 1979 building assessments and found that the one-rate towns (taxing land and buildings the same) increased their total assessments by 486%, but the two-rate towns (taxing land more than buildings) experienced a 561% increase; the 46 towns that taxed only land assessments experienced an 850% increase. Inflation affected all these figures equally, but note that the more a town taxed land values, the faster it grew. Further substantiation from the same study: the eight towns that switched from one-rate to two-rate increased their building assessments by 748%, and the 15 towns that switched to land-taxing-only increased their building assessments by 996%. A later Dunkley study of a different time comparison yielded similar figures.

(9) Then there's the study by professors Wallace Oates and Robert Schwab, both of the University of Maryland. They reported that 15 large northeastern cities in the U.S. averaged a decline of 15.5% in their annual value of building permits issued between 1960-1969 and 1980-1989, but two-rate LVT Pittsburgh recorded a 70.4% increase. Columbus, Ohio was the only other city in the study that recorded an increase – a rather modest 3.6%, but it had annexed some fast-growing suburbs in the interim.

(10) In 1995, Professor Nicolaus Tideman of Virginia Tech University and his graduate student, Florenz Plassmann (now a professor at the University of Binghamton) completed a highly technical study of land value taxation in Pennsylvania entitled "A Markov Chain Monte Carlo Analysis of the Effect of Two-Rate Property Taxes on Construction". It was published in the peer-reviewed *Journal of Urban Economics* (3/00, pp. 216-47) and concluded as follows: The results say that in all four categories of construction, an increase in the effective tax differential is associated with an increase in the average value per permit. In the case of residential housing, a 1% increase in the effective tax differential [on land] is associated with a 12% increase in the

average value per unit...From the perspective of economic theory, it is not at all surprising that when taxes are taken off of buildings, people build more valuable buildings. But it is nice to see the numbers." This study completely confirmed all the Pennsylvania studies that had been done at the time (then 15, now 21).

(11) Harry Gunnison Brown, a prominent American economist, found that the suburbs of Melbourne (Aus.) which were about five rail miles from Flinders Street in downtown Melbourne and which taxed land values only, had 50% more dwellings constructed per available acre during 1928-1942 than similarly situated suburbs which taxed land and buildings at the same rate (source: Aus. govt. statistics). Making a similar comparison for suburbs seven miles out, the land-value-tax suburbs did 2.33 times better; LVT suburbs 9.5 miles out did twice as well. Suppose you own some vacant land and you read in the newspaper that the tax on land will be gradually increased in the ensuing years, wouldn't you develop that land or sell to someone who will? So isn't it a tax that creates development and jobs?

(12) A Pittsburgh City Council study (1976) concluded that a 1% earned income tax would hit the city's homeowners 3.59 times harder than an equivalent-in-revenue LVT increase. If land were taxed, 73.6% of homeowners would pay less; all non-landowning tenants would pay less apartment rent in the long run.

(13) A Washington D.C. council-authorized study done in the 1970s concluded that if only land was taxed (not building assessments), there would be these tax reductions: single family homes 18.1%, two-family homes 20.9%, row houses 14%, walkup apartments 8.9%, elevator apartments 22.5%.

(14) In 64 suburbs outside central Melbourne from 1955/56 to 1957/58, there were 42 new factories, of which half were in the 17 suburbs using only a land tax. Factory employment in these 17 LVT-only suburbs increased by 445 whereas in the other 47 suburbs, factory employment decreased by 361 (source: Aus. govt. statistics).

(15) Twelve studies in rural Victoria found that the LVT-only towns averaged a construction-and-renovation growth of 29% as compared to a 2.6% growth for their real-estate-income-taxing neighbors in the same period of time (source: Aus. govt. statistics). The land tax was always adopted as a result of a poll of landowners only.

(16) If eastern Americans fall through the earth, they would emerge near Perth, Western Australia (pop. 400,000). 17 nearby localities taxing land values only experienced a 34.36 increase in the total number of dwellings between 6/30/71 and 6/30/76. The nine nearby localities taxing both land and buildings (presumably subject to the same economic-growth influences) experienced a 0.02% decrease in the same time period (source: Aug. govt. statistics).

(17) In North Dakota, farmers paid no tax on farm buildings. A survey by a high official of the North Dakota League of Cities revealed that this encouraged new farm construction (U.S. News & World Report, 4/3/78, p. 54).

(18) California Irrigation Districts – a 1909 California law required that new irrigation networks were to be financed by a tax on the affected land values only; all privately owned improvements were to be property-tax exempt. The theory was that irrigation networks increased land values, so the expense of those networks should be borne by the affected landowners. The result was beneficial to the local farmers, particularly the smaller ones. The irrigated valleys are among the most productive in the world. This is what the Modesto Chamber of Commerce stated in 1914 (according to a 1978 Congressional Research Service study, “Property Taxation,” p. 48): “As a result of the change many of the large ranches have been cut up and sold in small tracts. The new owners are cultivating these farms intensively. The population of both country and city has greatly increased. The new system of taxation has brought great prosperity to our district. Farmers are now encouraged to improve their property. Industry and thrift are not punished by an increase in taxes.”

(19) Malvern, Australia experienced a marked construction spurt after it adopted LVT-only in August 1955. The most extensive construction took place in its blighted problem neighborhoods: before August 1955, those neighborhoods accounted for only 22% of the city’s building permits, but in the five ensuing years that percentage jumped first to 35% and then steadily moved up to 47% in 1960 (these percentages are of continually larger construction figures) – per Victoria Bldg. & Construction Journal.

(20) In New Zealand in the late 1950s, ten large land-taxing-only cities had slightly less tax defaults than three large non-LVT cities, indicating that tax defaults are likely to decrease if buildings are not taxed so much (H. Bronson Cowan, 1961 report of the Canadian Federation of Mayors and Municipalities, p. 31).

(21) A city-funded 1980 study in New Castle, Pa. revealed that seven vacant and two poorly developed downtown sites would be an estimated \$150,851 more profitable to build upon with a land-tax-only property tax. If county and school taxes were also to tax only land values, then the extra profit would approximate \$243,750 a year.

(22) Random-sample studies in sixteen U.S. cities substantiated that most homeowners would pay less with a two-rate building-to-land property-tax shift. We can tell you how to exactly ascertain how each voter would fare with this gradually implemented tax on land values before going public with the idea; you can look before you leap.

(23) The Best Study of Them All: Pittsburgh had been taxing land assessments more than building assessments ever since 1915, but in 2001, it reverted to taxing both types of assessments at the same rate. Why did the city do that? Briefly, the well-to-do voters in Pittsburgh were suddenly aroused to fever pitch about their property tax as never before because a county re-assessment increased their land assessments by five-to-eight times overnight – an absolute political no-no (most county council members lost their next election). These voters thought they would pay less if they got the land tax rate brought down to the building tax rate, so they pressured the city council to reduce the land tax rate; they were completely unaware of the many Pittsburgh studies supporting land value taxation, and of course the property tax of most homeowners in the city shot up.

>>>>>>> After the two-rate rescission, Pittsburgh's private new construction (now more taxed) declined 19.57% (inflation-adjusted) in the three years after rescission as compared to the three years before, while the value of construction nationwide increased 7.7% (also inflation-adjusted). A computer examination of the entire Pittsburgh assessment roll found that the rescission caused 54% of all homeowners to pay more property tax. As for non-landowning tenants (office tenants also), eventually they all paid more space-rent because more building tax was passed on to them but the land value tax never can be. Since big cities generally have many tenants (both residential & business), they would particularly benefit from a building-to-land property-tax switch. This LVT rescission has actually been a blessing in disguise because it enables us to examine the effects of a land-to-building tax switch.

<http://www.urbantoolsconsult.org/Tax-Reduction.html>