LAND USE PLANNING
AND THE PROPERTY TAX

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Jackson E. Sullivan, Jr.

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SUMMARY

The purpose of this study was to examine the role that the property tax plays in land use planning. The emphasis of the study is to examine the property tax in its economic role in land utilization decisions. Through analysis of existing studies and interviews with various officials in state and local government, recommendations were made regarding guidelines which could be used in developing tax policies.

The data and information developed and/or utilized by this study came from a number of sources. Many reference works were used to establish what is known or theorized concerning tax/land use relationships. Various uses of the property tax to influence land use decisions were selected and studied through the case study approach. In these examples, the emphasis is placed on determining how effective the property tax is in influencing a land use decision rather than an examination of the quality of the land use activity after development has occurred. The case studies selected were: the homestead exemption to study the tax effect on homeownership; the industrial tax exemption as it affects industrial location; the use of tax abatements or an assessment freeze on central city renewal programs; the use of preferential assessments to preserve open space in suburban fringe areas, and; the use of land value taxation to influence overall urban development.

Although the evidence concerning the effect the property tax has on land use decisions is very mixed, there are definite steps and procedures the planner should utilize in formulating tax proposals designed to influence land use decisions. These guidelines are outlined in the final chapter of the study.

CHAPTER I

INTRODUCTION

The purpose of this study is to provide planners and local government officials with an understanding of the part the property tax plays in land use planning; to provide an appreciation of the complexities involved in utilizing the property tax to achieve land use objectives; to analyze and evaluate leading examples of property tax as related to land use planning programs; and, to offer recommendations to local officials and planners alike which will provide them with guidelines in developing appropriate tax policies.

General Importance of Work

Many factors play a part in the economics of land utilization. Because of its impact at the local level, the property tax exerts direct and indirect influence over land use economics. Since the property tax is one significant factor in land use decisions, planners should insure that property tax policies do not work against desired land use objectives, and if possible should be molded to work toward such objectives.

At present, there is inadequate groundwork to properly discuss many critical tax/land use relationships. In addition, planners are generally not very knowledgeable in tax

matters. This study will provide the planner with an adequate knowledge of the property tax, how it has been used in other areas to achieve land use objectives, and the considerations necessary in developing a tax/land use program.

Methodology

The methods used in this study were: (1) a review and analysis of the existing literature on the property tax; (2) personal and postal interviews with various officials in state and local governments to learn more about specific tax/land use programs; and, (3) analysis of literature, statutes, and data provided by state and local governments concerning individual tax programs.

CHAPTER II

NATURE OF THE PROPERTY TAX

Before attempting to delve into the use of the property tax in land use planning, it is necessary to provide an understanding of the tax itself. This chapter presents an examination of the property tax in its historical perspective. The significance of property taxation in relation to local government is also analyzed. Finally, in order to place the property tax in perspective in land use planning, a survey of the development problems resulting from the tax and the various reform proposals to mitigate these effects are presented.

Property Taxation in the United States

The use of the property tax occurred early in American history. In colonial America, the chief taxation consisted of various excise taxes. In New England, however, property taxes called "faculty" levies were assessed on land, livestock, and other assets of the colonialists. After the American Revolution, the property tax greatly expanded as a revenue source for local government. Westward expansion and the addition of new states and territories created an abundance of land. Land became a general indication of

wealth and, consequently, was the primary source of tax revenue.[1]

During the eighteenth and nineteenth centuries, the property tax in the United States gradually became a general tax measured by the value of all types of privately owned assets. This period was characterized by attempts to apply the principles of democracy and equality to taxation. Democracy in taxation took the form of an all-inclusive general property tax which included numerous forms of personal and real property. The equality concept found its way into most state constitutions by 1900 through the adoption of uniformity clauses. Such provisions were intended to insure that all property was taxed at the same rate.

It soon became apparent that to tax all forms of property uniformly and at an equal rate was an administrative impossibility. Therefore, since 1900 no states have adopted uniformity clauses, and several have repealed them.[2] The difficulty in tax administration resulted because of inherent differences in types of property. Consequently, by virtue of administrative necessity, distinctions in property were made according to different bases. The most important of these is between <u>real</u> and <u>personal</u> property.

There are several standards by which the distinctions between real and personal property may be drawn. However, for practical purposes, real property consists of land and its physical improvements, such as buildings. Personal

property may be divided into tangible and intangible categories. Tangible personal property includes household effects, factory and farm machinery and merchandise stocks. Intangible personal property includes securities, mortgages, and credit instruments.[3] In discussing the property tax, it should be kept in mind that the general property tax includes taxation of both real and personal property while a tax only on land and improvements refers to a real property tax.

Reduction of the Property Tax

While the eighteenth and nineteenth centuries evidenced a gradual buildup of the property tax base, the twentieth century has been characterized by a general reduction or breakdown of the property tax base. As one can readily ascertain, personal property is very mobile and easily hidden from the tax administrator. Real property, however, is relatively immovable, and for all practical purposes, impossible to hide. Consequently, inequities in the administration of the general property tax soon developed. In effect, the tax penalized those who were honest in reporting taxable assets and rewarded those who were not.[4]

Movements to reform the property tax resulted in many changes to the system. Chief among these administrative reforms was the classified tax movement. The goal of the movement was to classify various types of property and tax each class at a different rate. The uniformity clause prevented classification in those states which had adopted such

provisions into their constitutions or had provisions which has been so interpreted by the courts.

By the early part of the twentieth century, Pennsylvania, Connecticut, Maryland, Alabama, and Virginia had all adopted legal measures for classification. Since that time, some degree of legal authority to classify property has spread to at least 30 of the states and the District of Columbia. The remaining states either have rigid uniformity clauses preventing classification, or, the language of their consitutions is insufficiently clear to determine if the state has the authority to classify property until the question has been settled in court.[5]

Further reductions in the general property tax have occurred through the use of exemptions. Although exemptions will be covered in more detail in this report, some mention should be made at this time to indicate generally the type of exemptions granted. Several states have exempted all or portions of personal property. Real property has been removed from tax roles by homestead exemptions in some states. Institutional and philanthropic institutions have also been granted full or partial exemptions of property value in most states. Exemptions to industry on both real and personal property have been used--especially in southern states. In addition to these exemptions, many other exemptions have been granted to various projects and interest groups for reasons ranging from military service to development incentives.[6]

Summary

In perspective, it can be readily seen that the property tax is an old institution. It has been used widely throughout the United States since this nation's inception and has yielded to change only over a long period of time. Further, because of the importance local government plays in our system, the property tax has developed into a complex collection of tax systems with thousands of local variations rather than as a single national tax.[7]

The American system of property taxation has followed a pattern of development somewhat like other societies in that it began as a tax predominantly on land. As different forms of wealth accumulated, these were added to the tax roles until a general tax on all forms of property resulted.[8] The basic inequities of such a system and the problems it presents for tax administration have resulted in a general reduction of many of the forms of wealth from the property tax base. For all practical purposes, the property tax today is one chiefly on real estate, business equipment and inventories.

Significance of the Property Tax Today

The property tax would merit little attention if it were only a minimal revenue producer, or restricted in its application to only a few jurisdictions in this country. However, just the opposite is the case. As this section will

point out, the property tax has almost universal application in local governmental jurisdictions. Further, it will be demonstrated that the property tax plays a dominant role in the fiscal systems of local government.

Preemption by Local Government

The fact that local governments have evolved as almost the sole users of the property tax has been caused in part by its abandonment by other levels of government. However, the continued heavy reliance on the property tax by local governments has come about by design in most instances. The power to levy taxes at the local level is derived from the state, and such power is usually delegated by specific state legislation.[9] Before World War II, very few local governments were permitted to levy nonproperty taxes. Since states themselves are hard-pressed to raise revenues they tend to resist incursions by local governments into their tax sources.[10] Therefore, local governments have had little choice in the matter of using the property tax, since it has historically been the main source of revenue open to them.

Since Work War II, the fiscal burdens placed on cities have caused new revenues to be channeled into local governments by way of new tax sources and through state and federal grants. New tax sources for local government include sales taxes, personal income taxes, commuter or payroll taxes, as well as a diverse number of other taxes. The

relative importance of each source of revenue is shown in Table 1.[11] Of all sources of revenue open to local governments, the property tax, as an aggregate, is still the most productive.

Pervasiveness of the Property Tax

The property tax plays a dominant role in the fiscal systems of local government. Of the $308.3 billion of revenue collected by all governments in 1971-1972, 42.8 billion was derived from property taxes. Of the $42.8 billion, 97.1 per cent or $41.6 billion was classified as local revenue. State property tax collections made up the remaining 2.9 percent.[12] When general revenues for local government are allocated according to source, the property tax provides 43.2 per cent of all revenue for local government.[13]

The property taxing power is available to the vast majority of local governmental units. In 1972, there were 78,218 units of local government. These includes counties, municipalities, townships, special districts, and school districts. Of these, only 12,304 or 16 per cent were without property taxing powers. Virtually all without property taxing powers were special districts which relied entirely on other revenue sources for current financing.[14]

Local governments not only rely heavily on the property tax in general for revenues, but of the property taxed, real estate comprises the largest component. In 1972, the combined value of locally assessed real and personal property

Table 1. General Revenue By Source For Local Governments
1971-1972
(millions of dollars)

REVENUE SOURCE	TOTAL	LOCAL GOVERNMENTS				
		Counties	Municipalities	Townships	School Districts	Special Districts
Intergovernmental Revenue	39,694	9,956	11,528	878	17,653	1,550
From Federal Government	4,551	405	2,538	51	749	808
From State Government	35,143	9,252	8,434	781	16,471	205
From Local Government	--	299	556	45	433	538
General Revenue From Own Sources	65,549	13,695	23,471	3,105	21,603	3,679
Taxes:	49,739	10,076	17,009	2,765	18,939	952
Property	41,620	8,625	10,937	2,584	18,572	903
Sales	4,268	899	3,191	62	68	49
General Sales	2,727	751	1,873	--	62	41
Selective Sales	1,541	148	1,317	62	6	8
Income	2,230	192	1,881	26	132	--
Motor Vehicle Licenses	225	111	114	--	--	--
Other	1,396	249	887	93	167	--
Service Charges	15,810	3,619	6,461	339	6,664	2,727
Miscellaneous	4,742	922	2,560	177	590	492
TOTAL	105,243	23,652	34,998	3,982	39,256	5,229

Source: U. S. Department of Commerce, Bureau of Census, 1972 Census of Government, Government Finances Table 3, p. 26.

was $664.2 billion. Of this value, the real property component was $572.9 billion or 86 per cent of the total assessed property values.[15]

Although it can be generally concluded that the property tax plays a fundamental role in local government finances, it should be pointed out that heavy reliance on the property tax is not evenly distributed among state and local governments. Interarea differentials are quite evident between states. In 1972, property tax revenues ranged from 15 per cent of state-local tax revenue in Alabama to 59 per cent in Nebraska.[16]

Regional influences appear to play some part in reliance on the property tax. This may result from similar economic, cultural and historical influences in each region. Reliance on the property tax is relatively high in New England as well as the Great Lakes states; the northern Plains states rely very heavily on property taxes; percentages in the mountain states and in the West are mixed while in the South, much less reliance is placed on the property tax.[17]

Summary

The significance of the property tax in local government finances is evident. Not only is the tax substantial in amount, but its use is universal among counties, cities, townships, and school districts. The only units of local

government not having the authority to levy property taxes appears to be special districts. Although heavy use of the property tax is the general rule, particular areas rely much less on the property tax than others. This occurs primarily in those states which have authorized local governments to levy other taxes such as sales, income or payroll, and/or have provided additional revenue to local governments through grants. Attitudes of state legislators appear to be changing, yet states have historically been reluctant to allow local governments to tap state tax sources and have preferred to supplement local needs with grants. Finally, it has been shown that of the property taxed, it is the real estate component which bears the greatest burden.

Problems Resulting from Real Property Taxation

The literature concerning property taxation can only be described as overwhelming in magnitude. Equally overwhelming is the adverse comment concerning the administrative and substantive defects of the tax. Jens P. Jensen, a noted authority on property taxation has stated that "If any tax could be eliminated by adverse criticism, the general property tax should have been eliminated long ago."[18]

The two areas of criticism of the property tax refer to administrative and substantive defects. Both areas have important economic and developmental effects on land use, and both will be addressed in this section. The

literature criticizing the tax covers a great many aspects not directly pertinent to this thesis. Consequently, this section will expand only on those points having a direct bearing on the impact the property tax exerts on land use and development in the urban area. In addition, a general discussion will be presented concerning various reforms which have either been implemented or suggested to rectify the shortcomings of the property tax.

Administrative Problems

Of all the procedural problems involved in property tax administration--and they are substantial--there are two areas that have significant ramifications for land use and economic development of the urban area. These two areas of concern are the fragmentation of taxing units and assessment administration.[19]

Fragmentation of Taxing Units. As mentioned, there were 78,218 local governmental units in 1972. Of these, only 16 per cent or 12,304 were without property taxing powers. Although many local governmental units are combined for property assessment purposes, the actual tax rate is determined by each jurisdiction. This large number of taxing units, especially in metropolitan areas, indicates that the size of such units are relatively small. Because of the great number and smallness of taxing jurisdictions, it is probable that wide disparities exist in the level and composition of the tax base as well as the tax rate.[20]

Dick Netzer, an imminent scholar in the field of property taxation, found that per capita assessed values exhibited a 15:1 range for 91 municipalities in the Chicago metropolitan area in 1957. Municipal tax rates reflected a 7:1 range. Similar statistics have been developed from studies in New York City, Cleveland, and New Jersey.[21] Netzer concludes that fragmentation has resulted in an impact on the location of business and industry within a metropolitan region. He suggests that where other factors are approximately the same, taxation may constitute the only significant cost differential.[22]

Fragmentation of taxing units has also created a wide variation in the burden of taxation among taxing jurisdictions. Such differences have important effects on urban development. First, relative tax wealth permits variations in the scope and quality of public services. This diversity in public services has been challenged in the courts recently in California and New Jersey where educational quality varied widely as a result of differences in the wealth of property tax jurisdictions.[23]

Second, since rich communities have a superior tax base to draw upon, they may spend more than poorer communities but in fact enjoy a lower tax rate. Low tax rates tend to encourage economic activity to locate in low-tax jurisdictions whether or not such locations are good for the community.

Because of the interaction of taxation and location, many communities have actively planned their land use based on fiscal advantage rather than on broader community or area considerations. This practice of "fiscal merchantilism" attempts to export service costs, such as school children, and import tax base, such as industry, commercial enterprise, or high value residential uses. Although these attempts may result in a new increase in tax revenue, seldom do they solve any problems for the metropolitan area as a whole.[24]

Assessment Administration. Part of the same general problem of fragmented governmental units is that of assessment administration. In order to assess individual properties, the value of the property must be determined. Usually, this can accurately be done only at the time of an actual sale. Consequently, the assessor, under most circumstances, must approximate the true value. This procedure admittedly is difficult, but it is generally concluded that the quality of assessment administration in this country has been quite poor for many years. This fact has been well documented in studies conducted by Harold S. Buttenheim[25] during the 1930's and more recently in the 1960's by Dick Netzer.[26]

Netzer has reduced the criticisms of assessment administrations to three salient points:[27]

1. Within individual assessment districts even the most homogeneous and presumably the most easily assessed

class of property--single-family nonfarm homes--is assessed at widely varying fractions of market value.

2. Within individual jurisdictions, differing types of property are treated differently by assessors. This may result from incompetence on the assessor's part or through design.

3. Assessment practices and levels of assessment differ among assessment jurisdictions within a single county or state.

Differential treatment of property classes can and has served as an impediment to the development of those types of property which have received unfavorable treatment. In addition to the inequities incurred, the uncertainty involved in such treatment is detrimental to new development.

Administrative Reform Proposals

Many reformers of the property tax advocate outright abolition of the institution itself, because it has become almost impossible to administer properly. It was reasoned that the revenue produced by the property tax could be totally replaced by other revenue sources. Although many local governments have and will continue to utilize other sources of revenue, it has become increasingly clear that none of these would be able to raise the amount of revenue now derived from property taxation. Consequently, serious reformers now lean toward trying to make the existing property tax institutions work better. Most notable among the

recommendations to improve administration of the tax are the following: professionalization of the assessing profession; centralization of tax administration toward or closer to the state level; and clarification of existing state laws.

Professionalization. In many jurisdictions, it is possible to hold the position of assessor even though an individual's knowledge of the profession is extremely limited. This trend is changing. Professional assessors and various state and national assessor organizations have been forceful in advocating minimum requirements for assessors. The states of Oregon, California, New Jersey, Tennessee, and Kansas have established statewide qualifications for assessors. Several other states are considering such measures.[28]

Training programs for assessors now exist in all states. Since 1965, the International Association of Assessing Officers has been actively engaged in conducting training programs. The states of Tennessee, Florida, Illinois, and Kansas have established state schools for assessors.

Increased professionalization of the assessing function has also led to increased efficiency through computerization. In addition to normal clerical functions, computer applications have been made on the following: mass computation of individual appraisals; statistical studies to test the quality of assessments; annual reappraisals, and; the collection and maintenance of a data bank.

Centralization. Fragmentation of taxing units, and, in some cases, overlapping of various assessment districts, have led to a movement toward centralization of tax administrative functions. The Advisory Commission on Intergovernmental Relations has recommended that where feasible, tax administration, including assessment, should be centralized at the state level. However, if a more diffused system is sought to maintain local autonomy, assessment districts should be organized to the extent required to give them the size and resources they need to become efficient assessing units. No assessment district should be less than county-wide, and all overlapping districts should be eliminated.[29]

Laws. The efficient administration of the property tax depends heavily on how well the assessor performs his job. Yet even with an assessor of great ability, the administrative task will probably have poor results if tax laws are unclear and are cluttered with diverse legislation accrued over the years. States have increasingly become aware of the need to reexamine property tax laws which are archaic, conflicting, and in some cases unworkable.

Of course, all states are not the same in relation to what each had accomplished in property tax administration. In 1957, for example, New York State completely overhauled and recodified their property tax law. The State of Texas conducted similar studies into their tax laws in 1961.[30]

Since World War II, many states have undertaken equalization programs to determine the accuracy of assessment in each district or county. As of 1965, 40 states have undertaken equalization programs.[31]

Substantive Problems

While administrative difficulty with the property tax has a long and well-researched heritage, substantive problems dealing with the intrinsic nature of the property tax have only recently received detailed and systematic research. Prior to 1962, very little empirical evidence concerning the economic and developmental effects of the property tax was published. Most notable among these early works are Jens P. Jensen' 1931 landmark work, Property Taxation in the United States, and a study directed by Harold S. Buttenheim for the National Resources Committee in 1939 on "Urban Planning and Land Policies."

In 1962, the Urban Land Institute began publication of a series of research monographs addressing the effects of taxation. This series appears to be the first major group effort since 1939. Over the years, but especially since 1960, many individuals have contributed to the general knowledge concerning taxation. However, most serious contributors to the field readily concede the need to continue to gather and analyze data on the property tax, since present knowledge is incomplete in many areas of concern.

With the above qualification in mind, this section will present many of the theories concerning the detrimental effects of the property tax on land use and development. Proposals for reform of the substantive defects of the tax are also discussed.

Effects on Land Use and Development. The impact of the property tax on land use and development has produced major problems primarily in two types of locations within the urban area: (1) the urban core, and (2) the urban fringe. The urban core areas are characterized by aging and deteriorated structures surrounded by equally low value residential uses which result in a poor market turn-over of real estate. Usually, high tax rates and low property values per capita prevail. The urban fringe areas on the other hand are under relentless pressure because of rapid population growth and service needs. The market, as a result, is very strong. However, rapidly rising tax rates exist in spite of a rapidly growing tax base.[32]

Important to these conditions is the fact that usually, if not always, there is a lag between the market measure of value as indicated by sales, and the actual tax assessment on the property. Consequently, in neighborhoods where the market is falling taxes tend to be too high and in areas where the market is rising, taxes tend to be too low. In effect then, the property tax works adversely where the market is weak, and helps areas where the market already

is strong.[33] Within this market concept, the interrelationships of tax-land use problems are more easily understood. The most important of these problems are discussed below:

1. Housing--The property tax on housing is analogous to that class of taxes commonly called consumption taxes. The burden of taxation appears to rest on housing consumers, whether they are owner-occupants or tenants. An exception to this is the portion of the property tax which falls on the land underlying the buildings. In rental property, this portion of the tax must be capitalized and therefore theoretically would not be passed on to the consumer. However, for the country as a whole, probably over 90 per cent of all property taxes on housing are borne by the consumer.[34]

What the property tax burden on housing consumers means is a substantial increase in housing costs. These costs when computed to a sales tax equivalent amount to 20 per cent or more for the country as a whole. For example, in 1960, 3.6 million multi-family dwelling unit households were subject to rates of 20 per cent or more, and 1.2 million in this type of housing were subject to rates in excess of 33.3 per cent.[35]

This condition is especially important when considering the housing needs of the poor. Considered as a consumption tax, the property tax is heavily regressive, because it absorbs a much higher fraction of the incomes of the poor than of the rich. This is so because housing expenditures

constitute such a large percentage of the budgets of poor families. The situation is further complicated by the fact that the poor tend to locate in central cities where tax rates are normally highest.[36]

The general effect of the property tax on housing is twofold. First, because the tax increases the cost of housing to the occupants, it effectively places a significant portion of the housing stock beyond the economic reach of the low-income population. Second, high property taxes generally discourage investment and consumption of housing by the entire population. As in most other items of consumption, studies have shown that consumers will buy more and better housing if the price is lower.[37] Further evidence in New York City indicates that increased investment in the housing stock will radically improve the housing conditions of the poor. Under conditions which increase the housing inventory, prices tend to decrease, and turnovers tend to increase. Both of these conditions serve to give the poor more choice in the housing market.[38]

As a final comment on the property tax and housing, it should be pointed out that property taxation deters improvements--expecially to the central city housing stock. The problem here lies in increased assessments as improvements are added. In many cities, assessors are aware of this problem, and consequently heavily discount any

improvements. However, a few case studies of the problem indicate that fear of potential tax increases effectively deter improvements to many central city properties.[39]

2. Non-Residential Land Use Location--During the last several decades, there has been much discussion concerning the effects of taxation on the location of economic activity. This relationship has spurred many states, especially in the South, to utilize exemptions or tax abatement plans as an economic incentive for industries to locate in their jurisdictions. Most analysts, however, have found that tax differentials have little impact on location because it represents such a small outlay relative to other costs of doing business.

However, these studies dealt with states or regions as their units of observation. But within a single metropolitan area, it has been found in some cases that the only significant cost differential was taxes. In the New York City area for example, a study conducted in the 1950's revealed substantial variations between local jurisdictions. In most instances, the central city held a highly unfavorable economic position in relation to its suburbs. More recent studies have shown that this unfavorable position has stimulated decentralization of economic activity away from the central city.[40]

Two important points should be emphasized here. First, tax differentials may trigger decisions to move

away from the central city, but usually only in those instances in which it would have occurred anyway. The results has been to speed up relocation. Nevertheless, it is an economic loss to the city. Second, not all economic activities are equally susceptible to tax differentials. Many activities require a central city location, such as corporate headquarters, banks, and newspapers. Other activities must remain in the central city, because they sell services to it, such as special types of public utilities.[41]

Although the effects of property taxation on housing and the location of economic activity are the most important, the property tax does have significant effects on specialized forms of land use activities and development.

a. Utilities--Some industries, particularly certain public utilities, bear a heavier burden from property taxes. For example, because of the property taxes paid on gas utilities, gas rates are increased to consumers relative to the prices paid for fuel oil. In New York City, it is estimated that the property tax on natural gas real estate results in a 10 per cent increase in price. Since both fuel oil and natural gas are priced about the same, the property tax on natural gas appears to be a real deterrent to gas use over fuel oil.[42]

b. Transportation--It is well known that railroads carry a substantial property tax burden compared to other forms of transportation. This results from the fact that

railroads own their own rights-of-way. Since these modes of transportation are regulated, the taxes show up in rates to users, thereby encouraging use of non-railroad modes. This action has probably helped to decentralize industrial activity away from central cities, since one of their past advantages was superior rail freight facilities.[43]

3. Suburbia and the Fringe Area--Tax problems evidenced in the suburbs have resulted mainly from the rapidly increasing tax rates necessary to stay abreast of population and service needs. This continually advancing tax burden has led many jurisdictions into "fiscal zoning" and other such measures to increase their tax base at the expense of other areas. Of importance here, is the problem associated with the advancing edge of suburban development commonly called the fringe area. Two problems of concern associated with the fringe area are premature conversion of land and speculative withholding of land.

Increasing tax rates on the urban fringe caused by new development have reduced net income for farmers. Because of this, conversion of farmland to urban uses has been speeded up. Although the conversion may have been premature, the general effect has been to force marginal farms to leave the industry and migrate elsewhere.[44] Generally, premature conversion has resulted in the following: (1) removing land form productive uses while waiting for the urban land market to "ripen"; (2) resulted in land subdivision and development

which is beyond the service capabilities of the local jurisdiction, thereby requiring abnormal public expenditures, or; (3) effectively reduced open space around the urban area.

Although increasing property tax rates in the fringe area adversely affect the marginal farmer, seldom do these same rates adversely affect the speculator. Taxation is no match for speculation in a land market where values are rising. The impact of taxation is negligible because the fringe area is normally characterized by rapidly increasing land values, and the lag in assessment allows the speculator to hold the land for a period of time before he is taxed at its increased value. The large increment in capital value which the speculator hopes to obtain renders the annual cost (property tax) of holding the land negligible.[45]

Generally, speculative withholding of land leads to "leapfrog" development, which fosters urban sprawl and increases governmental expenditures to meet service demands. As a result, services are often impossible to schedule with development.

Substantive Reforms

Two broad categories of reform have been suggested to alleviate or at least minimize the equity, efficiency, and over-all economic defects of the property tax. These two avenues of change suggest (1) modification of the structure of the property tax, but still levy on the basis of property, or (2) shift more of the burden of local taxation on non-property taxes.[46]

Modify the Structure. In suggesting different structures for property taxation, a spate of alternatives have been presented. Among the most prominent of these are the following: the land value tax; an incremental tax on land values; income versus capital basis for taxation, and; a hybrid basis--earnings plus capital value. Each of these will be discussed below:

1. Land Value Tax--In 1879, Hentry George, a journalist, advanced the theory that a single tax on land would solve the inherent inequities of the property tax.[47] Since Henry George advocated a complete abolition of all taxes except that on land, few people took him seriously, and little is heard of an outright single tax today. However, the argument for a heavy tax on land coupled with an abolition or reduction in taxes on improvements, has particular appeal to economists as well as planners today.

Generally, the land value tax proposal would simply shift the burden of taxation from land and improvements to land alone. The ramifications this action would have on land use and economic development may be summarized under capitalization, holding costs, fixed costs, and unburdening effects.[48]

a. Capitalization--Through the process of capitalization, the result of a higher tax on land would be to lower its capital value.[49] The reduced price of land would serve many purposes in economic development. First, it would open

up the land market, and generally make land available to more investors. Second, it would lower the real cost of construction through lower land prices which comprise a part of the total cost of development. Third, it would allow the capital released by lower land cost to be invested into buying larger sites or making better improvements to the site.

b. Holding-Cost--Generally, the taxes on land would be the highest in those areas which command the best locational sites with the most economic potential. The taxes would be high regardless of the use of the land. This would force the owner to increase the intensity of use if it were under-utilized in order to increase his net income to offset the taxes. The owner may not have the necessary capital to invest in a more intensive use, and consequently would have to sell or lease the land to someone who could invest in order to escape the costs of the tax.

c. Fixed-Cost--The land value tax is based on the value of the site according to its location and development potential. It is not based on the use to which the land is put. Therefore, any increase in taxes is determined by an increase in the site potential, not by the addition of improvements or investment to the site. In reality, the tax per unit of improvement will go down as the land is developed closer to its potential. As a result, by remaining constant,

the land value tax encourages the development of land to its capacity without increasing the tax liability.

d. Unburdening Effect--The unburdening effect refers to the increased economic development as a result of removing the tax on improvements. Increased economic development would occur for much the same reasons as under the fixed-cost effect. Increased new construction and rehabilitation could be made without incurring an increased tax liability. Both serve to provide economic incentives toward developing land to its highest potential.

e. Corollary Effects--From the preceding discussion concerning the effects of a land value tax, several other particular consequences are usually mentioned in the literature based on the above principles.

(1) Urban Sprawl and Land Speculation--The land value tax, working through the fixed-cost and unburdening effects, would allow land to be developed more intensively. The holding-cost effect would serve to reduce speculative withholding of land, especially within the urban area by making the non-use of land too much of a burden. The capitilization effect would reduce the overall cost of building through lower land cost. The net effect, theoretically, would be to utilize the land more intensively, bring vacant land into use, and to bring about a more compact urban area.

(2) Slums--Because of land speculation and the increased tax burden incurred when improvements are made,

the present property tax inhibits the rehabilitation of slums by private enterprise. The land value tax, however, would relieve land speculation and remove the tax on improvements, thereby generating economic incentives toward private rehabilitation of slum areas. These same forces would apply to the construction of better quality housing stock in suburban areas.[50]

f. Problems Arising from the Land Value Tax. The arguments in support of land value taxation are impressive. In terms of being equitable, the land value tax seems to be socially desirable because it does not impose any increased tax burden on the persons desiring to make improvements to his property. Equity may also be established on the concept that the land tax only recaptures the increased value of land created by the community.

The land value tax is also held to be neutral in its economic effect on land use. This means that the property-holder may change the use of his land without altering his tax liability. The present property tax is not neutral since making improvements incurs an increase in tax liability.

Impressive as these arguments are, a review of the literature reveals some trepidation toward the operational consequences of the land value tax. Several of the arguments are summarized below.

(1) Land Speculation--An economic consequence of a heavy tax on land would be to curb speculative withholding of land. This premise has been attacked on the grounds that the extent to which the land value tax would curb speculation is in direct proportion to the burden of the tax. The burden of the tax should not be measured only in terms of the rate of taxation, but also in relation to the opportunities of the market. It is argued that in order to capture the gains of the speculator in a growing economy, the tax rate of land assessments would have to increase dramatically. Such high rates might force many small property owners into bankruptcy.[51]

Within the general content of most of the literature concerning land value taxation, it is almost universally assumed that land speculation is detrimental to orderly development. However, it has been argued that land speculation has served to conserve open space and to reserve land which could be utilized for a better use in the future.[52] Although this has probably been inadvertent, the economic and social benefits are no less real.

(2) Adverse Developmental Impact--In considering the development of an urban area, one must evaluate the impact that the land value tax would have on the social and developmental goals of the community. One impact on the small property owner has already been mentioned. However, other considerations must be weighed when the withholding of land is

not speculation at all but merely the desire to retain it due to social or other reasons. This may be especially true of neighborhoods containing the aged who either do not have the funds to relocate or desire to remain because of sentimental reasons.[53]

The economic forces released by the land value tax also spur a more intensive use of land as well as bring vacant land into productivity. Although the resulting compact urban form would probably yield governmental savings by inhibiting urban sprawl, thereby cutting service costs, it might also come into conflict with other community goals. For example, intensive urban development might be in direct conflict with a general community goal of open space preservation. These and other considerations of the land value tax must be examined to determine the effects of such a fiscal policy.

The land value tax has extremely powerful economic and equity arguments in its favor. Probably the most dramatic observation of the tax in light of its favorable espousal by most researchers is the fact that it has been largely ignored by taxing jurisdictions in the United States. To this author's knowledge, only four jurisdictions in the United States presently use land value taxation or some variant: the Single Tax Corporation in Fairhope, Alabama; the State of Hawaii; and, the second-class cities of Pennsylvania which include Pittsburgh and Scranton. Chapter IV of this

thesis will critically analyze these jurisdictions to further determine the effectiveness of the land value tax technique.

2. Increment Tax on Land Values[54]--Although the land value tax has occupied center stage in most studies concerning alternatives to the present property tax, other taxing techniques have been advocated, which possess the advantage of equity and also have powerful allocational effects. One such proposal used in Denmark and Spain is the taxation of land value increments.

The tax is imposed at the time the property is transferred from one owner to another. The tax is a percentage of the increased value of the land, since the last transfer. It would affect only those property-owners who had in fact realized a profit. If no profit were established, the owner would not be taxed. An added benefit is that no tax would be imposed until the owner actually had his money in hand. This would alleviate the inequitable problem with the present property tax in the United States in which higher taxes are charged during inflationary periods even though actual profit may not be realized.

The increment tax would have no tendency to disrupt the real estate market by stimulating or depressing buying at any particular period. Further, the increment tax would provide a continuous flow of money into the public treasury rather than on a periodic basis. This process might be

disruptive, however, if very little market turnover existed in a particular taxing jurisdiction. Assessment administration would be extremely easy because sales figures would always be available to compute the increase in profit.

Although the increment tax appears to contain many positive attributes, it has not been widely used, and even in those countries in which it has been used, it is not a major tax or a large revenue producer. Its defects have not been thoroughly analyzed to give a complete picture of the tax, and this fact probably accounts for its underuse.

3. Income Versus Capital Value Basis of Taxation--A method of taxation utilized by Great Britain and many countries following the British tradition is income rather than capital value as a basis for valuation. The British "rates," are taxes on the annual value of occupied real property. Taxable values are based on actual use of the property rather than the owner. If no rent or income is derived from the property, no tax is paid.

This system of taxation was heavily pushed in the United States during the 1930's as a way to adjust taxes to declining rents and high vacancies. However, after World War II and its subsequent real estate "boom," interest in the method declined. However, assessors in the United States appear to be relying more and more upon income as one measure of capital value.[55]

4. Earnings Plus Capital Values. One property tax reform proposal advanced in 1935 by Peter Grimm, a New York realtor, was the tax on land be based on capital value while the tax on improvements be based on earnings or imputed earnings.[56] This type of taxing procedure would get at the profits of slum owners which the present property tax does not. However, assessors would probably oppose the arrangement, because it would require separation of land and improvements for valuation purposes. This problem does not seem insuperable in view of favorable experience in other countries which have devised methods for accomplishing this task.[57]

Shifting Property Tax Burden to Non-Property Taxes.

The second avenue of substantive change has already occurred to a great degree in many jurisdictions. The substitution of other bases of taxation instead of property include a number of alternatives: (1) local sales or use taxes, including excise or gross receipts taxes; (2) local wage or payroll taxes; (3) local income taxes levied on residents; and (4) service charges (user-benefit charges) for municipal services.

These tax sources are in wide use by local governments. The adverse effects of the property tax have been mitigated to a large degree because the tax's market impact has been lessened through reliance on alternative sources of revenue. This is not to say that these other revenue

sources are without fault. The sale tax is notoriously regressive for example. Yet, they are becoming a more reasonable alternative to property taxation almost daily. However, the problem of revenue production for local governments is such that it is probable that none of these tax sources could completely take over the tax burden now shouldered by the property tax without a dramatic increase in tax rates.[58]

Prospectus

In attempting to assess the use of the property tax as a land use control, it is necessary to at least obtain some notion as to its continued prominence as a fiscal device of local government. Although one is hard-pressed to find anything complimentary concerning the property tax in volumes of literature spanning almost a century, the tax persists despite its shortcomings. This apparent paradox can probably be attributed to two salient features which reinforce continued reliance on the property tax: revenue production and local autonomy.

One of the most notable and vehement detractors of the property tax today is Dick Netzer. However, concerning the revenue production capacity of the property tax, Mr. Netzer states:

> The consequence...has been rapidly increasing property tax revenues, with only relatively modest increases in property taxes as a fraction of property values in the market. The indications, then, are that the property tax is and will continue to

> be an attractively productive source of local public funds. In view of its many faults, this attractiveness of the property tax is perhaps to be deplored rather than applauded.[59]

Local autonomy is another strong argument advanced in defense of the property tax. In part, this claim is founded on historical observations in the United States and elsewhere, which suggest that local government is most important where property taxation is heavily relied upon.[60] Regardless of whether this association is unavoidable, the administration of the property tax in the United States reinforces the traditional philosophy of local self-government. Consequently, the property tax continues to be a locally administered tax whose rates are generally set by locally elected legislative bodies. While the argument for local autonomy may not be valid, the tradition and philosophy it reinforces is still a potent political stumbling block to any radical reform of the tax and most assuredly to the abolition of the property tax.

In view of the extreme likelihood that the property tax will continue to hold its place of prominence in the fiscal systems of local government, it is incumbent on the planner to not only know how the taxation of property influences land use and development but also how to use this tool as one means of accomplishing planning objectives. With this goal in mind, the balance of this thesis will be directed toward discerning the parameters in which utilization of the property tax may be accomplished.

CHAPTER III

THE PROPERTY TAX AS A METHOD TO ACHIEVE LAND USE OBJECTIVES

The purpose of this chapter is to provide the planner with a general understanding of the considerations which must be evaluated in using the property tax to influence land use and development. Specifically, the chapter points out the salient characteristics of property tax incentives. Tax incentive measures are then discussed in relation to other subsidy methods. Finally, the legal constraints involved in using the property tax as an incentive to influence land use and development are examined.

Overview

Generally speaking, most attempts to use the property tax as a device to influence land use and development decisions have clustered around various "incentive" programs. Such proposals have usually meant some form of tax exemption, abatement or deferral of taxes. Seldom has the proposal for an <u>increase</u> in property taxes to regulate land use and development been utilized. Even in the literature concerning the land value tax, which would result in higher taxes on land, the emphasis of discussion has been on the elimination or reduction of the tax on buildings. This attitude and practice is understandable in view of the political

volatility of taxation in general and property taxes in particular.

Whatever the reasons, most incentive measures have resulted in a reduction in the tax burden in order to induce a desired activity. To point up this fact, Table 2 presents the results of a 1963 survey of 120 professional planners conducted by Donald G. Hagman,[61] Associate Professor of Law, University of California. The survey resulted in a compilation of tax measures recommended by the planners which could be used to aid in the accomplishment of planning objectives. Tax exemption, abatement, and deferral measures are prominent in the results of the survey. Tax increases as well as metropolitanization of taxes and conversion taxes are also mentioned. In practice, however, these tax measures are relatively rare.

Helpful though it may be, Hagman's listing does not provide the planner with much understanding of the mechanics of using each measure; nor does it aid the planner in determining which method should be used to accomplish a desired objective. To do this requires a more precise understanding of tax incentives. The following sections help provide this understanding by delineating the characteristics of tax incentives; by examining the legal implications of using a particular tax measure and; by setting forth some of the economic, social, and political arguments concerning tax incentives.

Table 2. Survey of Property Tax Incentive Measures

Tax Exemption

Public housing projects
Certain types of low- or middle-income housing
Home improvements
All structures
Public parking
All real estate
Industrial buildings

Tax Abatement

New construction
  Redevelopment projects
    Use same assessed value as before redevelopment
    Use proportion of present value as new assessable value
  Industrial plants
Support for agricultural zoning
Preservation of open space
  Outside municipal borders
    For recreation areas, parks
    Flood plains
    Holding for more intensive use--industrial sites
  Within urban areas--golf clubs
Historic buildings
Public parking
Freezing taxes on land during development stage

Tax Deferral

Preventing development of farms for other uses
Improvements for central business district

Tax Increases

On land
  Kept out of development for speculative reasons
  Platted but otherwise unimproved lots
  When rezoning to more intensive use permitted
  Close to other buildings and public utilities methods
    By valuing on basis of rental value for permitted uses
    By valuing on potential rather than actual use
    By valuing on market rather than artificially low value on buildings
On buildings
  Value slum properties on capitalization of income method
  Penalty tax on "slumlords"
  Where not kept in good condition
  Real estate
    Increase in general
    Owned by exempt institution where historic exemption no longer sensible
    Where public facility results in unearned increment
    On basis of cost revenue survey
    Tax increment bonds

Metropolitanization of Taxes

In accord with services rendered
On basis of metropolitan cost-revenue surveys
Community service districts
Assessment districts
Redistribution schemes, federal grants, state subventions, special districts, metropolitan reallocation schemes

Capital Levies or Conversion Taxes

On permitting change in use
On permitting development

Source: Current Municipal Problems, Vol. 9, 1967-68, pp. 354-355.

Because of the wide-spread use of tax exemptions, abatements and deferrals and the relative disuse of other tax measures, the following discussion of the above points will be directed primarily to those incentives involving tax exemptions, abatements, and deferrals. However, in many instances, the generalizations drawn from the discussion may apply to all incentive measures.

Characteristics of Tax Incentives

What is a tax incentive? Before the planner can evaluate how to use it, he must know what it is. As mentioned previously, tax incentives are used to induce a desired activity. This is accomplished in the majority of cases by providing monetary assistance or benefit through the tax laws so as to make the desired course of action more palatable. The result may be to make an activity less costly to perform; to reduce the risk involved, or; to increase the after-tax profit.[62] Since public funds are involved, it is assumed that the public both desires the result to be achieved and is willing to spend government funds for the purpose rather than let the marketplace determine the extent to which the result will obtain.

Tax incentives then, are public subsidies utilized to induce a desired activity by reducing the tax hardship on the recipient of the subsidy. Two key words in this definition are "public subsidies" and "tax hardships." These concepts are developed further.

Tax Hardships versus Personal Hardships

Many so-called incentives are actually concerned with involuntary activities of taxpayers which could not be changed regardless of the incentive. These special tax provisions usually involve various types of personal misfortune or hardship which legislators wish to alleviate.[63] For example, property tax exemptions for the elderly are granted in many areas to relieve the tax burden on those with low, fixed income. Yet in this context, such exemptions are nonincentive, because it is impossible to grow old any faster as a result of the exemption.

In some cases, distinctions become fuzzy as the subsequent impact of such exemptions are noted. For example, the exemptions for the elderly may foster increased migration to tax exempt jurisdictions. In that context, the exemption would be incentive even though it may not be desired. Such ramifications are subtle and seldom receive more than passing attention by legislators. The planner, however, should be cognizant of these distinctions and be able to follow through interrelationships and consequences and predict the rounds of effects a tax measure would have on planning goals. As a general rule, the planner should use the criterion that tax/land use incentives must be capable of inducing a particular activity. The tax incentive attempts to reduce the tax hardship of performing the activity.

Tax Expenditures are Subsidies

Much of the confusion concerning tax incentive measures has been the failure to recognize such incentives as a form of public subsidy. Tax incentives are expenditures similar in many respects to those direct expenditures undertaken by federal, state, and local legislators to achieve various social and development purposes. The differences between the tax incentive subsidy and the direct expenditure subsidy are more illusory than real.

Generally, tax incentives are pitted against direct governmental expenditures in terms of a "hidden subsidy" as opposed to an "open" or direct subsidy.[64] The implication is that incentives are generally considered to be somewhat "shady" benefits squeezed out of legislators by selfishly motivated special interest groups. Other arguments depict tax incentive programs as being loosely administered with little or no supervision over details as opposed to a direct expenditure program which is usually well supervised.

Although both of these examples of the deficiencies of tax incentive programs are true to a great degree, such conditions are not inherent in any tax incentive program. In fact, examples could be found to show direct expenditure programs which exhibit all the bad traits attributed to tax incentive programs. The point to be made is that both programs involve an expenditure of public funds and are, therefore, public subsidies. Either program of subsidy may

entail as much direction and supervision as the lawmakers decide is necessary.

Socio-Political Context of Tax Incentives

Although there may be general agreement among economists, politicians, tax experts, and planners that some economic activities must not be left to the vagaries of the market, there is a great deal of disagreement as to the actions needed to modify the economics of the marketplace. Furthermore, even though it may be agreed that a subsidy is necessary, there is still considerable dispute concerning whether the subsidy should take the form of a tax expenditure (incentive) or a direct expenditure.

Such arguments reflect the difficulties in sorting out the issues involved in providing government subsidies. These issues are not easily categorized, and usually are more appropriately addressed in specific circumstances rather than in generalized or hypothetical situations. Nevertheless, there exists in the literature several recurrent themes which point up the pros and cons of both tax expenditures and direct expenditures. These viewpoints are discussed in the following sections.

Incentives Encourage Private Sector Participation in Social Programs

Many times, a government perceives a social problem to be of such importance that it feels it must assist in the

solution. In addition, such difficulties usually occur because the marketplace is not functioning in such a way as to eliminate the problem.

In many such cases, the problem may be a result of inadequate levels of investment because of the adverse market impact of high taxes. Consequently, tax incentives could play the role of neutralizing the disincentive effect of high taxes. This form of subsidy is important to the private sector when (1) the economic activity entails a great deal of financial risk and estimated returns are drastically lowered as a result of taxes, or; (2) an already low profit rate is further lowered by taxes.[65]

Cynics of tax incentives assert that the need to modify market conditions to help private enterprise is not necessarily a virtue of tax incentives but merely an indication that government assistance is needed, and could be accommodated as well by direct expenditures. The preference for tax incentives in such cases leads to the next assertion concerning tax exemptions:

Tax Incentives are Simple and Involve Less Government Supervision and Detail

Part of the general argument that tax incentives are simpler than direct expenditures is one of differences in ownership interpretation. Once revenue is collected, it is the property and responsibility of the government. Consequently, various procedures are set up to control the custody

and efficient use of such funds. However, subsidies provided through tax incentives are essentially still privately owned. Ownership and control rests with the taxpayer. Action is initiated and executed unilaterally by the taxpayer acting within the established tax laws and regulations.[66]

This concept of ownership has led to a far simpler subsidy arrangement in the case of tax incentives. For the most part, there has been less need for negotiation, less governmental supervision, less red tape, and a smaller or no new bureaucracy created from the subsidy. In addition, it is maintained that a tax incentive program permits quick action, because the program could begin as soon as the taxpayer initiates action. No extended negotiation with third parties would be necessary. Further, no taxpayer would be deterred from participation because of lack of expertise in obtaining grants from governmental officials.[67]

In rebuttal, advocates of the direct expenditure approach agree that incentive programs lack supervision and government control, but view this as a drawback because it does not allow expenditures to be evaluated for effectiveness. In contrast, it is claimed that not all tax incentive programs lack such control. It has been observed that the framers of tax incentive programs have many times found it desirable to include numerous substantive requirements.[68]

Tax Incentives Promote Private Decision-Making in Contrast to Government-Centered Decision-Making

This assertion is based on the belief that if the taxpayer is the initiator of action, then private decision-making is promoted. This is felt to be laudable because it fosters a pluralistic society with many diverse power centers rather than a centrally powerful government. Direct expenditure advocates maintain that if more flexibility for private action and less governmental control is desired, then a direct expenditure program can be so designed.[69]

Tax Incentives Permit Windfall Gains When Taxpayers Are Paid For Doing What They Normally Do

It is argued in many instances that tax incentives are wasteful because tax benefits generally go to those taxpayers who would have performed the functions desired anyway. The homestead exemption, for example, is a tax incentive to promote homeownership. Yet, it is likely that homeownership would continue to increase at the same rate without the exemption.

The problem of windfall gains is not unique to tax incentives, but because most incentives have been loosely structured and supervised, they have been more open to attack on this point. Direct expenditures with a program containing similar loose controls would probably suffer the same criticism.[70]

Tax Incentives Are Inequitable

Of all the charges leveled against tax incentives, its inequitable effects are more usually true. By the very fact that tax incentives normally entail exemptions or other deletions from the tax base, it is inevitable that incentives will constrict the tax base and usually result in an increased tax burden for the remaining taxpayers.[71]

Another important failing is that tax incentive measures do not directly affect those outside the tax system.[72] Using the homestead exemption again, it is evident that to take advantage of the incentive, one must be a homeowner. For those too poor to own property, no benefit is derived. Usually such people will rent accommodations. A portion of their payments go for property taxes which are not reduced at all by the homestead exemptions.

Tax Incentives Distort the Choices of the Marketplace and Produce Unneutralities in the Allocation of Resources

This criticism is almost always valid since tax incentives are designed to interfere with the allocation of resources. Implicit in the statement is the accusation that tax incentives have continuous rounds of effects, secondary and tertiary, which are not recognized by policy makers. This criticism is well taken, but could apply equally well to direct expenditures. The stigma remains attached to tax incentives because for the most part incentive programs have

received very little thought and consideration as to their indirect effects before being implemented.

Tax Incentive Programs Continue Year After Year Unchecked

Most tax programs in the past were not designed with termination dates. Consequently, many of these programs continue from year to year without any evaluation to determine the effectiveness of the program. The longer such unchecked programs stay on the books, the more apt they are to become tax havens for those able to maneuver themselves into receiving the tax benefits. Although this is not an inherent defect of incentives, it has proved to be true for a great many incentive programs.[73]

In addition, the nature of tax incentives make them openended, available to any taxpayer to use. This openendedness makes it impossible to foretell in advance how much in subsidies will be provided in any year. Although incentives are normally not budgeted, cost figures would be helpful in making some kind of cost-benefit or cost analysis of the incentive measure to determine its usefulness before it is implemented or reimplemented each time.[74]

Legal Considerations

Just as the social and political considerations surrounding the use of tax incentives may be widely divergent, so are the legal considerations. In addition to being constrained by federal constitutional limitations, tax measures

must also conform to the limitations imposed by the state in which the measure is to be enacted. This section will discuss both of these areas of concern.

General

The governmental power of taxation is an attribute of sovereignty, and unless restricted by consitutional provision, is vested exclusively in the legislative branch of government.[75] Although most authorities recognize the taxation power as a mere extension of the police power, legal precedent has evolved into a commonly accepted distinction between the two. This distinction is generally related to function. The police power relates to regulation while the tax power is for revenue production. However, this legal fiction has been duly recognized as such by political theorists, and many courts alike.[76] In effect, most, if not all taxes, have a regulatory effect, whether intended or not. Even where the regulatory effect is obvious, many courts, both federal and state, have upheld certain taxes.[77]

However, in light of obvious overlapping, courts have continued to make distinctions between the two powers. One reason for this is the great number of inconsistencies and contradictions among the laws of the several states. When courts are faced with a conflict between constitutional limitations and the demands of social progress, they have been able to resolve such conflicts only through legal fictions and divergent decisions. As a consequence, cases before the

courts have been upheld variously on the police power or the power of taxation depending on the limitations existent in state laws.[78] This discontinuity in legal opinion is difficult to generalize and concrete observations can only be attained by perusal of each state's laws and legal precendents.

Federal Limitations

Although states are primary sovereign bodies and possess full taxing power, the federal constitution does establish certain restrictions on the use of that power. Although ten constitutional restrictions apply to state taxing powers, only two are of interest here--due process of law and equal protection of the law.

Due Process of Law. One clause in the Fourteenth Amendment to the Federal constitution provides that no state shall deprive any person of his life, liberty, or property without due process of law. The clause has three specific applications to state tax laws: (1) it does not allow a state or local taxing government to levy a tax beyond its jurisdiction; (2) it may be used to check extreme or confiscatory state and local taxes; (3) it prohibits the utilization of any forms of assessment or review which are arbitrary, unjust, or unfair, or which deny the taxpayer an opportunity to assert his rights before a proper judicial authority.[79]

Although these restrictions seem straightforward, legal interpretation has allowed considerable latitude to states in determining their own tax policies. Thomas Cooley in his Treatise on the Law of Taxation states:[80]

> In order to bring taxation imposed by a state, or under its authority, within the scope of the provision of the Fourteenth Amendment which prohibits the deprivation of property without due process of law, the case should be so clearly and palpably an illegal encroachment on private rights as to leave no doubt that such taxation by its necessary operation is really spoilation under the power to tax. A state has the right to devise its own system of taxation free from federal interference.

As a consequence of this wide latitude given to states, rarely is the "due process of law" clause invoked in defense against confiscatory state or local taxes. However, in those taxes which involve a valuation to determine the tax base, such as property taxes, the "due process of law" limitation is important. In such cases, there must be a formal act of assessment to determine property value. This value is a matter of public record. The taxpayer must be notified of his liability and have the opportunity to present his case against the assessment.[81]

Equal Protection of the Laws. In the same sentence of the Fourteenth Amendment which includes "due process of law" is also the provision that no state shall "deny to any person within its jurisdiction the equal protection of the laws." This clause forbids arbitrary or hostile discrimination which is not based on reasonable distinctions.

Again, however, federal courts have been extremely reluctant to strike down any state or local tax law as arbitrary or hostile. Such laws will usually be upheld if any reasons can possibly be found to justify tax distinctions or classifications.[82]

This clause has most often found its use in cases concerning property taxation when local or state laws attempt to exempt or classify various types of property. In such cases, the federal courts have liberally applied the doctrine of reasonableness and in most cases left such determinations to state legislatures.[83] Professor Cooley demonstrated the court's attitude to this question in citing part of an opinion of the U. S. Supreme Court in the case of Bell's Gap R. Co. V. Pennsylvania, 134 U.S. 232,237:[84]

> We...are safe in saying that the Fourteenth Amendment was not intended to compel the state to adopt an iron rule of equal taxation. If that were its proper construction,...it would render nugatory those discriminations which the best interests of society require, which are necessary for the encouragement of needed and usefull industries, and the discouragement of intemperence and vice, and which every state, in one form or another, deems it expedient to adopt.

State Limitations

In practice, most restrictions placed on the use of the property tax emanate from the limitations imposed by each state. The variety of limiting provisions in state constitutions is so great that only those which have primary importance to utilizing the property tax as a land use

control will be discussed here. It should be noted that the limitations on the tax are important, because they greatly curtail the flexibility of the tax. Without some degree of flexibility, it becomes difficult to adopt the tax to specific or changing conditions without engaging in lengthy political and legal conflict. Many tax limitations are the result of conditions and attitudes which were temporary in nature--at least more so than the constitution of which they are many times a part. It is generally agreed among theorists that most state constitutions contain altogether too much detail on tax matters.[85]

The following discussion of state constitutional limitations is of necessity generalized. However, as Chapter IV will indicate, these restrictions are commonplace and in many cases represent the first hurdle toward utilizing the property tax as a land use control.

Sovereignty and Delegation of Authority. In the American system of government, states have sovereign powers which include that of taxation. Local governments, however, are not sovereign and in fact are considered subjurisdictions of the state. Consequently, in order for local governments desiring to (1) obtain the power of taxation and (2) modify or utilize the tax in some manner not already prescribed by the constitution, statutes or by judicial interpretation, a grant of such power from the state is required.

Even when the constitution of a state delegates the power or taxation to municipalities, such delegation is normally not self-executing and requires a statute to bring the power into force.[86] In almost every situation which requires modification of existing taxing practices, local governments must obtain enabling legislation from the state or in some instances, a constitutional amendment.

Equality and Uniformity. As indicated in Chapter II, the "equal and uniform" taxation of property was a response to democratic ideals during the nineteenth century. The result was the build-up of the general property tax, which included both personal and real property, and attempted to tax all types of property proportionally and at the same rate. By 1900, many states had adopted such provisions into their constitutions. These limitations to the property tax have been used in many instances to block attempts to influence land use through taxation.

Such attempts have usually centered around trying to classify different types of property and applying different rates to each type; or, to give special tax rates or exemptions to a particular type of property. Because of the inflexibility and administrative difficulty involved in the uniform and equal taxation provisions, numerous states, either through constitutional amendment or judicial interpretation, have allowed complete or partial classification

of property for tax purposes. Approximately 32 states now have full or partial authority to classify property while 12 states still do not have such power. Six states and the District of Columbia have no constitutional limitations at all concerning uniformity.[87]

Classification of property may still be contested based on a violation of the uniformity clause in state constitutions. However, classification will generally be upheld if it is fair, reasonable, not arbitrary, and based on substantial distinctions. Again, however, the courts accord the legislature broad discretion in determining such distinctions and will not interfere unless the tax is clearly arbitrary or unreasonable.[88] Broad interpretation of proper classification by the courts has also allowed state legislatures to exempt those properties from taxation which they deem appropriate.[89]

Assessment at Market Value. All states require property subject to taxation to be assessed according to its market value. Although the states vary as to the term actually used, market value has been defined by the U. S. Supreme Court as: "the price that property would bring to its present owner if it were offered for sale on an open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other..."[90]

This means that even though the actual tax rate might only be applied to a part of the property value

(because of fractional assessment ratios), the actual assessment must be based on 100% of the property's market value. Consequently, any state or local jurisdiction wishing to influence land use decisions by assessing a particular property or class of property at lower or higher than market value would run afoul of most constitutional provisions. To obviate this limitation would require a constitutional amendment deleting the necessity of assessing at full market value and substituting instead other criteria for assessment.[91]

Rate Limitations. Limitations on state and local property tax rates are found in approximately one-third of the states. Rate limitations are usually expressed in terms of a maximum rate of so many mills on the dollar. One mill equals one-tenth of one per cent (.1%). Mill rate limitations may be fixed at a certain number of mills, or graduated based on assessed valuation of the property or the population of the jurisdiction. Rate limitations may be exceeded in some states by referendum or upon review and approval of the state tax commission. Other variations of rate limitations occur in the various states.[92]

The implication of this limitation upon using the property tax as a land use control is largely fiscal. Rate limitations have become fiscal "strait jackets" for many local jurisdictions. Tampering with the property tax for land use purposes through exemptions, tax abatement, or

deferral programs, may place the ever-pressing revenue production functions of the property tax in jeopardy. Even without such tampering, rate limitations have caused local areas to curtail necessary government services and/or engage in dubious assessment manipulations and excessive borrowing.[93]

CHAPTER IV

ANALYSIS OF TAX INCENTIVE PROGRAMS

The purpose of this chapter is to analyze the practical application of tax incentive measures. The objective of the analysis is to examine how the property tax has been used in various land use and development situations and determine the reason for the effectiveness of the tax measure in accomplishing its stated objective(s). Because of the similarity of many programs, as well as the sheer number of tax incentive examples, a case study approach was selected.

The methodology employed consisted of a review of the literature concerning tax incentive proposals and a selection of representative examples which were then researched in more depth. Personal interviews and postal interviews were utilized to gain more information on each tax measure as well as sound out governmental officials on the usefulness and/or disadvantages of the tax incentive device.

Based on the above approach, these case studies have been organized according to the land use or land use related development objectives they were designed to achieve. These objectives are as follows: homeownership, industrial location, central city renewal, rural-urban fringe development, and overall urban development.

The limitations of this analysis are numerous. The primary limitation is the lack of sufficient empirical data concerning most tax incentive programs to allow concrete conclusions. Where such data have been available, they were utilized. Nevertheless, in some instances, conclusions have been drawn from inferences, assumptions, or opinion.

Homeownership

One attempt to influence residential land use development has been through the encouragement of homeownership. The tax incentive measure which has as its objective to increase homeownership, is the so-called "homestead exemption." Designed to reduce the property tax burden on homeowners by exempting a portion of the value of their real property, this measure was introduced and then rejected in the Dakotas and Wisconsin between 1917 and 1923. The Depression of the 1930's revived the concept, and various schemes were presented in at least 30 state legislatures. Many were rejected; several were adopted and later repealed--Wyoming most recently in 1955.[94] Today, 11 states still utilize the "homestead exemption." They include Colorado, Florida, Georgia, Hawaii, Iowa, Louisiana, Mississippi, North Dakota, Oklahoma, Washington, and West Virginia.[95]

It should be mentioned that although the original homeowner's exemption in the Dakotas and Wisconsin was intended to encourage new homeownership in rural areas, the "homestead exemption" of the 1930's was designed to stem the

tax burden on existing owners. Then, as now, homeownership was regarded as beneficial, because it was felt that it would stabilize the community. The Depression produced a great number of foreclosures and tax delinquencies. In short, there existed a trend away from homeownership. The use of the homestead exemption was an attempt to alleviate the tax burden on homeowners and hopefully to stem the movement away from homeownership.[96]

The particular characteristics of each state's homestead exemption varies. The amount of the exemption ranges downward from $5,000 in Mississippi and Florida ($10,000 in Florida if the homeowner is over 65) to $1,000 in Oklahoma.[97] In some states, the exemption is only applicable to state assessments.

Other states vary in their administration of the exemption. In Iowa, for example, a homestead credit is in effect. The state refunds to the local tax jurisdictions credit amounts equal to the first $2,500 of assessed value. No credit is allowed on any portion of the tax which results from rates higher than 25 mills. Funds for the credit are derived from the state sales and income tax. This practice prevents local tax jurisdictions from losing any revenues because of a state "mandated" tax exemption.[98]

Effects of Homestead Exemption

The actual effects of the homestead exemption are generally regarded to be negative, both in terms of increasing homeownership and in terms of undermining the property

tax base. In relation to the tax base, homestead exemptions comprise a large portion of the total exempt property in those states which utilize it. In addition, millage rate limitations coupled with numerous other exemptions which exist in many states, complicate the fiscal capacity in a great number of local jurisdictions. While homestead exemptions result in a constricted tax base, the remaining taxpayers must shoulder increased tax rates to supply necessary revenues. As the local government reaches or approaches its legal rate limitations, local policymakers and administrators must seek new revenue sources and/or submerge the government into debt.[99]

It has also been argued that the subsidy supplied through the homestead exemption is not sufficient to outweigh other factors more important to homeownership, such as the availability of mortgage credit, favorable interest rates, and an adequate income. In addition, the homestead exemption does very little to solve the housing problems of the poor. Their problems are more related to level and continuity of income.[100]

Case Studies

In order to obtain further insight into the use of the homestead exemption, the states of Florida and Georgia were examined. Both states adopted the exemption during the 1930's and have utilized it continuously since then. It appears to be a relatively permanent facet of the tax

structure of both states. In addition to research information, officials were interviewed to determine how the exemption relates to homeownership, what effect the subsidy has on revenue production and the future of the exemption in each state.

Florida. Florida's homestead exemption provides that up to $5,000 of the assessed value of a bona fide homestead is not subject to real property taxes. The exemption applies in the stated amount irrespective of the relationship of assessed value to market value. Eligibility is limited to one-half acre in urban areas and 160 acres in rural areas.[101] Furthermore, homestead exemptions were increased in 1972 to $10,000 for homeowners 65 years old or more who have been residents of the state for five years.

The results of the investigation into Florida's homestead exemption are summarized as follows:[102]

1. Relationship to Homeownership--Although no scientific investigation has been undertaken in the state to determine the relationship between the homestead exemption and homeownership, state officials in Florida convey the belief that there is a significant relationship between the two. It is generally concluded that homeownership is more attractive because the homestead exemption serves to reduce housing costs. In addition, the fact that the exemption was increased by $5,000 for those homeowners over 65, points to a distinct relationship between the exemption and

homeownership for the elderly. Although not pointed out by state officials, it is generally known that the over 65 age group is a significant portion of the Florida population and has the sophistication and numerical strength to lobby for preferential treatment.

2. Effects on Revenue Production--State officials felt that homestead exemptions were not an unreasonable burden on local governmental units. They indicated that revenue production has been hampered more seriously by legislation in 1969 which shifted assessing to the county unit. The resultant county assessments were lower than previous city assessments. Another financial problem area is a 1968 constitutional amendment which restricts millage rates of local governments to 10 mills for each governmental unit except for debt service.

These conclusions given by state officials appear to be extremely naive upon any critical examination. The significance of the homestead exemption in restricting local revenue production in Florida is ably demonstrated in a 1965 study conducted by Rober J. Garrett and Roy L. Lassiter, Jr. for the University of Florida. The study analyzed the burden of real property taxes under varying assessment ratios. One key element taken into consideration was the $5,000 homestead exemption in Florida.

Among other significant findings, Garrett and Lassiter revealed that in 1962, 41 counties were assessing real

property at ratios to market value below 60 per cent, and 34 counties were using assessment ratios below 50 per cent (Florida has 67 counties). Further, it was concluded that the homestead exemption is the major factor which distorts the tax burden under fractional assessments. As a result of fractional assessments, the effective homestead exemption is greatly increased. In Alachua County, which assessed at a 45 per cent ratio in 1964, the constitutional exemption of $5,000 yelded an effective market value exemption of $11,000.[103] In Duval County, a 40 per cent assessment ratio raised the exemption to $12,500, and the result was complete exemption of 51,000 of the 96,000 homesteads in the county.[104]

The magnitude of the reduction in revenues should be clearly evident. Even so, Florida laws do not provide for any state subsidy related to the "mandated" property tax exemption. It is significant, nevertheless, that the 1972 Florida Legislature passed a Local Revenue Sharing Act which provides approximately $29,000,000 to city and county governments. Ostensibly, this subsidy resulted because of the mill levy restriction and other financial problems of local government and not because of the foregone revenue from homestead exemptions. Yet, the loss of property tax revenue from the exemptions are clearly part of the overall fiscal problem at the local level.[125]

3. Future of the Homestead Exemption in Florida. In light of the recent increase in the homestead exemption for the elderly, it is the opinion of state officials that the exemptions will continue. However, state officials are already concerned that continued migration of a large elderly population into the state will lead to decreasing property tax revenues as well as an abnormal demand for services. So great will these pressures be, that the homestead exemption may be reconsidered and possibly abolished. It was even suggested that the exemption could be used on a selective basis to redistribute the elderly within the state.

Georgia. Georgia's homestead exemption applies to owner-occupied homesteads in an amount not to exceed $2,000. For homeowners 65 years of age or older with a net income from the applicant and spouse not exceeding $4,000, an exemption up to $4,000 is allowed.[106]

Based on interviews with officials in the Georgia Department of Revenue and the results of the 1968 Tax Revision Study Commission report, the following conclusions were drawn concerning Georgia's homestead exemption:

1. Relationship to Homeownership--Generally, without reference to any studies, officials of the Revenue Department felt that homestead exemptions were of economic benefit to homeowners, and therefore, had a significant relationship to homeownership. However, the 1968 Tax Revision Study

Commission concluded that homestead exemptions have not caused a larger proportion of homes to be owned in Georgia. By way of comparison, the Commission indicated that Georgia had the lowest proportion of homeowners of any neighboring state having no homestead exemptions.[107]

2. Effect on Revenue Production--The Tax Revision Study was straightforward in its condemnation of the property tax for its effects on revenue production. It was recognized that the homestead exemption reduced the tax base with the result that exempted homeowners paid less property tax while other property holders paid more. In 1965, for example, homestead exemptions equaled about 20 per cent of all property listed for taxation. These exemptions resulted in tax bills 25 per cent higher for other property owners.[108]

3. Future of the Homestead Exemption in Georgia--Both officials and the Tax Revision Commission foresee continued use of the homestead exemption. It was noted, however, that Georgia ranges next to last in its reliance on the property tax.[109] Further, one of the most expensive operations of local governments, education, is financed to a larger degree from state funds in Georgia than is surrounding states. If and when the State and/or Federal government makes more money available to local governments, the impact and importance of homestead exemptions will decline.

Conclusions

From the case studies, it can be concluded that the homestead exemption may well have the effect of increasing

homeownership if the exemption is high enough, such as that for the elderly in Florida. However, there still lingers the doubt that the exemption is only a subsidy for doing what would occur without it. In Georgia, the Tax Revision Commission flatly concluded that there was no significant relationship. Neither conclusion has been fully substantiated, and would merit further study.

The problem of constricting revenue production appears to be clear. In both states, the effect of reducing revenue production was fully documented. In addition, it was recognized that the exemption presented problems of equity in that other property owners were required to shoulder an unequal burden with little control over whether or not such a burden is desirable.

Based on the information at hand, it is apparent that the homestead exemption causes more problems--especially those of revenue production and equity--than it tends to solve in land use planning. With some amount of tinkering, these problems could be overcome as has been done in Iowa with the homestead credit. The severity of both problems would depend also on the extent to which the property tax is utilized as a fiscal tool for local government. On balance, however, the homestead exemption as presently used does not appear to be a useful tool to achieve the objective of homeownership.

Industrial Location

Possibly one of the most frequently suggested tools for luring industry into an area is the "tax incentive." In practice, most jurisdictions which have seriously attempted to attract industry have used property tax exemption as only one of a broad range of inducements. Some of these inducements include the following: industrial promotion campaigns; provision of free land; free or low-cost utilities; construction of buildings; financial assistance in moving a plant; issuance of bonds or levying taxes to assist plant development; field representatives; provision of industrial districts, and a host of other specialized activities to aid prospective industries.[110]

The practice of providing inducements to industry has evolved over a considerable period of time. However, the modern form of inducement program was born out of the Depression years (1929-1941). Unemployment and the economic situation were so critical during that time, that special inducements became commonplace. After World War II, economists projected that chronic unemployment would again be a problem. States and local communities began to actively seek out industries and attract them as insurance that healthy economic conditions would exist. As some states began inducement programs, other states followed suit in order to retain a competitive posture.[111] All fifty states

now have industrial development agencies to aid in bringing in industry. In 1966, over $300,000,000 a year was spent to entice the $60,000,000,000 a year in industrial investment.[112]

Tax Incentives and Industrial Location

Although numerous studies exist which critically analyze the effects of the property tax on industrial site location, the Advisory Commission on Intergovernmental Relations has summarized most of these points in its report, "State-Local Taxation and Industrial Location."

The points put forth by the Commission include those areas of widest agreement among businessmen and tax practitioners and are summarized below:[113]

1. Even though non-tax factors such as labor, transportation, power, sites, industrial fuel, water, markets, distribution facilities, and living conditions are of predominant importance in plant location, state and local taxes constitute an element of business cost which must be considered in making managerial decisions.

2. Small plant operations, especially those with limited resources and little product diversity, are more vulnerable to unfavorable cost situations than large industries. Therefore, tax costs may exert more influence on the location of these operations.

3. Certain firms demonstrate preferences for given taxes depending on the nature of their operations. Labor intensive firms are concerned about payroll taxes while firms with heavy capital investments and small labor requirements would be more concerned with the burden of property taxes.

4. Managers of industrial firms are concerned that tax costs be kept in line among competitors. This concern about relative treatment leads many industries to emulate one another and to locate in relative proximity to one another.

5. Many areas of the country earn the image of being a "high tax" state or area. Even though policies might change in the area, many times the stigma remains.

6. There is wide-spread agreement among company executives that if the company is entitled to a property tax exemption, it is taken as a matter of course. Further, little evidence exists to show that any jurisdiction attempts to overtax a business which it originally lured into the area with an exemption.

7. Generally, tax considerations are not prominent factors in choosing a general region or area for plant location. However, within the region or area, all cost factors are considered, including taxes, and taxes may provide significant cost differentials.

State Policies on Tax Exemptions to Industry

In 1966, special property tax benefits for new industries were found in the legislation of 13 states. In most instances, local governments were authorized to exempt from local taxation the real estate of "new industries" for a designated number of years.

Of the thirteen states which authorize industrial exemptions, one study noted that only seven states use them extensively--Alabama, Kentucky, Lousiana, Mississippi, Rhode Island, South Carolina, and Vermont.[114] In addition, there are variations in the type of exemption given. For example, some states such as Hawaii, exempt only certain types of industries. Rhode Island and Vermont provide a tax freeze on new industries rather than outright exemption. Eleven of the thirteen states allowing exemptions specifically permit local governments to offer tax exemptions, although many times this requires a majority vote of the electorate of the local community.

Problems Attributed to Industrial Tax Exemptions

The critics of industrial tax exemptions are numerous and vocal. The most common criticism is the same as for all exemptions--inequality. The grant of a tax exemption reduces the tax base, and places the burden of taxation on fewer property owners. In addition, tax exemptions for "new" industries receive their subsidy at the expense of earlier developed firms.

Another criticism is the problem of windfall gains received by an industry. Many times, exemptions are too liberal in terms of scope and duration, resulting in a subsidy in excess of that needed to actually bring an industry into an area.[115] Such criticism is usually true for those communities which have not prepared a cost/benefit analysis of the subsidy to be offered. In fact, it may be discovered from a cost/benefit analysis that a subsidy is not desirable.

Another important criticism concerns the competition for new industry among local as well as state governments. In an effort to maintain a competitive posture, state and local governments legislate tax concessions which are harmful to the equity as well as the revenue production requirements of the property tax. Even if tax exemptions are not legislated, intergovernmental competition is still a strong incentive for local officials to "negotiate" preferential treatment in their taxes. Although such practice is usually illegal, it is nonetheless widespread.[116]

Case Studies

To study the practical application of industrial tax incentives and the correlation with industrial location, two case studies were undertaken. The first is the industrial development program in Louisiana. Louisiana is usually cited as one, if not the most active state, in utilizing tax exemptions. It is also one of the few states which

keeps records of the amount of exempt property. In addition, several researchers have studied and evaluated Louisiana's program therefore allowing this researcher more insight into the answers provided by state officials in a postal interview.

The second case study utilizes Puerto Rico's industrial development program to analyze the impact of tax exemptions. Puerto Rico was chosen for several reasons. First, Puerto Rico has experienced a dramatic increase in industrialization since 1947 when its first functional tax exemption law was passed. Second, Puerto Rico utilizes its property tax exemption law in conjunction with numerous other devices--such as income and sales tax exemptions--to lure industry. Third, to a great degree, Puerto Rico's industrial development program is tied to an overall land use development plan in that industries are induced to locate in particular zones on the island.

The methodology of the case studies involved research into specific details of each incentive program with a special emphasis on the relationship between the incentives offered and the location of industry. In addition, a postal interview was conducted with the Research Director of the Department of Commerce and Industry, State of Louisiana, and, a personal interview was conducted with an industrial representative of the Economic Development Administration of the Commonwealth of Puerto Rico. Both interviews were oriented

to a general response by local officials as to how effective their program was and any problems encountered in the program.

Louisiana. Louisiana's present tax exemption program dates from an amendment to the Constitution on November 5, 1946. Louisiana did operate a similar program from 1936 to 1941, but the program was allowed to lapse.[117] Generally, the current law provides that any manufacturing establishment entering Louisiana, or any manufacturing firm expanding its Louisiana facilities is eligible to receive exemptions on plant and equipment--not land--from state, parish (county), and local property taxes for a period of ten years. The intent of the law is to stimulate industrial expansion by offering tax benefits at the most critical stage of any business endeavor--the beginning. The law is administered by the Department of Commerce and Industry.[118]

In addition to the provisions of the 1946 law, several amendments have been made. In December of 1966, the State legislature authorized the Louisiana Council on New Industry to negotiate contracts with manufacturers. Through negotiations, the Council can, in effect, meet the lowest tax offer of any other state in which the industry is contemplating locating. The contract is reviewed every five years and requires the approval of competing manufacturers in the area of possible location.[119]

Louisiana has also assured industries accepting tax exemptions that after the exemption runs out, taxes will not be raised to a "prohibitive" level. A constitutional amendment passed in 1967, specifically protects an industry from local "catch-up" taxes upon expiration of its state-granted exemption from local property taxes.[120]

An important facet of the Louisiana program is the fact that all exemptions are granted through the State rather than from local governments. This allows central control as well as central records-keeping. Because of the existence of adequate records, it was possible for studies to be conducted by other researchers on the effectiveness of the exemption program. These studies were heavily relied upon for this analysis.

The conclusions concerning the relationship between tax exemptions and the location of industry have been summarized as follows: 1. Location Incentive; 2. Cost-Benefit Analaysis; and, 3. Interstate Competition.

Location Incentive. It was concluded from the interview with Louisiana officials that the Department of Commerce and Industry in fact believed in the effectiveness of its tax program in luring new industry into the state. The petrochemical industries are cited as examples of industries that have taken advantage of the tax exemption program. Louisiana officials point to a number of giant petrochemical

firms that have taken advantage of the program, including Standard Oil of New Jersey, Allied Chemical, American Cyanid, Dow Chemical, Grace, Wyandotte, U. S. Rubber, Kaiser, Ethyl, and Shell.[121] Critics are quick to point out, however, that Louisiana's geographical location is so favorable for chemical complexes that these companies would have located in Louisiana even if inducements had not been offered.[122]

Wiliam D. Ross, Dean of the College of Commerce, Louisiana State University, studied the effects of the state's exemption program from 1946 through 1950. Based on his research, there is some evidence to support the contention that the industrial property tax exemption will become the deciding influence in the decision to develop and to locate a new industry in Louisiana rather than another state. This would occur only if the particular industry was vulnerable to property taxation. However, the incidence of this happening is very low, simply because property taxes are such minor business costs compared to overall business expenses.[123]

In terms of lowering business costs, Dr. Ross indicates that the firms most likly to be influenced by the exemption will be foreign firms, firms producing regionally oriented products, firms with multi-unit operations, and the firms making relatively large new investments.[124] Not all firms, even those mentioned above, will be equally effected by property taxes.

2. Cost-Benefit Analysis--The cost differential allowed by the tax exemption is the measure by which the management of an industry should judge the location potential of an area. However, management may also conclude that the cost differential is outweighed by other factors. On the other hand, the value and soundness of the exemption program itself should be judged in the light of the cost of the program to the state.

Although state officials indicate that each tax-exempt industry is evaluated as to whether the exemption granted is in the best interest of the state, a procedure for making this evaluation was neither offered by state officials nor defined by statute or administrative procedure. Dr. Ross evaluated the costs of the exemption program during the 1946-1950 time period, both as a cost saving factor to the enterprises receiving exemptions and in terms of the benefits received relative to the costs entailed to the state and local governments.

As a cost-saving factor, Dr. Ross's survey of industries receiving tax subsidies indicates that there is some doubt as to the validity of the significance attached to the tax exemption by the industries in making their development and locational decisions. Dr. Ross bases his conclusions on the fact that many of the subsidies were too small to have a cost impact regardless of the firm's size. In other cases

where the subsidy was large enough to make a cost difference, the temporary nature of the subsidy militated against developing or locating a firm strictly on the basis of the tax saving involved. Only in a few instances of the industries surveyed did Dr. Ross feel that the cost saving was significant enough to base a locational decision on.[125]

Dr. Ross was able to calculate the approximate costs and benefits received from the tax program from 1946 to 1950. His estimates revealed that over $300,000,000 of the $355,121,753 in new investment from companies with the tax exemption would have come into the state without the exemption. In addition, Ross estimated that the combined parish governments lost $2,971,123 per year, and special tax districts lost another $638,890, while the state governments lost $816,782 annually as a result of the exemptions. These funds could have been used to alleviate the burden of providing services to the new industries receiving the exemptions.[126]

State officials indicated in the interview that the state government does not reimburse local governments for the revenues foregone as a result of the state-mandated industrial property tax exemptions.[127] This would appear to be unequitable to the local governments, because they have no influence on the location of exempted industries, yet must supply utilities and services to the business and the

additional workers and their families. The state assumes that the additional new employment, payroll, and expansions of local business activity will offset the costs to the community. As Ross points out, however, even if the industry is an asset to the community, a free ride in the form of a tax exemption can be justified only if the exemption is responsible for the location of the industry in the state.

3. Interstate Competition--At the time of Dr. Ross's study, there was evidence to indicate that Louisiana's overall tax load in relation to taxable capacity was well above other southern states and above the average for all states.[128] Then, as now, the Department of Commerce and Industry defends its tax exemption program as one designed to place Louisiana on a competitive basis with neighboring states. As mentioned previously, the state legislature authorized in 1966 the use of negotiations with an industry to meet the lowest tax offer of any state in which the industry is contemplating locating.

These actions do not necessarily give Louisiana a tax-cost advantage. Rather, they neutralize the tax advantage another state may have over Louisiana. This effect was noted by Dr. Ross. His conclusion was that if no advantage was evident relative to other states, then locational decisions must be based on other than tax factors.[129]

The Advisory Commission on Intergovernmental Relations has also noted the neutralization policies embarked upon as a

result of interstate tax competition. Two methods are used: 1. direct matching in which a state attempts to stay in line on a tax by tax basis, and, 2. a trade-off approach in which an unfavorable tax situation in one tax category is offset with a favorable situation in another category. The tax matching policy, if carried to its extreme, would make a state's tax system too dependent on adjacent state's actions, thereby making a mockery of state tax sovereignty. Usually, states seldom can go beyond just "staying in line" with adjacent states because of the constant pressure for additional tax revenues.[130]

Puerto Rico. The Commonwealth of Puerto Rico is another governmental unit that has used tax exemptions extensively to induce industry to locate on the island. The industrialization of Puerto Rico has been dramatic since 1940. In 1940, per capita personal income was about $125 a year. In 1972, it was estimated to be $1,500 per capita.[131] Agriculture--especially sugar production--was the dominant force in the economy, while industry was very rudimentary. Three factors came together around 1940 to set Puerto Rico on its way toward a true economic revolution: 1. the Popular Democratic Party, under the leadership of Luis Munoz Marin, won a majority in the legislature; 2. Rexford Guy Tugwell was appointed Governor of Puerto Rico by President Roosevelt; and, 3. Puerto Rico received remissions of Federal excise

tax collections on the sale of Puerto Rican rum in the United States amounting to $160,000,000 more than had been expected.[132]

The Popular Democratic Party was significant because it committed the government to a program of economic development rather than making a major issue of statehood or independence which the other two parties emphasized. The Popular Party maintained a middle-of-the-road policy and promoted the status of "Commonwealth." Utlimately, this position prevailed, and Puerto Rico achieved the economic advantage of retaining unincorporated territory status which meant no Federal taxes, yet retained the advantage of being a part of the United States through association. Consequently, in 1952 Puerto Rico formally became a Commonwealth. Its Spanish name of "Estado Libre Asociado" (Free Association State) accurately describes its economic and political status.

The platform of the Popular Democratic Party was "Bread, Land, and Liberty." The Popular Party undertook a program of economic development to answer the political promise for "Bread." The promise for "land" was satisfied to a large degree through government activities condemning tracts of land and parceling it to farm laborers who could build a home and produce enough food for the first time. "Liberty" did not mean independence from the United States,

but freedom from the overpowering economic and political domination of the U. S. sugar companies. The Land Act of 1941 did much to break up the holdings of the sugar companies and redistribute the land.[133]

Puerto Rico attained the right to elect their own Governor in 1947. Munoz was so elected in 1948. Throughout his public service, Munoz was instrumental in cleaning up politics, especially through his campaigns against vote-selling which the sugar companies widely practiced.[134]

The appointment of Rexford Guy Tugwell as Governor of Puerto Rico was also opportune for the industrialization of the island. Tugwell served from 1941 to 1946. His background was as an economist and planner with extensive experience in federal and municipal government. Tugwell brought with him a group of technically trained men into the government. This group of men, with Tugwell leading them, provided the technical assistance necessary to plan and direct the economic program.[135]

In addition to creating the Puerto Rico Planning Board which prepares the capital budget and carries on economic planning work, Tugwell helped create eight public corporations, one of which has been liquidated. These include the following: 1. Government Development Bank; 2. Department of Agriculture; 3. Ports Authority; 4. Land Authority; 5. Public Utility Corporations; 6. Industrial Development

Company; and, 7. Economic Development Administration. The Economic Development Administration and the Industrial Development Company together are known locally as "Fomento."[136]

The use of the corporate form has two great advantages which have helped Puerto Rico. First, it greatly reduces the red tape and inefficiency which is usually inevitable in conventional government agencies. Control and coordination of these individual corporations is maintained by placing cabinet rank government officials on the boards of directors; by having "interlocking" boards of directors, and; through strict audit of each corporation by the Comptroller who is answerable to the Legislature. The second advantage derives from the fact that corporations which have established earnings records can then borrow in the U. S. capital market or locally on their own credit. This allows public credit to remain unimpaired and available for public works projects.[137]

The third factor important to the industrialization of Puerto Rico was the remission of $160,000,000 in rum excise taxes. This money was invested in the new corporations. During this initial investment period, the emphasis of the program was on government ownership and operation of business. By 1947, problems with this emphasis were increasing. The corporations--primarily "Fomento"--were too involved in operating details, capital funds were low because the rum bonanza had run out, and operating funds were running low

because profitable operations were being offset by unprofitable ones. In addition, only 2,000 jobs had been created when 100,000 were needed. It was at this point that the decision was made to utilize the government to promote and develop private industry rather than engage in outright government ownership and operation.[138]

The essential ingredient to turning industry over to private enterprise was the tax exemption law enacted in 1947. In the years that followed, the Industrial Incentives Act of 1963 was enacted, and is essentially the same as the 1947 Act. The 1973 Act with amendments is now in force.[139]

The objectives of the economic program which the tax exemption law was to help carry out included the abolishment of poverty, the prevention of excessive urbanization, and the provision of relief to especially distressed municipalities.[140]

The justification for tax exemption rests on the premise that it compensates a firm for the higher cost of establishing a business for which there is no body of previous operating experience within the particular tax jurisdication. Such "pioneer industry" laws have historically focused more strongly on property taxes and duties on materials which are regarded as business costs, than on business income taxes. However, since Puerto Rico is an independent tax jurisdiction and U. S. internal revenue laws do not apply, new industries receive a tax break both ways.[141]

The Act contains numerous detailed qualifications, but its general tax exemption provisions are as follows:

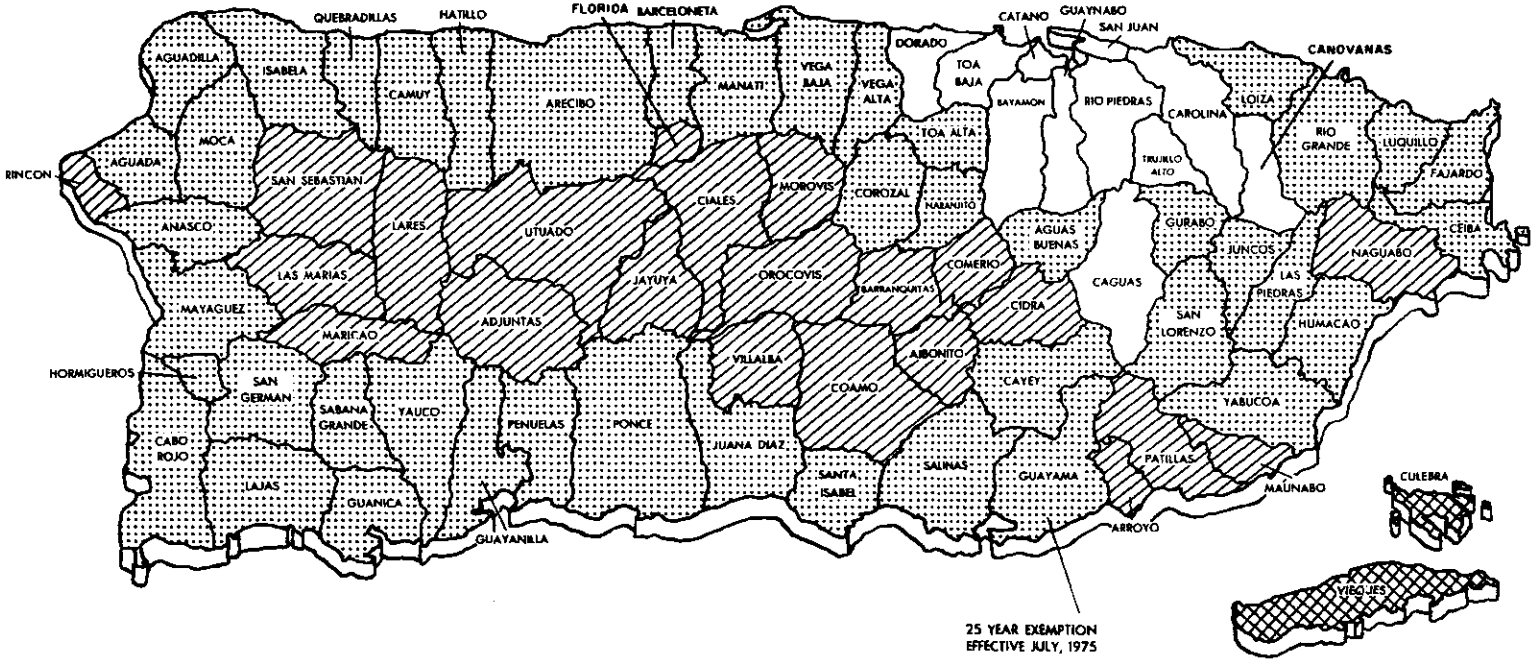
1. Almost any new industry or tourist hotel can be exempted from taxes on business and property;

2. Owners of property leased to tax exempt firms are exempt from taxes thereon, and dividend income to resident stockholders of tax exempt corporations is exempt from personal income tax;

3. Exemptions range from 10 years to 17 years depending on the zone in which the industry locates.

In accordance with the objectives of the economic program which sought to prevent excessive urbanization and to aid especially needy municipalities, the government initiated a program of decentralization of industry in 1953. A major portion of this decentralization effort included the use of tax exemptions. As indicated above, the term of the exemptions corresponded to the area in which the firm located. To aid decentralization, firms locating in the most developed municipalities, e.g. San Juan, receive only 10 years exemption, while those locating in the most underdeveloped municipalities receive 17 years exemption. There are exemptions of 12 and 15 years for municipalities of intermediate development.[142] These zones are delineated in Figure 1.

A final footnote to this background data is the function of the Office of Tax Exemptions which helps administer



10 Years
15 Years
25 Years
30 Years

Figure 1. - Puerto Rico Industrial Tax Exemption Zones January 1975

Source: Executive Order of the Governor, Administrative Bulletin No. 3025 and Act No. 147, approved July 23, 1974.

the tax exemption law. The Office is located in the Department of State. Its function is to hold public hearings and to evaluate the recommendations of "Fomento" and the Department of Labor, Justice, and Treasury--each of whom must also evaluate the exemption applications from their own point of view. The Office of Tax Exemptions then makes a recommendation to the Governor on each application for a grant of tax exemptions. The advantages of this organization are the following: 1. centralized administrations and records-keeping; 2. rapid decision-making; and, 3. the ability to evaluate each exemption from a fiscal, social, and planning point of view.[143]

There is considerable difficulty in evaluating merely the property tax exemption in relation to the success of Puerto Rico's industrial development program, since there are so many elements to the program. That the program has succeeded, there is no question; to what extent this success may be attributed to the property tax exemption alone, there are no definitive answers. The analysis of the property tax exemption must of necessity be a generalization from the effects of the total program and particularly the tax exemption portion of the program. The effect of the tax exemptions has been evaluated in terms of its incentive effect on industry and also in terms of the costs and benefits of the exemptions to Puerto Rico.

1. Incentive effects--The fact that tax incentives have played the dominant role in attracting industry to Puerto Rico has been substantiated from several sources. A 1957 survey by Milton C. Taylor[144] of 44 firms that had recently established themselves on the island, was made to determine their motivating location factor(s). The first question asked, "What was the primary motivating factor inducing your movement to Puerto Rico or the establishment of your business"? Only three inducements were mentioned--tax exemptions (51%), low labor costs (41%), and promotional activities of "Fomento" (2%).

The second question which was designed to emphasize the tax exemption, asked company executives whether their firms would have established a plant in Puerto Rico without the tax exemption. Thirty-seven of the 44 replies or 84 per cent answered that they would not have established a plant in the absence of the tax exemption.

A similar survey conducted by H. C. Barton of the Harvard University Center for International Affairs reached the same conclusion. This 1959 survey indicated that 83 per cent of those U. S. firms in Puerto Rico responding to the questionnaire cited tax exemptions as being a major reason for their decision.[145]

Barton also cites the opinion of the "Fomento" staff members who are in constant contact with prospective

investors. The staff are convinced that tax exemption is the main motive for considering Puerto Rico in the first instance, and that exemption is a main factor in almost all decisions to actually invest in the island.[146] This opinion was also shared by the industrial representative of the Economic Development Administration interviewed by this researcher.[147]

As interesting question was posed by Mr. Barton as a result of his research in Puerto Rico. Upon analysis, Barton found that the before-tax rate of return on investment among "Fomento" plants is about double the U. S. average. Presumably, this high rate of return resulted from low labor costs and high productivity. Barton poses the question of why should doubling a profit through tax exemption which is already double the U. S. average make so much difference. His conclusion is that many firms still believe in the "gold rush" psychology of making a fast profit and getting out. Barton cites as evidence the general lack of large, publically-owned corporations who have located on the island. These "blue chip" companies generally think in the long run and of marginal returns. Only recently have such firms undertaken a move to Puerto Rico.[148]

Another important question arises as to the overall cost impact the tax exemption has on location decisions. As noted in the Louisiana case study, only occasionally will

tax benefits be sufficient economic incentive to offset other, more important business expenses such as the cost of labor, the distance from markets, and the source of raw materials. In Puerto Rico, however, exempt business, under certain circumstances, may operate without paying any major tax levy either to the island government or the United States. Such a large exemption does counteract increases in other business expenses and generally accounts for the success of the inducement program in Puerto Rico while other exemption programs elsewhere have failed.[149]

2. Cost-Benefit Analysis--In terms of evaluating the costs of the tax exemption program to the benefits derived, it should be stated that current figures were not available. Records, however, are kept of the taxes "foregone" as a result of the exemptions granted. Barton's study during 1959 indicated that roughly $15,000,000 per year in all taxes were "foregone." Puerto Rican officials feel that this is strictly a theoretical cost, since few industries would have located in Puerto Rico without the exemption.[150]

On the benefit side, during 1959, it was estimated that 14 per cent of the net income directly and indirectly generated by a new export industry is collected by the Treasury on successive turnovers. Actual revenue yield to the Treasury in 1959 from all "Fomento" programs was about $40,000,000. Compared to a theoretical loss of $15,000,000,

the tax exemption generated $25,000,000 in additional revenue. Moreover, the "foregone" taxes are not permanent, and after the exemption period the remaining firms will pay full taxes.[151]

It was also noted that in comparison to an earlier program of direct subsidies of about $30,000 per year to help locate an industry, the tax exemption program of $15,000,000 annually was much easier to administer. The higher administrative costs of the direct subsidy program resulted from having to determine the amount of each grant through administrative procedures and having to audit each contract to insure that the terms of the grant were complied with.[152]

3. Future of the Tax Exemption Program--Probably the greatest testament to the continuance of the tax exemption program is the fact that it has been wholly embraced and strengthened by the first new Governor since Luis Munoz Marin. Luis A. Ferre assumed the governorship in January, 1969, and reaffirmed the government's active participation in industrial promotion.

Tax incentives, as well as other incentives in the program were cited by the new governor as necessary to continue the industrialization process, and to achieve new objectives. Several of these new directions were identified by Commonwealth officials.[153] First, the tax laws should be amended to induce a greater number of factories to stay in

Puerto Rico after their tax exemption period has expired. Second, legislation should be proposed to promote scientific and industrial research through scholarships and tax exemptions. Third, incentives--possibly tax exemptions--should be used to spur the development of ocean transportation firms.

Finally, the increase in wages--198 per cent from 1960 to 1967 in "Fomento" promoted plants--is gradually closing the competitive advantage Puerto Rico has over other states in the U. S. Once this competitive advantage is lost, the need for other inducements, including tax exemptions, to remain competitive will become more dominant.[154]

Conclusions

As the two case studies point out, there is no single unqualified answer as to the effectiveness of the property tax as an inducement to the location of industry. In Louisiana, there appears to be considerable doubt as to the effectiveness of the tax. In Puerto Rico, there was overwhelming evidence that tax exemptions were effective, but it was impossible to isolate the property tax from all other taxes.

Instead of a single answer, it would be more beneficial to draw conclusions as to the conditions under which the property tax may be successful as a locational tool in industrial land use decisions. Based on the research, the following conclusions are submitted:

1. To be effective as a cost factor, the tax exemption must be high enough to compete with other business costs. This condition is usually quite rare.

2. The impact of the property tax varies depending on the type of industry involved. Naturally for those industries which are hardest hit by property taxes, an exemption of those taxes would produce a relatively greater locational incentive.

The above conditions reflect the criteria under which a property tax exemption might succeed in inducing an industry to locate. There are other conditions, however, which should be considered before concluding that tax exemption is a desirable incentive.

1. If the tax incentive does not actually cause the industry to locate in the area, there can be no justification for the exemption. This will require some procedure for evaluating the exemption. This was lacking in both Louisiana and Puerto Rico.

2. The tax incentive should not cause a serious disproportion between the cost of the incentive and the benefit of the industry to the community.

The future of property tax exemptions for industry seems assured for at least the foreseeable future. On the mainland, Louisiana is typical of most of the states with tax exemption programs for industry. As indicated

previously, however, such exemptions usually do not create a tax-cost advantage as much as they allow the state to remain "in line" with other competing states.

Puerto Rico, on the other hand, has numerous advantages in its industrialization program not the least of which is an overall moratorium on state income and sales as well as property taxes for new industries. In addition, no federal income tax must be paid by those firms operating in Puerto Rico. These conditions are enough to provide an inducement to new industry. Puerto Rico's past record and their future plans indicate that the property tax exemption for industry will continue indefinitely.

Central City Renewal

The property tax plays a major role in the economics of land use in the Central City. Three factors are prominent concerning the tax in the development and redevelopment of the central city. First is the large amount of tax exempt land already on the tax rolls in many central cities. This has resulted because such cities harbor most of the government buildings, schools, churches, and other institutions which are usually exempt. Washington D. C., for example, had 44.1 per cent of the value of its real estate exempt in 1960. Boston, Massachusetts experiences an equally debilitating amount of tax exempt property when it was revealed that 39.3 per cent of its assessed value was exempt in 1959.[155]

The effect of exempt properties has been to constrict the tax base of the central city to the point where there is a substantial difference between the effective tax rate in the central city as opposed to the suburbs. Unfortunately, the central city frequently houses a disproportionate share of low-income residents who require higher than average welfare expenditures and return less per capita in property taxes. This double burden has created serious fiscal and land use problems in the central city.[156]

A second tax factor of significance to the city is lag time in performing reassessments. In many cities, land values in the central city have declined. However, assessments frequently do not drop as rapidly as values. Investment in high tax areas slows down or stops. This constricts the tax base to fewer taxpayers and results in higher taxes for the remaining property owners. These higher taxes come at a time when values are depressed, and there is little incentive to invest in the maintenance of the property.[157] Assessment lag is thought to be more generally true for commercial property than for other uses.[158]

The third factor of the property tax is the disincentive effect it has on inducing improvements and rehabilitation efforts in blighted areas. Because the property tax is an ad valorem--"according to the value"--tax, any major improvement to a building increases its value and, therefore,

its tax. In addition to the cost of the improvement, the owner must also pay a higher tax for rehabilitating his property while his neighbor who has made no investment but will benefit from the upgrading of the neighborhood will have his taxes increased only slightly or not at all.[159]

Alternative Tax Incentives for Urban Redevelopment

Although there are probably an unlimited number of tax programs and policies used by various local governments to spur central city development, such programs generally seem to cluster around three approaches. First is the outright exemption or tax abatement approach in which all or a portion of the property taxes are temporarily or permanently exempted. The New York City tax abatement program for housing resulting from the Mitchell-Lama Act of 1955 is an example.[160] New York City also enacted in 1971 a tax abatement program for otherwise unsubsidized multi-family construction.

The second approach is similar, but with a slight variation, and is called the "assessment freeze." This approach insures that from the time redevelopment occurs the local property tax will remain the same for a period of time even though rates for the rest of the community may go up. Milwaukee, Wisconsin utilized the assessment freeze for a short period before it was declared unconstitutional.[161]

The third approach is the most innovative in that it substitutes property taxes with an assessment based on gross

income. This approach allows taxes to be tied to actual income rather than imaginary income based on property values. Boston is a major city which uses this method. Legislation in that city allows developers an exemption of property taxes on improvements but not on land. In return, the developer paid the city 15 per cent of gross rental income.[162]

Case Studies: General

The case studies involve the exemption programs of New York City and St. Louis. The New York City program deals with residential land use through the development of low cost housing. The St. Louis tax exemption program has been directed at commercial land use as well as residential redevelopment. These two cities were chosen because each has compiled a total program of redevelopment with defined objectives rather than simply a tax exemption program.

New York City. New York City has a long history of being a leader in the movement to provide tax exemptions in order to spur low cost housing construction. New York State legislation in this area dates to 1920 in which localities were permitted to exempt all new dwellings from taxation. New York City was the only city to use the enabling legislation. In 1927, New York City also authorized the exemption of property taxes for housing built by limited dividend corporations for a period of 20 years.[163]

The enactment in 1955 of the New York Private Housing Finance Law, popularly known as the Mitchell-Lama Act,[164]

was a continuation of previous housing development efforts. The Act permits state and city loans below market interest rates and tax exemptions to provide new rental and cooperative housing for lower and middle income families. Housing companies may be formed to provide housing and related facilities, but their activities are limited with regard to profits, dividends, rents charged, and disposition of property and franchises. The program may be used for rehabilitation as well as new construction. The Federal 221(d)(3) housing subsidy program is similar in almost every respect with the New York program. The combined federal, state, and city publicly assisted housing starts ranged from 11,314 in 1960 to 27,539 in 1965 and to 24,420 in 1970.[165]

The number of private housing starts on the other hand fell off rapidly during the 1960's. The problem centered around the increasingly upward spiral of costs. The trend of private investment in housing is reflected in Figure 2. In 1960, for example, 34,600 privately financed units were started. This rose to a high of 48,500 in 1961 and held steady at 47,500 in 1962. After this, starts began to quickly decline until in 1965 only 13,500 units were initiated. This trend continued downward to 10,000 units in 1968 to 8,000 in 1969 and to 6,000 in 1970.[166]

This sharp decline was disturbing to housing officials in New York City. It was felt that a plan was necessary to

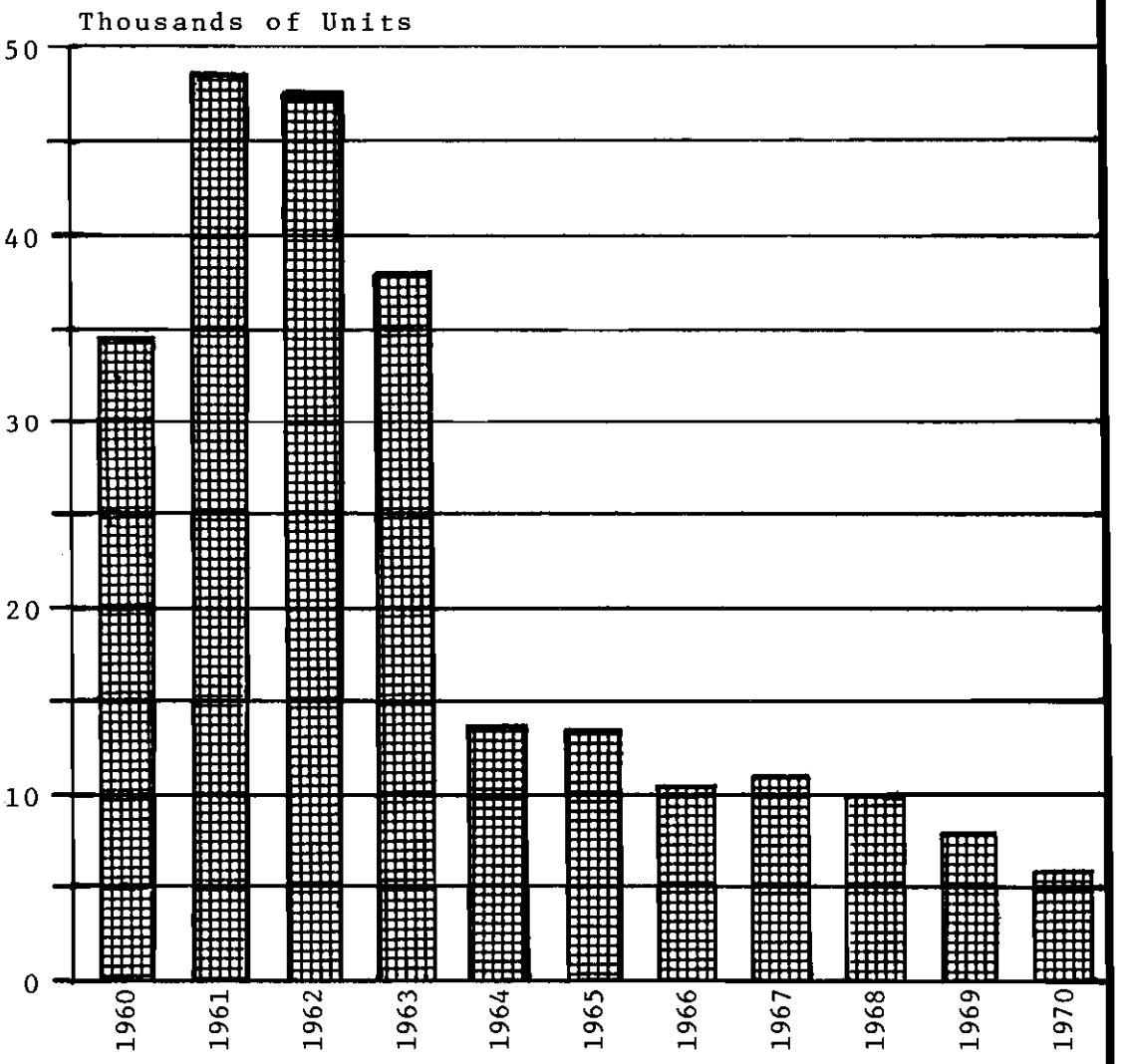


Figure 2. Private Housing Starts, New Construction New York City, 1960-1970

Source: New York Times, 31 October 1971, p. 82.

halt the downward trend, rejuvenate private housing construction, and stem the outward migration of executives and business people to the suburbs. Therefore, in July, 1971, Governor Rockefeller signed into law a tax-abatement program which would enable cities of 1,000,000 population or more to utilize tax exemptions for private multi-family housing.

Provisions of the Act. The Act was drawn up by the Housing and Development Administration of the City of New York. The major features of the plan include the following:[167]

1. An initial exemption from New York City real estate taxes equal to 100 per cent of the taxes on the new building, scaling downward to 80 per cent after two years, 60 per cent after four, and so on until the exemption ends in 10 years. The developer will continue to pay taxes equal to the taxes on land and buildings (if any) which existed during the tax year prior to the initiation of construction.

2. Tax abatement is for rental and cooperative multiple dwellings constructed between July 1, 1971 and December 31, 1974. Construction must start no later than December 31, 1972 and each building must contain at least 10 units.

3. The owner must guarantee a 15 per cent reduction in initial rents as compared to similar housing put up in the two years previous to the program.

4. To compensate for the gradual loss of the tax exemption, a 2.2 per cent annual rental increase, starting

with the second year and based on the initial rent, is permitted.

5. Exempted building owners must join the Rent Stabilization Association and future rent increases are limited to the renewal and vacancy rates set by the Rent Guidelines Board during the ten-year period.

6. The exemption applies only if the building goes up on vacant, predominantly vacant (at least 85 per cent), or on underutilized land; or land in a residential zone on which the existing buildings are nonresidential and nonconforming. Underutilized land may include building on air rights.

Objectives of the Program--The program was designed to spur private construction of housing by lowering overall housing costs through tax abatement. The HDA estimates that total production under the program should reach 150,000 units. By lowering housing costs, builders will be able to mass produce highly marketable, medium-size apartment houses.

Most of the new units are projected to be built in outlying areas--meaning outside Manhatten. It was estimated that only 12 to 15 sites in Manhatten might be developed while there was a wide-open market in outlying areas, especially for six-story apartment buildings.

Another objective of the program was to subsidize new construction, but without the attendant problems of relocation. Limiting building sites to areas which are

vacant, predominantly vacant, underutilized or are nonconforming, non-residential uses should result in few if any relocations.[168]

Program Results--In cities which have very high tax rates, the tax abatement weapon can be very powerful. In researching the effect of tax abatements in New York City, Dick Netzer found:[169]

> "For new apartment housing built without any public aid in New York, property tax payments currently (1966) equal almost 25 per cent of gross rents. For projects built with a 50 per cent tax abatement, the tax savings can reduce monthly rents by more than $6.00 per room."

This finding by Netzer appears to be confirmed by the initial developments which have occurred under the tax abatement plan. Not only has the program initiated new construction, but the rental rates are lower as well. A listing of the new developments and comparative rents as of February, 1972 was supplied by the HDA.[170]

1. Parc Plaza, consisting of 223 rental units, had a four-room rental cost of $230.00, compared to $315.00 for nonsubsidized units. Parc Plaza is located in Woodside.

2. A ninety-six rental unit complex in Flushing, had 3 1/2 room apartment rentals, for about $67.00, per room, which contrasts with $78.00 for comparable units.

3. One hundred and ninety-eight rental units were constructed on Staten Island. These units will also receive financing under the FHA 236 Program which will further lower

rental costs. A two-bedroom unit will rent for $204.77 including utilities and parking as compared to $314.43 in comparable units.

4. One hundred and thirty-two cooperative units were built at 900 Park Avenue in Manhatten. Although no comparative rents were available, it is expected that rents will be lower than unsubsidized units. In any case, income tax benefits for taxes and mortgage interest are passed on to tenant cooperators.

At the time the postal interview for this report was conducted, New York City had not completed their 2 1/2 year tax abatement program. Consequently, it is not known whether all the objectives of the program have been achieved. Based on the small sample of developments noted above, it would appear as if a good many of the objectives had been achieved. The tax abatement did induce developers to construct multi-family housing. Even cooperative housing has been developed under the program. Housing costs were also lowered. In the case of the units at Parc Plaza, costs were down $12.00 per room. The Flushing units were down $11.00 per room. Both of these are in line with Netzer's findings of a $6.00 per room savings at a 50 per cent abatement. In terms of decentralizing new construction, it was noted that only the cooperative units were built in Manhatten. The remainder were scattered outside the central core.

Criticisms--Criticisms of the program have come primarily from the Real Estate Board of New York. The first criticism is of the definition of "predominantly vacant" land. The HDA requires that any assemblage of parcels must be at least 85 per cent vacant. Builders argued for a figure closer to 65 per cent. The HDA proposal was designed to restrict new construction to outlying areas rather than the city core (Manhatten), while builders felt this was too restrictive.

Along similar lines, builders feel that exemptions are not the whole answer. Relief is also needed in other areas, especially zoning. Builders specifically indicate a need to permit higher densities and greater bulk. Higher densities would allow builders to increase their return per acre. This would help lower land costs and eventually should result in lower rental costs in the development. The HDA did not attempt to tackle zoning problems in the tax abatement program.[171]

St. Louis

St. Louis initiated an urban redevelopment program in 1959 utilizing existing redevelopment legislation passed by the State of Missouri in 1949. The program was felt necessary because there had not been a single major structure erected in the city since before the Depression. The program is based on Chapter 353 of the Revised Statutes of the State

of Missouri, 1949. It has come to be known as the "353" program. Local officials see the program as a supplement to federal urban renewal and other programs, not as a substitute.[172]

Provisions of the Act. The provisions of Chapter 353 are administered through the requirements established in Procedural Ordinance 49583 passed by the City of St. Louis on October 27, 1959. The basic provisions of the "353" program are as follows:[173]

1. The program can only be used in cities having a population in excess of 350,000. Only St. Louis and Kansas City presently qualify.

2. A private developer can set up a redevelopment corporation which can submit plans for the clearance, replanning, reconstruction or rehabilitation of any areas designated by the Mayor and the Board of Aldermen as "blighted" as defined in Chapter 353. Structures may be built for commercial, residential, industrial, recreational or public use.

3. Once a project is approved by the City, the private redevelopment corporation has the right to acquire the property by borrowing the City's power of eminent domain.

4. The redevelopment corporation receives a tax exemption for 25 years from the date of acquisition of the property. This consists of an exemption from all taxes on

buildings, but not land, for ten years. For the next 15 years, taxes on both land and improvements are based on 50 per cent of the normal assessed value. In St. Louis, for the first ten years, the developer is also required to pay a contribution in lieu of taxes equal to the tax levy on the former improvements.

5. Corporations are limited to an annual return of eight per cent on investment.

6. Once selected, a redevelopment proposal is written into a contract, through an ordinance, between the city and the developer.

As the program summary indicates, the two most important aspects of the "353" program are the lending of the power of eminent domain to redevelopment corporations, and the granting of tax exemptions. After all assessments and in-lieu payments are made, tax exemptions actually amount to relief from any new taxes on improvements.

Results of the Program. Although the program was started in 1959, no new structures appeared as a result of the program until 1967, when Plaza Square, a $24,000,000 apartment structure was built. Most of the new construction has been office buildings. However, as Table 3 shows, the "353" program has been utilized to construct commercial, residential, recreational, and public structures. The program has not yet been used to construct industrial structures.

Table 3. Buildings Constructed in St. Louis Utilizing "353" Program 1960-1971

Building	Cost (millions)	Year Completed
Equitable	$ 20.0	1971
500 Broadway	12.0	1971
1st National Drive In	1.5	1970
Blue Cross	1.9	1962
Gateway Tower	12.0	1968
American Zinc	1.2	1968
Pet Inc.	10.0	1969
Stadium	28.5	1966
Stouffer Riverfront Inn	12.0	1969
Plaza Square	24.0	1961
Mansion House	52.0	1966
Stadium Garages (4)	15.0	1965-1967
	$190.1	

Source: Unpublished interview data obtained from the City Plan Commission, St. Louis, Missouri, 28 May 1972.

Construction in the "downtown" area between 1960-1971 totalled $285.7 million. Of this total, $190.1 million was constructed utilizing the "353" program. Even more impressive is the size and cost of proposed developments in the CBD which may utilize the program. Present estimates indicate that in the next few years approximately $298.4 million will be invested in the CBD on eight new projects. Of these, three projects totalling $210 million have or will apply for the "353" program.[174]

These three developments include the following:

1. Laclede's Land which will cover a 2.5 acre tract and include a multi-purpose complex with apartments, shops, office buildings, an entertainment center, and six large plazas free of traffic. Estimated cost is $85 million.

2. The Planters Development will be an office/hotel structure. Estimated cost is $25 million.

3. The "Center City" proposal is a $100 million project for five blocks in the CBD retail core. It includes a 40 story office tower, a major department store, and a four-block three-level shopping mall.

There is little doubt by St. Louis officials and especially the City Plan Commission, who recommended the program to the city, that the program has had its desired allocational effects. Of additional importance is a study by the City Plan Commission which indicates that even with

the granting of tax exemptions, the city has clearly shown an overall gain in revenue. The gain in revenue is attributed in large part to the fact that St. Louis only receives 20 per cent of its total revenue from the property tax while a flat one per cent levy on gross earnings of residents and nonresidents alike produces 36 per cent of the city's revenue.[175]

To demonstrate the cost-benefit characteristics of the "353" program, two examples were utilized: the 500 Broadway Building and the Gateway Towers.[176]

The 500 Broadway Building is a 22-story office structure with an assessed valuation of $12 million. A breakdown of revenues generated before and after construction were computed as follows:

	Prior Use	After Construction And Occupancy
Property Tax		
Land	$10,119	$ 10,119
Improvements	4,305	4,305
Earnings Tax	1,500	163,200
Total Revenue	$15,924	$177,624

After ten years, the annual tax based on one-half of the assessed value on improvements and land should be $294,480. After 25 years, the full tax should be $425,763 annually.

The second example is the Gateway Towers, a 20-story $10.4 million office building. The revenue analysis for this "353" project is as follows:

	Prior Use	After Construction And Occupancy
Property Tax		
Land	$ 4,629	$ 4,540*
Improvements	1,137	-- **
Earnings Tax	3,600	144,460
Total Revenue	$ 9,336	$149,000

* Assessment is lower because a portion of the tract was taken for a highway widening.
**There is no payment in-lieu-of-taxes for improvement, because this provision of the law was passed later in the program. Gateway Towers utilized the program before this provision was enacted.

By 1975, the tax exemption will revert to 50 per cent of assessed valuation on all real estate. The tax should then be $256,480. After 15 years, it will rise to $367,500.

Objections to the Program. The primary objection has come from those who do not desire to see the city forego revenue through exemptions when it needs money so badly. Even the cost-benefit analysis presented above did not satisfy the objectors. Part of the resulting political compromise was the payments in-lieu-of-taxes on improvements mentioned earlier. The early projects--prior to 1968--did not pay in-lieu taxes but were wholly exempt from all taxes on improvements. The compromise lead to the "no tax loss" approach now in effect. The selling point is, of course, that the city cannot lose any old taxes, and stands to gain a lot more on other taxes.[177]

Early in the program, opponents tested the constitutionality of granting the power of eminent domain to a

private corporation for its profit. The circuit court ruled the use was public if condemnation waa used in an area designated by the city, through ordinance, as "blighted" and carried out under a contract, approved by ordinance, between the city and the corporation.[178]

Conclusions and Future of the Program. The dual use of eminent domain to assemble land, and the tax exemption to lower costs, appears to be an imaginative use of governmental powers. From all evidence, it has spurred development without the bureaucratic entanglement normally associated with such a program.

It was interesting to note that the redevelopment corporations have seldom had to use the eminent domain power even though land assembly has often involved numerous small parcels. This has been attributed to the city's procedure of making studies and officially designating "blighted" areas, then holding public hearings. In addition, the corporations have been able to legally pay more than a public agency for such land. This has circumvented the lengthy hearings and procedures for condemnation.[179]

All of these factors in combination seems to recommend the "353" program for continued use. There are several additions and improvements which are being sought, however. First, the limitations on profit now held at eight per cent should be related on a sliding scale to the market rather

than arbitrarily pegged. Second, the use of the term "blighted" in existing legislation causes undue friction among resident groups. A term with less derogatory connotations such as "development districts" is being sought.[180] Finally, because of the success of the "353" program in the central business district, the city has initiated a program of redevelopment in outlying neightborhoods. Emphasis is to be focused on declining strip commercial developments. Of four neighborhoods proposed for inclusion in the program, only one was rejected by local residents.[181]

Fringe Area Development

As mentioned in Chapter II, numerous problems have resulted from the explosive growth occurring in the fringe area of most metropolitan centers. In the fringe area, there is extraordinary competition for land. This has placed the farmer in poor economic straits in many instances, because the great demand for land has driven prices up. As prices increase, so do tax assessments. Further, as residential subdivisions and other urban uses develop, service needs, such as water, sewer, schools, and highways, also go up. Rising tax assessments, resulting from increased prices and service needs, have forced many farmers to sell out to land speculators who can temporarily absorb the increased tax load, exploit the potential value of the land, and reap a large profit in the end. The impact of the property tax

in the fringe area varies considerably between the farmer and the speculator. The speculator, in a market of rising land values such as exists in the fringe areas, usually deems the holding cost of the property tax as negligible compared to eventual earnings.

This speculative conversion of land has had three major consequences for the metropolitan area. First, it has removed land from productive uses while waiting for the market to "ripen." Second, it has further contributed to the sprawl of our urban centers and added to service costs which are already extremely high. Finally, the continuation of sprawl reduces the open space around our urban areas. Even if present tax policies do not specifically cause the above results, at least they do nothing to keep them from happening.

Tax Policies to Aid Fringe Development

Numerous states have recognized the tax/land use problems in the metropolitan fringe areas. Many of them have acted with legislation to help alleviate these problems. Two types of legislation have been advanced to deal with the problem: one is known as "preferential assessment" and the other as "tax deferral." The differences between these two types of legislation are minor but significant.

Preferential assessment laws require that in assessing farmland, assessors must consider only the factors relevant to its present use. Market trends which would have an

influence on potential use should be ignored. In the case of farmland, this allows farmers a much lower tax. Tax deferral laws have essentially the same provisions, but with an important difference. If and when the property is transferred from agriculture to another use, all or a portion of the taxes foregone as a result of the preferential assessment are recouped.[182]

Interviews designed to investigate the application of these two legal approaches included Florida which uses preferential assessment, New Jersey which also uses preferential assessments, but with a tax deferral provision, and Maryland, which has utilized preferential assessments for many years, and has recently enacted a tax deferral amendment to their preferential assessment law. Most of the provisions of these laws are similar. The results have been similar also. Therefore, to avoid redundancy, only Maryland's law will be examined in detail. Findings in New Jersey and Florida have been used where appropriate to support or contrast with the findings in Maryland.

Legislative History of Maryland's Preferential Assessment Law

After World War II, population growth in the metropolitan areas of Baltimore and Washington, D. C. caused a significant upward trend in land values around those two cities. The population explosion created demands for the conversion of rural and farm land properties into housing

developments. The price of rural land skyrocketed. Farmers found it increasingly difficult to continue a farming operation and pay property taxes when the assessments were based upon a market value created by the demand for development and residential land.

In an attempt to provide economic relief for the farmers, Maryland went through five periods of legislative enactment on preferential assessment. The first preferential assessment law, enacted in Maryland, occurred in 1955. This law required that "lands which are actively devoted to farm or agricultural use shall be assessed on the basis of such use and shall not be assessed as if subdivided or on any other use." The Governor vetoed the law in 1956, but the General Assembly overrode the veto.[183]

The second period of legislative activity came shortly thereafter in 1957, when the General Assembly repealed and re-enacted the preferential assessment law. As a result of some administrative experiences with the law, new provisions were added which were designed to aid in determining whether lands were actively devoted to farm or agricultural use. Such criteria included present zoning, past and present use, productivity and the ratio of farm or agricultural uses as against other uses.[184]

Court litigation resulted, and in 1960 the Maryland Court of Appeals declared the law unconstitutional. The

court ruled that although the Maryland Constitution permitted classification and subclassification of improvements on land and of personal property for tax purposes, it did not permit the subclassification of land.[185]

This court action led legislators to the third phase of legislative activity. Another bill was introduced in the 1960 session of the General Assembly. The old law was repealed and a replacement was enacted as Chapter 57 of the Acts of 1960. At the same time, two amendments to the State Constitution were submitted to the voters. The first proposed to amend Article 15 of the Constitution so that the General Assembly would have authority to provide for the subclassification of land for assessment purposes. A second proposal would amend Article 43 of the Declaration of Rights by allowing the Legislature to provide that land actively devoted to farm or agricultural use shall be assessed on the basis of such use and not as if subdivided. Both amendments were adopted by the voters of Maryland in November, 1960.[186]

After the initial period of conflict, the law remained as written for nine years. However, it was becoming increasingly evident that speculators were buying active farms at prices substantially above those that farmland would normally bring. Such farms would be operated only nominally, or at a temporary loss. This resulted because there were no methods detailed to determine if a person was a bona fide farmer. Speculation was the main motivation and

the preferential assessment gave speculators a tax break as well while they waited for their "farms" to appreciate. Something was needed to penalize speculation. The deferred tax provision was the recommended solution.

After several years of false attempts, the General Assembly enacted Bill 139 in 1969, which retained the provisions of the 1960 law and added two new provisions. The first was a deferred tax provision which required that when land under the preferential assessment is rezoned to permit a more intensive use or when a subdivision plat is recorded, such land will be assessed both on its use (farm) and its potential use. Taxes are paid only on the farm assessment until the land is actually sold or is converted to a higher use. The deferred tax is computed on the difference between the use value assessment and the potential value assessment. The difference in assessment is multiplied times the tax rate for no more than the three years preceding. The deferred tax was not to exceed five per cent of the "full cash value" assessment.[187]

A second provision allows preferential assessment with a deferred tax provision for large developments such as "new towns" or "satellite cities." Lands comprising 500 acres or more zoned for "new town" or "satellite city" development receive a preferential assessment equal to farm use value. Dual assessments are maintained showing values according to agricultural use and also "full cash value." When the

area or a portion of it is subdivided by recording a plat, the subdivided portion loses the special assessment and it taxed at "full cash value." If lands are withdrawn from "new town" zoning, the deferred tax must be paid for the previous ten years. The tax may not exceed ten per cent of the "full cash value" assessment.[188]

The fifth and current phase of legislative activity has attempted to increase the impact of the tax on speculation by increasing the amount of deferred taxes payable by speculators for converting land to a more intensive use. A 1972 bill, Senate Bill No. 367, had been passed by the General Assembly and was awaiting the Governor's signature at the time of the postal interview with Maryland officials. The Governor was expected to sign the bill into law at any time.[189]

Bill 367 deletes those provisions concerning payment of deferred taxes at the time of conversion and the limitations on the amount of tax to five per cent of full cash value. These were replaced by a simple addition stating that no land being assessed on the basis of agricultural use shall be developed for non-agricultural uses for three years after the time when such preferential assessment was terminated. If the land is converted before that time, a deferred tax is paid equal to <u>twice</u> the tax due on the difference in assessment between use value and "full cash value." In addition to raising the amount of the deferred

tax, the Bill provides for a permit system to deny a landowner the right to construct any buildings or improvements until the local tax collecting authority certifies the payment of all deferred taxes due.[190]

Criticisms of the Preferential Assessment Program

Many of the criticisms connected with Maryland's law stem from the fact that it was an experimental program subject to a trial and error method of evaluation. As can be seen from the legislative history, Maryland has continually changed and modified its laws concerning this program. However, even throughout the evolution of the program, it received criticism on three points: the inequality of the preferential assessment; the loss of tax revenues; and, the difficulty and expense of administration.

The inequality of the preferential assessment is evident because it allows favorable tax treatment to only one class of property owner--the farmer. However, the farmer has argued that if assessed at a market rate inflated by speculators, he is paying taxes on land value that he not only did not create but does not want.[191] If the preferential assessment is viewed as a public subsidy to help maintain farms and open space near the city, the voters overwhelmingly approved such action in the 1960 Constitutional Amendment referendum mentioned previously.

The second criticism concerning the loss of tax revenue was substantially allayed by the enactment of the

deferred tax requirements in 1969.[192] Yet, if the land owner does retain his land in agricultural use and the tax break accorded by the preferential assessment is realized, it should be viewed as a public subsidy since the deferred tax requirement does not recoup all of the foregone taxes. However, a recurring question has been whether the land owner would have acted the same way even without the preferential assessment.

The third criticism concerning administration is many-sided. The importance of a good law in the beginning with proper administration led William H. Riley, Chief Supervisor of Assessments, Maryland Department of Assessments and Taxation, to write:[193]

> The knowledge gained from efforts to strengthen the law so that only bona fide farmers would be entitled to the preferential assessment suggests that any state considering a similar...law..., should exercise extreme care in framing any such proposed legislation. Our experience has shown that once the preferential treatment is enjoyed, it is difficult to withdraw...from those not entitled or intended to receive it.

Mr. Riley readily admits that Maryland's law was too general. It allows widespread abuses by persons who were not legitimate farmers. This resulted primarily because of a lack of adequate criteria upon which a determination could be made as to whether the land was actually devoted to farming or not. In 1967, the Legislature acted to prevent abuses by directing the Department of Assessments and

Taxation to prepare such criteria. A list of 29 criteria for determining agricultural usages were established but were not evaluated as to the weight each should receive. To this author's knowledge these unweighed criteria are still in use.[194]

Another administrative difficulty was the problem of assessing land based on its agricultural use rather than on potential use as had been done in the past. A system has been developed in Maryland which categorizes land based on the productivity capability of soils. Value is determined by capitalizing the income from agricultural crop yields in each land category.[195]

The added administrative costs necessitated by maintaining dual assessments has also been criticized. Parenthetically, an increase in assessment costs was also noted by Florida officials. Neither state could indicate the degree of added expense resulting from dual assessments.[196]

Evaluation of the Program

The most important question concerning the program is whether the use of preferential assessments has actually maintained farms in the urban fringe areas. The information from the interviews could not answer this question. Mr. Riley of Maryland did relate that "Although the Department (of Assessments and Taxation) originally recommended the 1955 veto (of the preferential assessment hill), it must be conceded, in

the light of the continued upward trend in market prices, that the use value law was necessary."[197]

Florida officials, who do not have the deferred tax provision, are of the opinion that the program is ineffective. They state "in urban areas in Florida it allows the landowner to hold premium land in dense areas with favorable tax consideration while the value increases."[198] The implication is that the farmland will be sold as soon as the market's ready.

The above comments notwithstanding, an in-depth answer concerning the allocational effects of the preferential assessment program was not provided by state officials. However, a report prepared by Carol S. Meyers in 1968, does present an evaluation of the use of the preferential assessment in Maryland.

Generally, Carol Meyers advanced three conclusions concerning the use of preferential assessments. First, in instances where landowners intend to sell or convert their land, preferential assessment has little or no effect on the timing of the event. Meyer concludes from her research that aside from a few holdouts and a few who prefer to farm in the face of much greater returns from sale or conversion, most landowners will yield to the pressure of the market about the time when the land is ripe for conversion.[199]

The only discernable effects of the tax concession according to Meyer would be a possible prolonging of the

pre-development or speculative period and possibly a delay of the final conversion not amounting to more than one and one-half years. However, Meyers does state that the quality of land development is probably significantly better because of preferential assessment. The tax relief provided farmers allows the maintenance of large land inventories which is much better for future land development.[200]

Meyer's conclusion that the tax concession does not have a significant impact on the timing of land conversion would appear to be supported in part by the fact that Maryland has enacted a tax deferral provision and then doubled it in an attempt to control speculation. On the other hand, it can also be argued that the tax deferral itself does not control speculation. Although a farmer's assets are generally illiquid, thereby making a current, high tax especially onerous, the deferred tax allows him to pay the higher tax rate only after he sells the land and has sufficient cash on hand. Viewed in this light, the deferred tax allows a farmer to become a speculator when he might not otherwise be able to do so.

The second conclusion advanced by Carol Meyer is that where landownders intend to continue farming and can do so only with a tax break, preferential assessment may be a solution. But, it is desirable only if the public is willing to suffer the loss in revenue in order to prevent premature conversion. In other words, the tax concession is

desirable only if public objectives coincide with private intentions.[201]

It is easy to realize that not all farmland should be maintained around metropolitan areas. Meyer points out that to assure that public policy and private intentions coincide, the state should officially designate specific areas for open space or other development objectives. In this arrangement, only lands publicly identified for maintenance as farmland should be given the preferential assessment.[202]

The final conclusion pertains not only to preferential assessments, but to most tax concession measures. Meyer concedes that tax policies could have leverage on land development, but the consensual nature of tax concessions means the public must be willing to assume a sizable risk of failure. Not all such programs will be subscribed. In addition, not all tax programs will have the intended effects, since many factors are at play in the land market. Meyer concludes that tax programs should be backed with other control measures, such as zoning. However, if these controls are highly effective, many times tax policies are not necessary.[203]

Overall Urban Development

The final set of case studies analyze how the property tax affects overall urban development. The land value tax, or a variant of it, was chosen as the tax program

because of the claims of its adherants. As Chapter II outlined in detail, property tax reformers have long held that the land value tax would force landowners to make the most economic use of their land and avoid speculative withholding of land. In addition, the land value tax would not penalize those who improved their land, since taxes would remain the same regardless of improvements. Consequently, with these overriding influences, the complete urban area would be continually renewed and rehabilitated.

In the United States there are several examples of land value taxation at work. However, all jurisdictions in the United States using the land value tax principle have modified it in some way. The jurisdictions in the United States using a modification of the land value tax are Pittsburgh and Scranton, Pennsylvania; the State of Hawaii, and; the "Single Tax Corporation" of Fairhope, Alabama. Of these, the "Single Tax Corporation" comes the closest to using the land value tax in an unmodified form. Both Fairhope and Hawaii were studied in an attempt to uncover new information on the use of land value taxation.

Practical application of the land value tax was researched through surveys and interviews with officials in the State of Hawaii and Fairhope, Alabama. The "graded tax" of Pittsburgh was not used because Hawaii's tax program

resembles Pittsburgh's very closely. In addition, interview responses from Pittsburgh were insufficient to add any new information to existing literature.

Hawaii

Hawaii has long been painfully aware that its land resources are limited. Hawaii's graded tax law is only one facet of a multiple approach to land reform. A general plan for the state was developed and adopted in 1961. The State Land Use Act was the first of its kind in the United States. The graded tax law, Act 142, was passed by the State Legislature in 1963. For various reasons, the tax law did not become fully effective until January 1, 1965.[204] Its basic intent was to encourage the highest and best use of land throughout the state. It was felt that the application of differential tax rates on land and buildings, with the higher rate on land, would encourage the development of vacant or underdeveloped land.

Hawaii is unique among most of the states in that property tax administration is highly centralized. In addition, its property tax is state-imposed, although once collected, the funds are turned over to the counties. The state makes all appraisals and assessments, and administers and collects the real property tax. Counties on the other hand, set tax rates which are uniform throughout the county. Under this system, assessment of real property in Hawaii has

been uniform and equitable.[205] Such a commendable record is unusual from a state in which property taxes comprise only 17 per cent of the total tax burden as compared to a national average of about 45 per cent.[206]

Provisions of the Act

The implementation of the law came in two phases. In the first phase, all land had to be classified into the following classes based on its highest and best use: 1. Residential (single family and two family); 2. Hotel/Apartment/Resort; 3. Commercial; 4. Industrial; 5. Agricultural; 6. Conservation. To classify properties into one of the above general classes, consideration was given to the state's land use plans, and also to the counties' zoning ordinances and districts.[207]

The second phase of implementing the law provided that differential tax rates be applied to properties in each of the first four categories. A single tax rate is applied to agriculture and conservation districts. Differential rates are obtained through the use of a "building tax factor" in the computation of the rates. Beginning in 1965, the building tax factor was 90 per cent. This meant that the building tax rate was 90 per cent of the tax rate on land. The law specifies that this factor was to continue for two years, at which time the factor would be lowered to 80 per cent. Future reductions are limited to a 10 per cent

drop every two years until it reaches its statutory minimum of 40 per cent.[208]

However, the law also provides the Governor with the authority to defer the reductions for two years. The Governor exercised the prerogative in 1967 and the building tax factor was not lowered to 80 per cent until 1969. The factor was scheduled for another 10 per cent reduction in 1971. The Governor has also deferred this decrease until 1973. In 1973, the building tax factor dropped to 70 per cent of the tax rate on land.[209]

Effect of the Tax Program

Since Hawaii's tax program has only been in effective operation for eight years, and the implementation of the differential rax rate has been slow, it is difficult to make conclusive judgements concerning its effect on land use and development. However, based on interview responses, and interview materials supplied by respondents, four general conclusions were evident: (1) the differential tax has forced more idle land into use; (2) it has caused a shift in relative tax burden from improve (new) residential uses to unimproved (old) residential uses; (3) it has caused land to be used more intensively; (4) it has contributed to the increase in construction activity.

The effect of the tax to force more idle land onto the market is based on examples on Oahu, the most urbanized of the islands. Shortly after the passage of the tax law,

many of the large landowners on Oahu entered into development agreements with land developers. This action transferred the development rights in the land to land developers; it also transferred the tax burden to them. The Bishop Estate, the largest private landowner in Hawaii, transferred the development rights to practically all its developable lands on Oahu to developers.[210]

The shift in tax burden from the newer and more expensive homes to the older and lower valued ones was considered socially undesirable by state officials.[211] The differential rate allowed the effective tax rate to be higher on older homes than on newer, more expensive ones. This penalized taxpayers living in older homes and those less financially able to make substantial improvements in their property.

This problem was circumvented with the passage of Act 218, Session Laws of Hawaii, in 1969. The Act removed this inequity by dividing the residential class into two groups: Improved Residential (older homes) and Unimproved Residential (new homes). The use of the building tax factor is no longer used in the computation of tax rates for improved residential properties.

Officials noted that in some instances the tax law has led to over-building at the expense of aesthetics and open space. These effects have been noticed in the City of Honolulu and in Waikiki, which in some portions, approaches

maximum utilization of land. To counter these effects, the legislature has considered allowing tax exemptions to certain hotel and commercial properties in order to preserve low density surroundings where this is desirable for scenic, cultural, or historical purposes.

The increase in construction activity attributable to the tax is completely a matter of conjecture. Hawaii has been growing steadily since 1955, and just recently went through a construction boom. It is felt by state officials that the tax program has contributed somewhat, but to what extent is unknown.

Fairhope, Alabama

Probably one of the most unusual examples of utilizing taxation to influence land use and development is the "single tax" enclave in Fairhope, Alabama. The missionary zeal of Henry George's single tax movement infected seven families of Des Moines, Iowa in 1894. In November of that year, seven families incorporated as the Fairhope Industrial Association. Ten years later, after favorable legislation had been adopted by the Alabama legislature, they were reincorporated as the Fairhope Single Tax Corporation.[212]

The Single Tax Corporation purchased approximately 160 acres of land on the east side of Mobile Bay. The Corporation had as its purpose the creation of a model

community, based on the single tax concept of Henry George. What has evolved is a situation in which the Corporation leases land parcels for a period of 99 years. An annual rental is paid which is equal to "the market value set by those who want land to use at its fullest productive capacity."[213] From the revenues generated, the Corporation pays all other property taxes and assessments made by all governmental jurisdictions on the lessee except those of the Federal government.[214]

The model community became the nucleus of what is known today as Fairhope. Although the Corporation has since grown to about 4,000 acres, of which 400 are within the city, it is now only an enclave within the larger community of Fairhope.[215] Less than one-fifth of the City of Fairhope is represented by the Single Tax Corporation.

The Corporation is subject to all ordinances, such as zoning, imposed by Fairhope and Baldwin County, Alabama. Because of its corporate status, the Single Tax Corporation is dealt with as a single entity by state and local tax assessors. During 1971, the Corporation paid a total of 41 mills per $1,000 at an assessment ratio of 20 per cent of market value to the State of Alabama, Baldwin County, the City of Fairhope, and the local school district. Property taxes amounted to $71,347 in addition to $19,935 in corporate income taxes.[216] Although the Corporation's property tax was derived from assessing both land and improvements, the

Corporation continued to realize its revenue from lessees completely through rents based on land value.

Factors Limiting the Effectiveness of the Tax Program

During the course of this study, the author traveled to Fairhope to observe the development of that community and discuss the effect of the "single tax" with local officials. Although local officials were overwhelmingly in favor of the "single tax" concept, they recognize the reality of the conditions under which they operate. Namely, these are:[217]

1. The Single Tax Corporation is an entity which is taxed by state and local governments using normal property and income tax laws. This mitigates the economic incentives inherent in land value taxation. If improvements are made to property, they raise the state, county, and city property assessments for the Corporation's holdings. The Corporation must accept and apportion this added cost regardless of its own tax structure.

2. The Single Tax Corporation is an enclave within the larger Town of Fairhope. Consequently, the Corporation must abide by other land use controls such as zoning. Officials of the Corporation criticize such controls as artificial restraints which are relatively inflexible and in some instances superfluous.

3. Being an enclave also produces problems because of the proximity of "deeded" land to the Corporation's

"leased" land. Since all of the Corporation's holdings are not contiguous, situations arise in which properties of similar potential, but both not being subject to the Corporation's control, may exist side by side. In such cases, the effects of the Corporation's single tax are not easily discerned.

4. Even though the use of a parcel of the Corporation's land involves signing a legal contract and making monthly payments to the Corporation, some lessees do not understand the land utilization implications of the arrangement. An example cited by local officials concerned central city commercial property. In this case, the property was controlled by absentee lessees who allowed the commercial property to stand vacant, but retained the lease. Ostensibly, the lessees mistakenly felt they were building equity and/or desired to retain the property for speculation purposes. Building equity is impossible under the lease, and if rents had been high enough, speculation would have been too costly.

Observations of the Tax Program

Because of the limiting factors mentioned above, it is difficult if not impossible to present empirical data which proves or disproves the effectiveness of the land value tax on urban development. However, based on interviews, first-hand observation, and a review of the material made available by the Single Tax Corporation, several

observations were made by this author concerning the use and possible effects of the "land value tax" in Fairhope.

Administration. Since the Corporation must pay for all of its taxes and other expenses solely from the rents charged its leasees, the computation of such rents is an important consideration in the Corporation's affairs. During the course of its history, the Corporation has had several consultants attempt to provide a method for assessing site rent based on the potential value of each parcel. William A. Sommers contributed the "unit system" of land valuation in 1915. Although an improvement, it was not until the period between 1966 and 1970 that a more satisfactory method of evaluating community improvements and setting absolute rent values was established. Arther P. Becker of the University of Wisconsin was engaged to help provide this information.

What evolved from this four year study was a site valuation method based on a contour map of land values relative to a "100 per cent corner" which is the intersection with the greatest amount of pedestrian and vehicle traffic. These raw values were then modified by a system which deducted value for defects such as unpaved streets, no sidewalks, or the lack of available utilities, and added value for such amenities as access to Mobile Bay or a view of a park. Although the system could be used and computed

manually, the Corporation programmed the operations for use in a computer.[218]

What is important from the foregoing information is the fact that the calculation of site value can be accomplished. This has been a criticism of site value taxation in the past. The administrative success of site valuation even in the early years appears to be borne out by the fact that the Single Tax Corporation has never been insolvent. Even during the Depression of the 1930's, the Corporation remained solvent. In addition, the Corporation has over the years used surplus revenue to construct a library, provide a playground, place about 66 acres of its holdings into parks, construct a pier and develop a beach, donate land for the first school, and operate and maintain a cemetery.[219] Adequate revenue production did not seem to be a problem for Fairhope.

Land Speculation. Theoretically, high taxes on land of great potential value will cause a greater utilization of these advantageous areas. Practically speaking, this will generally mean that a city under land value taxation would develop more intensively and more completely from the central business district outward to its fringes. High land taxes would help prevent speculative withholding of land by making the holding too costly.

These benefits of land value taxation appeared to have taken place in Fairhope at least to some degree.

According to local officials, the Town of Fairhope grew in the Single Tax Corporation's jurisdiction, and completely utilized all of their initial land holdings before moving into the hinterland and onto "deeded" land. Within the central business district, even at present, there are some vacant buildings under the jurisdiction of the Corporation. However, these vacancies were attributed to several causes:[220]

1. Obsolescense of structures making them inefficient in competition with new structures;

2. Since Fairhope is relatively small there is not enough market demand to cause immediate turnover and reuse;

3. The absentee-lessees of these structures do not understand the lease and assume they are building equity and holding the land and buildings for speculative purposes.

Local officials did not deny that speculative withholding of land occurred in Fairhope. However, speculation was said to occur because land rents were not high enough. In turn, low rents resulted from a long "lag-time" in reevaluating land rents. In fact, there was some evidence that land value taxation does work in the direction of releasing land from speculation. In one area, a new road and a school were built. Adjacent Corporation property remained idle for some time. After rents were reevaluated, and the new rents on the property were substantially raised, the old leasees terminated their contract and the land was leased for

development shortly thereafter. Negative evidence of the economic pressure exerted by the land value tax is the fact that of the vacant parcels in the central business area, all of the land is "deeded" property.[221]

Adverse Social Consequences. In many accounts of the effects of land value taxation, mention is made of the fact that the tax becomes too high for those unable to effectively utilize the land. In Hawaii, it was the older homeowners who were unable to pay the increased taxes. This did not seem to be a problem in Fairhope, because the area is predominantly rural, and the effective tax rate is low.

In other areas the land value tax is faulted because it forces out open space and recreation areas, since these uses are normally not as competitive in generating a return. In Fairhope, this was not a problem simply because the Corportation had already designated certain parcels as parks, schools, the library, or as open space, and had taken them out of economic competition.

CHAPTER V

CONCLUSIONS AND RECOMMENDATIONS

Based on the research information reviewed and the survey of individual tax programs, several conclusions have been drawn concerning the use of the property tax as it relates to land use planning.

Conclusions

1. Both administrative and substantive problems exist with the property tax which influence land use investment decisions. In many cases, this influence is detrimental. Of the reform proposals implemented thus far, the most successful have been those regarding administrative faults. Very little experimentation with substantive reform has been made. Because of this, legislators continue to retreat to property tax exemptions as a means of correcting substantive defects in the property tax.

2. With the exception of the tax systems in Hawaii and Fairhope, Alabama, the incentive measures studied in the case studies were based on the traditional property tax system. Such incentives involve exemptions, abatement, or deferral of the property tax. This type of exemption incentive is by far the most common.

Such incentive exemptions are normally used only to achieve specific objectives such as additional industry, the

construction of new housing or renewal. The incentive exemption usually does not consider the total system of taxation. The Hawaiian and Fairhope examples, however, did attempt to provide a total tax system which would have desirable allocational effects on land use and development. More study needs to be made along these lines.

3. Individualized tax programs had very few means of evaluating the effectiveness of a tax measure. None of the case studies revealed a cost-benefit study having been prepared by the local government. In fact, few if any records are kept of the revenues foregone as a result of tax subsidies, much less the amount expected to be brought in as a result of the tax exemption.

4. Generally, many of the tax programs were coordinated with an overall plan of development or with well-defined objectives. It also appeared as if many of the tax programs would be more effective if they were coordinated with other regulatory controls. The combination of zoning districts with tax districts in Hawaii is a notable example.

Although the evidence is mixed, it is also concluded that the property tax can be used as a device to induce desired land use and development activities. Setting forth the conditions under which the property tax should be

manipulated to achieve desired objectives and suggesting the steps the planner should follow in accomplishing this task is the objective of the balance of this chapter.

Reform of Exemption Procedures

Before attempting to outline any method for utilizing the property tax to achieve land use objectives, it should be emphasized that any realistic program to so use the property tax will probably be in the form of an incentive exemption. This conclusion is reached by virtue of the fact that very few substantive reforms to the property tax appear to be politically and/or socially acceptable at this time. Consequently, this means the property tax in its present form will continue to be used, and exemptions historically appear to be part of that use.

If substantive reform of the property tax is not feasible, there are numerous administrative reforms especially concerning the use of exemptions, which are needed. Generally, these reforms fall into three areas of need:

1. Provide Accurate, Published, Continually Updated Inventories of Exempt Properties

Among others, the Advisory Commission on Intergovernmental Relations, the National Congress of Cities, the National Committee on Urban Problems, and the National Tax Equality Association have all gone on record recommending such accounting of exempt properties.[222] This action is a

necessity in allowing proper analysis and evaluation of a tax program. It also helps keep tax subsidies from being buried in legislation and continued unnecessarily.

2. Clarify Vague and Permissive State Tax Laws and Exemption Provisions

The Advisory Commission on Intergovernmental Relations has recommended that each state should examine its tax laws and if necessary rewrite and recodify them.[223] Specifically, states should rid themselves of all features which are impossible to administer or which cannot be competently administered. Constitutions should be divested of all details which prevent sound utilization and administration of the property tax. Defects caused by property classification and/or exemptions should be eliminated. No new changes should be undertaken without adequate study of the impact and implications of each proposal. All exemption provisions should be as explicit and free from interpretation as possible.

3. Revenue Production Problems for Local Governments Should be Eased as Much as Possible

Part of the problem with the property tax today and with any attempt to use it to achieve land use objectives is the primary necessity of supplying revenue for local government. Exemptions have a way of building up until the local government no longer has any flexibility in its tax procedures without risking insolvency or a burdensome debt.

Some exemptions, however, cannot be avoided by local government and continue to drain the local treasury. Numbered among such exemptions are usually such properties as state, federal, and local public buildings, churches, or other constitutionally exempted charitable organizations and other "state-mandated" exemptions such as the homestead exemption or education exemptions. Although unavoidable, the exemptions should not impose an unfair burden on local government revenues.

To ease the revenue production problems created by such exemptions, local governments should receive:

1. Intergovernmental payments in lieu of taxes for those public properties normally exempted;

2. State reimbursements for constitutionally mandated exemptions such as those for homesteads, veterans, or educational properties; and,

3. Payment of charges for municipal services provided to exempt organizations.

Local governments would probably be on better financial footing if all local services were charged to the user as a separate fee. However, even when the financing of local government services is strictly from tax revenues, exempt organizations should pay for those services.

Guidelines in Tax Policy Formulation

The exemption reforms listed above will normally occur at the state level. How effective local tax measures are may

depend in part on these reforms. Since each state is different in its tax policies, the planner should begin his analysis of any tax/land use proposal with a thorough perusal of his state's tax policies, attitudes, and legislation especially as they pertain to the above exemption reforms. This preliminary action should be part of any planner's familiarization process with planning legislation in his state.

Using the research and especially the information derived from the case studies in Chapter IV, the following guidelines are offered for the planner's consideration in formulating tax/land use policy. Although each guideline is framed with the design of implementing a tax exemption measure, these guidelines should prove to be useful in analyzing other types of tax measures as well.

1. Determine the Land Use or Development Objective

The planner should spend adequate time in determining the specific development objective(s) which need to be achieved. In many instances, a very detailed knowledge of the economic aspects of a problem must be known in order to properly evaluate the impact of a tax measure.

2. Determine the Relative Need or Urgency of the Objective and the Level of Assurance That it be Accomplished

Tax exemptions have three inherent problems: First, they almost always require legislation and/or legal preceedings before they can be implemented. Second, the affected taxpayer is usually the initiator in actually implementing

the tax exemptions. The taxpayer may or may not subscribe to the tax program. Consequently, this will produce variable results. Third, as Carol Meyer points out, many other forces operate in the land market besides taxation which will influence decisions. Because of this, tax exemptions sometimes do not have the intended results.[224] All of these drawbacks mitigate against using a tax program to achieve rapid results and a high level of success. Such results from a tax policy are not impossible however.

3. Explore Tax Policies in Relation with Other Implementation "Tools."

Once the planner has given sufficient consideration to pinpointing specific objective(s) and relating those objectives to other needs, he should investigate the various policies and controls which he may bring to bear on the problem. Care should be taken to match implementation measures with objectives. For example, if a high level of assurance in achieving the objective is needed, outright purchase or condemnation may be more satisfactory than a tax incentive.

The planner should examine what other jurisdictions are doing to accomplish similar objectives. Such research may prove helpful in suggesting alternative courses of action as well as exposing programs which prove to be defective.

Examples in other areas may also suggest coordinated uses of several implementation measures. In the New York City case study, for example, tax exemptions did spur

multi-family development. Builders, however, revealed that zoning controls, if modified to permit higher densities and more bulk, would aid the tax measure by allowing builders to increase their return per acre and, in turn, lower housing costs. Such suggestions can prove invaluable to the planner in formulating a tax policy.

4. Examine the Function and Effects of the Property Tax in the Local Area

After preliminary investigation, the planner may decide that a tax policy involving manipulation of the property tax could prove to be effective in achieving desired objectives. An important step in evaluating any property tax policy would involve a detailed examination of the property tax as it functions in the local jurisdiction. Some of the questions which should be answered are:

a. How much of the local revenue is derived from property taxes?

b. What is the effective rate in the area, and how does it compare regionally?

c. Is the local area fragmented into many tax jurisdictions?

d. If a specific tax program is suggested, what number of taxpayers would be affected?

e. Are local assessments administered fairly and efficiently?

The answers to the above questions will allow the planner to assess the use of the property tax in his

local jurisdiction, and thereby judge the effect the property tax may have on land use and development decisions.

5. Evaluate the Need for and Impact of a Tax Subsidy

This step in the tax policy formulation process is the most time consuming, difficult and critical to any program. It is at this stage that specific tax subsidy programs must be analyzed. Establishing guidelines for the evaluation of a tax policy is hazardous at best. Nevertheless, there are several basic questions which the planner must seek answers to:

Should the local government spend funds to achieve the objective? The costs of a tax exemption program should be evaluated to determine the desirability of the program. One tax authority points out that property taxes are a legitimate cost of business, and a tax exemption means that the local government is subsidizing this business cost. For this reason, he stipulates two criteria for tax exemptions:[225]

First, property tax exemptions should only be used in rendering a service affected with a bona fide public interest. Discerning the public interest should not be difficult if the desired objective is the result of a plan which has survived public scrutiny and debate and has been properly adopted by local officials.

Second, the tax exemption method of subsidizing a service should not be used unless it can be done without serious

disproportion between the benefits and the cost to the community concerned. If the tax subsidy exceeds the benefits resulting from the program, subsequent revenue losses should only be foregone by public consent based on the desirability of the subsidized activity. In many cases, the planner will be able to calculate the costs and benefits in a specific tax exemption program before committing the local government to any subsidy. If this can be done, it should be. If not, there should at least be a periodic evaluation of the effectiveness of the tax program.

Will the tax subsidy achieve the intended purpose? The planner should make every effort to quantify the level of subsidy needed to achieve the desired result. Once quantified, the proposed subsidy should be examined to determine its market impact toward the objective. In addition, the overall effects upon the land use and tax rates of the community which might result from the indirect impact of the tax subsidy should be examined.

To exemplify the point concerning the need to quantify the level of subsidy, New York City's case study can be used. One objective--as stated in the provisions of the New York enabling act--of the tax program was to reduce housing costs by 15 per cent or more. Based on this objective, the subsidy was presumably calculated. Preliminary results showed that housing costs in three subsidized developments were in fact decreased by 27 per cent, 14 per cent, and 35 per cent

respectively.[226] The framers of New York City's housing program were relatively accurate in setting their subsidy level.

Carol Meyer provides further insight into the planner's assessment of whether the subsidy will achieve its intended purpose. Although Ms. Meyer deals with the provision of open space in her study, some generalizations can be made from her observations. Meyer asserts that in determining the adequacy and necessity of a tax subsidy, the planner must weigh several factors: the development potential of the property; the owner/taxpayer's intentions; and, the owner's financial position.[227]

The development potential of the property is critical. Meyer maintains that property with high development potential will be almost completely immune to even a 100 per cent tax exemption if it encumbers the use of the land for development. Of course, this depends on the type of development potential and the objective of the tax subsidy. But if the two are at cross-purposes, it is most often the case that the tax subsidy is relatively small in contrast to the profit to be realized and consequently will not be subscribed.

Also important is to determine the property owners intentions as well as his financial position. The farmer who is determined to maintain his land in low density use in an area of urban growth or the subdivider who wishes to state a large residential development, are specific examples of situations in which a tax subsidy may aid them in

accomplishing their objective. Meyer emphasizes that if the taxpayer's financial position is illiquid, a tax subsidy, especially an abatement, will probably be more heavily subscribed. Meyer's point is important to the planner in that he must gain some appreciation of whether his proposed tax program will be subscribed. If not, then the program does not stand much of a chance of achieving its purpose.

Would the objective of the subsidy be better achieved through a direct expenditure? Some of the pros and cons of using tax subsidies or a direct expenditure are outlined in Chapter III. These social and political considerations need to be weighed before the tax policy is formed. Socio-political factors may play a great part in determining which type of subsidy should be used. The planner should take care though not to allow a tax subsidy to be used merely to hide the expenditure from public scrutiny.

6. Examine Specific Needs for Legislation

Once a particular tax policy is proposed, the planner must examine existing legislation to determine if his tax policy can be implemented with existing legislation. If so, he must determine any further legal steps necessary to bring it into being, such as a local ordinance, a referendum or other measure.

If existing legislation is not sufficient, the planner must determine what would be necessary to obtain proper authority. This may require a state statute or a

constitutional amendment. These considerations will be dictated by the specific tax program. One further legal consideration is the advisability of providing a test case for those legislative enactments which may pose constitution questions. Similar to the test cases for Urban Renewal, such action would allow policymakers the knowledge of the legality of their actions before making substantial investments of public funds.

7. Careful Attention Should be Paid to the Implementation of the Tax Program and to Administrative Considerations

Great care should be exercised in developing the administrative rules of the tax subsidy so as not to allow the subsidy to be used by unintended persons. Once a taxpayer maneuvers himself into receiving the subsidy, it is difficult to withdraw it.

The administration of the tax subsidy program should be oriented as much as possible toward discerning the effectiveness of the program and assuring the program does not continue without being effective. Several recommendations are offered which can aid in this purpose:

a. Set up an accounting system for the subsidy expenditure, and if possible, quantify the benefits received from the subsidy.

b. Establish an expiration date for the subsidy and/or allow for a periodic evaluation of the program's effectiveness.

c. Monitor the program for adverse effects from indirect impact of the subsidy as well as its intended allocational effects.

d. Tie the tax program through administrative procedures to the overall plan which is being implemented if possible. For example, as was suggested in Maryland, before a bona fide farmer should be able to obtain a preferential assessment on his land to help maintain it as open space, his property should be identified as such in an open space plan. Administrative procedures should be set up to accomplish such coordination.

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