

Testimony on the benefits of land value taxation programs

Prof. Jeffrey P. Cohen

**Professor of Economics, University of Hartford
David C. Lincoln Fellow, Lincoln Institute of Land Policy**

Municipal Tax Authority Sub-Committee

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PLACE

COMMENTARY ABOUT WHERE WE LIVE

'Split Tax' Would Encourage Buildings – Not Vacant Lots

By JEFFREY P. COHEN

Legislation proposed earlier this year would have authorized Connecticut's large cities to levy a two-rate tax, also known as a "split tax," on land and buildings. Mayor Eddie Perez supported the idea, and is likely to push for it again next year.

At present, the tax rate is the same on land and buildings, but the assessment, the valuation of the property for tax purposes, is different.

On average in Hartford, 15 to 20 percent of an assessment is for the land and 75 to 80 percent is the value of the building (For downtown high-rises, well over 90 percent of the valuation is for the building.) So if a property is assessed at \$100,000, to use a round number, \$80,000 to \$85,000 is the value of the building and \$15,000 to \$20,000 is the land it sits on.

Since the tax rate is the same, the owner pays much more tax on the building than on the land.

What if that were reversed? What if the majority of tax were instead paid on the land? Would the change make a difference? Would it be sound public policy for Hartford?

A high tax rate on buildings in Hartford might be part of the explanation for urban decay, because it encourages the abandonment of marginal buildings and discourages repairs, because the work will cause taxes to rise.

So, the higher tax on buildings leads to a decrease in the number, quality and sizes of buildings that residents and businesses want. In a number of cases, major buildings have been demolished to save on the tax bill.

Unlike the number, quality and size of buildings, the amount of land in Hartford cannot change, re-



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WITH TAXES HIGHER ON BUILDINGS than on land, Hartford policy seems to encourage empty property and surface parking lots.

ardless of whether the land tax rate rises or falls. An owner cannot demolish land to save on taxes. So an increase in land tax would not affect property owners' behavior in the same way as a higher tax on buildings. In theory at least, since there would be less tax avoidance, the city would collect more tax revenue.

Advocates of the split tax believe lower taxes on buildings would encourage renovation and new construction, because there'd be less of a penalty for doing the work. Also, there would be a greater incentive for people to replace abandoned buildings and parking lots with useful structures such as affordable housing.

Looking at these advantages, some people might wonder why the city needs to have a tax on buildings at all. The reason is that if the building tax was completely eliminated and the tax on land was increased high enough, some landowners might abandon their land. This likely would mean that the city would have to take over that land, making development more difficult in Hartford. So a split tax may be a happy medium, encouraging development with lower taxes on buildings and making land taxes higher but not too high.

There might be other drawbacks to a split tax. Since Hartford will need to collect at least as much in tax revenues as it does now, some property owners will pay higher taxes than they do now, and some will pay less. People living in the homes with big yards near Elizabeth Park might pay higher total tax bills, if that area were in the split-tax zone, and the future residents of the high-rise condos planned for downtown may see much lower tax bills. Is that what city officials want?

It is possible that lowering building taxes too much could lead to overdevelopment and increased traffic congestion, unless carefully proscribed by zoning. And, doesn't the city need some surface parking lots and open spaces?

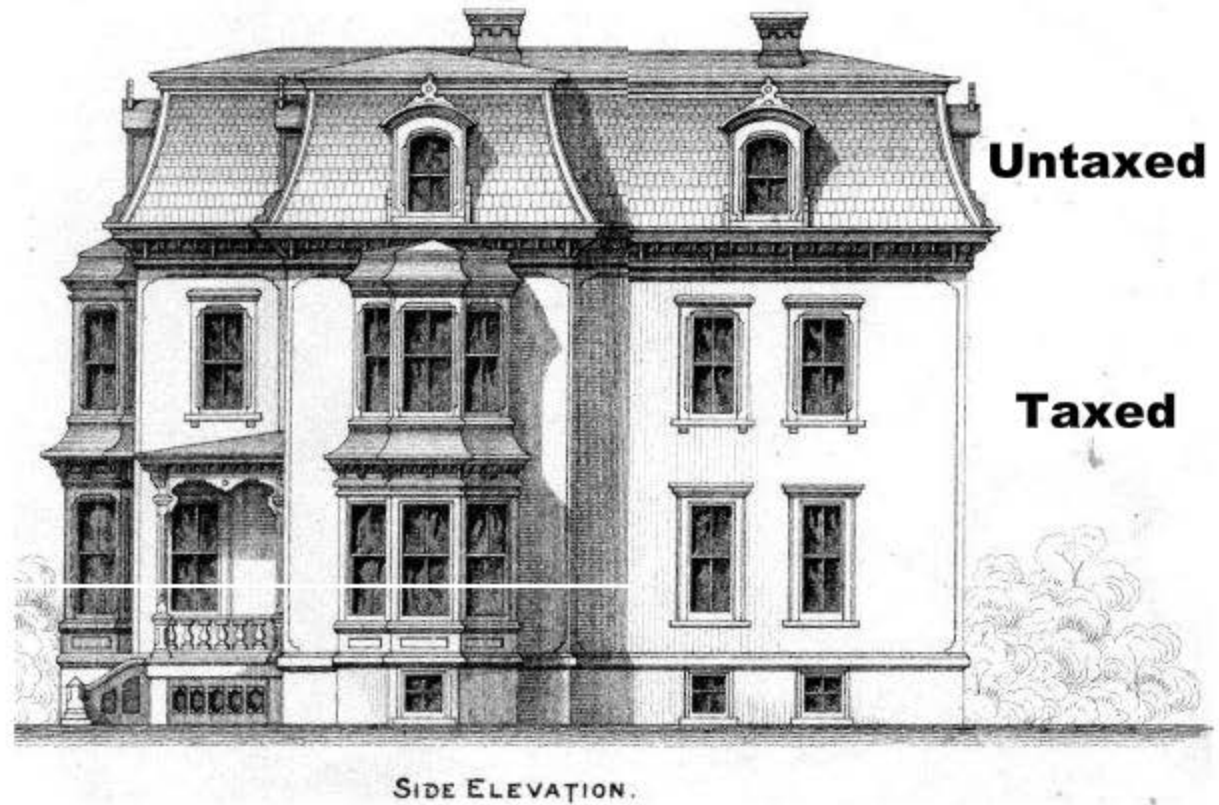
The split tax is a promising idea whose effects cannot be accurately be predicted without some experience. So perhaps the answer for the legislature is a limited experiment or a pilot program, to see how it works. It certainly is worth a try.

Dr. Jeffrey P. Cohen is an associate professor of economics at the Barney School of Business, University of Hartford.

Benefits of a Land Tax

- Taxes on Improvements Discourage Development
- A Land Tax Can Encourage Improvements on Land
- Examples of Consequences of Taxes on Improvements:
 - Shotgun Housing in New Orleans
 - Delaying major renovations on residential property
 - Mansard Roofs (first started in 17th C. France)

Mansard Roof



Benefits of a Land Tax (continued)

- In some cities in Connecticut, such as Hartford, vacant land (e.g. parking lots) are abundant
- If raise tax on land, lower tax on improvements, would encourage development without affecting amount of land in cities: George (1879); England (2007); Cohen and Coughlin (2005); Oates and Schwab (1997); Dye and England (2010)
- e.g., if raise tax on land, boundaries or the size of Hartford would not change

Benefits of a Land Tax (continued)

- More difficult for taxpayers to “escape” land tax than most other types of taxes (including sales tax, motor vehicle tax, etc.)
- Government can raise more revenue with land tax, while not discouraging mutually beneficial transactions
- Greater construction from lower improvements tax can be expected to increase retail sales, job creation

Benefits of a Land Tax (continued)

-PA results: Land use is more capital-intensive in cities with higher land taxes than building taxes; also can combat urban sprawl

(Yang, 2013)

-Sales tax results for AZ and PA:

-There can be significant improvements in benefits to consumers and producers from additional transactions (~ \$500 million annually in 21 MSA's in these two states) if state and local sales taxes were eliminated, and replaced with land tax (Cohen, 2013)

Benefits of a Land Tax (continued)

Progressivity:

- Land Tax can be more progressive than other forms of taxation (such as sales tax, which is commonly considered regressive)
- Schwab and Harris (1999): Washington DC
- Bowman and Bell (2008): Roanoke, VA

Land Taxation in CT: A Reality

Pilot LVT Program in CT: Public Act 13-247, Sec. 329:

- Secretary of OPM shall establish application procedure for municipalities
- Up to 3 municipalities may be selected by the Secretary of OPM
- After selection, municipalities form committee to develop a LVT plan
- By December 31, 2014, municipalities' plans are to be submitted to the Connecticut General Assembly