International Property Tax Institute

PRESIDENT'S MESSAGE

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As this will be my last monthly newsletter before the forthcoming festive break, may I take this opportunity to wish you all a relaxing and enjoyable time with family and friends over the holiday period.

I read an interesting paper published recently by the Institute on Taxation and Economic Policy titled "America Used to Have a Wealth Tax: The Forgotten History of the General Property Tax". Below are selected extracts from the paper.

The authors state: When Americans hear "property tax," they tend to think taxes on houses and other real estate. And for good reason. While property taxes are often levied on motor vehicles, and occasionally on business net worth, the vast majority of property taxes in the U.S. today apply only to real estate. It was not always so. The historic "general property tax" applied to almost all property, including intangibles like stock, bonds, cash on hand, accounts receivable, and interest in a partnership. Once a mainstay of American public finance, the general property tax helped finance the nation's early industrial growth.

Over time, these broad wealth taxes were whittled away to become the narrower property taxes we have today. These selective wealth taxes apply to the kinds of wealth that make up a large share of middle-class families' net worth (like homes and cars), but usually exempt most of the net worth of the wealthy (like business equity, bonds, and pooled investment funds). The rationale for this pared-back approach to wealth taxation has grown weaker in recent decades as inequality has worsened, the share of wealth held outside of real estate has increased, and the tools needed to administer a broad wealth tax have improved.

The general property tax was an idea ahead of its time and reviving this American tradition in some form is worth a closer look. In the immediate postbellum U.S., property taxes routinely used a broad definition of property. That meant real estate to be sure, but also real personal property such as valuable possessions (vehicles, livestock, etc.), and intangible personal property (value of debts, business equity, intellectual property, etc.). Local general property tax receipts grew dramatically for decades - from about 2 percent of Gross Domestic Product in the 1850s to 5 percent in the 1920s. These collections were substantial; in 1902 local revenues were close to state and national revenues combined. But by the 1930s, cracks were beginning to show in the system as states had trouble enforcing their taxes.

Michigan's experience offers a useful illustration. At the turn of the 20th century, the state was about to enter a period of remarkable dynamism and prosperity powered by the Great Migration and the automobile industry. In 1893, the state passed The General Property Tax Act, which authorizes the state's property tax to this day (albeit in an extensively amended form). Its aim: to tax the fair market value of all property in the state. At the time, this was standard.

In 1893 Michigan taxed all property - including intangibles - at the same percentage of its "face value." But over time, different rates were introduced for different property types to promote greater compliance with the tax. As of 1940 the state had an expansive intangible property tax that included "moneys on hand, on deposit or in transit, shares of stock and other units of interest in corporations, … and any and all other credits and evidences of indebtedness, whether such intangible personal property is secured or unsecured."

The tax rates on these properties were generally lower than on real property. The rate charged for most intangible property was the greater of 0.1 percent of the face value or 3 percent of income generated. For shares of stock in building or savings and loan associations the rate was 0.04 percent, or $0.40 per $1,000.

The early 20th century was a pivot point for American tax policy. In the immediate postbellum U.S., property tax administration was less formalized than it is today. Real property - acres of land, barrels of bourbon, head of cattle - was on relatively public display, but markets were smaller and less liquid, and therefore assets were often difficult to value. Although property taxes did raise significant revenue, assessments were less than comprehensive, constrained as they were by the technology of the day.

As the tax historian Joseph Thorndike has explained: "The general property tax … was a tax ill-suited to a world chock-full of intangible property but not yet endowed with a reliable means of making that property visible to tax authorities. (Author's comment: less of a problem these days, of course.)"

The classic contemporary objection to the practice is surely Edwin R.A. Seligman's 1890 broadside against a general property tax, which concludes: "[The general property tax] puts a premium on dishonesty and debauches the public conscience.… It is the cause of such crying injustice that its abolition must become the battle cry of every statesman and reformer."

The views of people like Seligman ultimately prevailed, and were helped along in 1913, when progressives won the 16th amendment to the U.S. Constitution, which gave Congress "power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration." As American governance became more professional and formal in the beginning of the 20th century, the tool of the general property tax was supplanted by the graduated income tax. Income taxes were easier to administer and to this day they remain the strongest progressive element of the U.S. tax system.

As the federal government increasingly turned to a broad-based graduated income tax for revenue, states' reliance on property taxes also began to trail off. Although state property tax receipts continued to grow in nominal terms well into the 20th century, they did not drive states' dramatic expansion in revenue. Instead, states turned toward new taxes on personal income and general sales, and toward taxing the rapidly growing auto industry.

And so, by 1965 Duke economics professor (and later chancellor) John O. Blackburn called the taxation of intangible property of "negligible importance." However, even then 14 states still had broad taxation of intangible property: Florida, Georgia, Indiana, Kansas, Kentucky, Michigan, Missouri, Nebraska, North Carolina, Ohio, Oklahoma, Pennsylvania, Rhode Island, and Virginia. Each of those would be repealed not long thereafter.

Ultimately, the demise of the general property tax was partly the result of an understandable - but ultimately misguided - belief that new forms of personal income taxation coming onto the scene made wealth taxation unnecessary or duplicative. However, as we know now, the income tax - while in many cases a powerful tool for progressive taxation - is often not particularly adept at reaching the fortunes of the very wealthy.

While reasonable people can debate the most effective means of taxing wealth, there is a strong case to be made for bringing back heavier levies on the fortunes of the wealthy. Wealth inequality has increased considerably since the middle of the 20th century when the general property tax was being hollowed out. Progress toward addressing racial wealth inequality, measured as the difference between White and Black per capita wealth, began to stall out around the same time.

Our current system of selective wealth taxation through the property tax is largely neglecting - and in some ways even worsening - these problems. Data from the Federal Reserve indicate that the bottom 90 percent of families have more than half of their net worth tied up in real estate, whereas the top 1 percent have just 13 percent of their wealth in real estate. A similar pattern is present across race and ethnic groups: White families hold just 27 percent of their wealth in real estate while Black and Hispanic families hold 40 percent and 58 percent, respectively. At the same time, real estate has also been declining as a share of total net worth, meaning that the narrow property taxes we have on the books today apply to a shrinking share of overall wealth.

In other words, wealthy families - particularly wealthy White families - have a far lower share of their net worth subject to property taxation than other groups. They also have a lower share of their wealth being taxed today than they did just a few decades ago, as intangible assets have grown in prominence. Given our nation's high level of inequality, and the unequal opportunities it affords based on race and class, a return to a broader system of wealth taxation is worth a closer look.

Recent advances in tax administration also make a return to broader wealth taxation more feasible. Measuring and cataloging property values in the pre-digital age was no small undertaking. But modern accounting and financial practices are more comprehensive, efficient, and traceable than in the early 20th century. The right-leaning Tax Foundation, for instance, has explained that in our modern era, "taxing wealth consisting of unrealized gains from publicly traded assets is relatively straightforward." Valuing assets without a clear and visible public value is more challenging, of course, but reasonable valuations can be arrived at by looking at the income streams those assets produce.

The arguments used by opponents of the general property tax are no longer as convincing as they once were and the limitations of taxing only income, but not wealth, in our highly unequal nation have begun to come into sharper view. With these concerns in mind, it's time to revisit whether past tax reformers were wrong to narrow the general property tax, and how best to restore the U.S. tradition of broader wealth taxation. The case for taxing wealth today is more compelling than ever.

IPTI comment: whilst we remain strictly neutral and do not advocate for or against a wider wealth tax, we are keen to share ideas about property/wealth taxation and hope you found the foregoing item of interest. The full the article is available via the link below:

https://itep.org/america-used-to-have-a-wealth-tax-the-forgotten-history-of-the-general-property-tax/

Moving on to IPTI activities, our most recent major event was the annual Caribbean conference that we held jointly with the RICS in early November. The conference was held in Barbados and we had a great range of topics and speakers. The well-attended event was enhanced by a very lively introduction from a Government Finance Minister and our audience was very engaged throughout. Following the conference, I was invited to attend a meeting of the Land Valuation and Assessment Team at the offices of the Barbados Revenue Authority.

We recently presented another in the series of webinars we deliver jointly with the Institute of Municipal Assessors (IMA). This was on the important topic of "Market Data Collection and Analysis". Our two expert speakers reminded the audience of the importance of effective and efficient data collection processes, the importance of having accurate and reflective market data, and the impact inaccurate data can have on the analytical process and valuations.

IPTI's next significant in-person event is our "Property Tax Conference - Policy and Practice" which will be held in The Hague on 6-7 December. The cooperating agency for this event is the Netherlands Council for Real Estate Assessment (NCREA) and the conference is being sponsored by the Property Valuation Services Corporation (PVSC) from Nova Scotia. The conference is also being supported by the Netherlands Ministry of Finance. We have an unrivaled line up of speakers from around the world and I know this will be a great event.

As usual, details of all our forthcoming events can be found on our website: www.ipti.org

Now it's time for a quick look at what is making headlines concerning property taxes in selected jurisdictions and countries around the world. For more information, and links to the original news articles, please refer to IPTI Xtracts which can be found on our website: https://www.ipti.org/ipti-xtracts

It is reported that Iceland will impose a property tax on all house owners to fund the construction of lava barriers that aim to prevent damage from volcanic eruptions. Icelandic officials are preparing for a more volcanic eruptions following a "seismic swarm" that has seen the Reykjanes Peninsula hit by about 1,400 earthquakes in 24 hours. As part of the nation's efforts to protect its infrastructure from geothermal activity, Iceland has passed a new law that establishes a tax of 0.08 per cent of a property's fire insurance valuation on all homes for a reported duration of three years. The bill is expected to raise almost 1bn ISK (£5.7m) in revenue, which will fund the construction of lava barriers and other protections - including dikes, embankments and canals - around Svartsengi, a geothermal power station 65km from the capital Reykjavík. The power station is the main supplier of water and electricity to the Reykjanes Peninsula - the same region that recently suffered the earthquakes. The area surrounding Svartsengi is known for its high geothermal activity. Recently, Grindavík, a fishing town with 3,000 residents close to the power station, was evacuated after its roads, homes and power and water infrastructure were damaged as a result of the earthquakes. The new tax is expected to help protect the region's infrastructure against such occurrences. However, the Prime Minister warned that preventing damage from a volcanic eruption might not always be possible, even with the proposed protective measures. The tax closely resembles the flood fee that was imposed on property owners in Iceland to pay for the construction of flood defences in 2009, which is still in place. The flood tax raised about 22.5bn ISK (£128.2m) over 10 years.

A recent news item says the New Zealand government should take a look at Australia and consider adopting Victoria's vacant land tax. It states: The tax is simple - all vacant residential land, anywhere in the State, attracts an annual tax of 1% of its value. But note that "vacant" is defined as land that has not been occupied or tenanted for at least six months in the relevant year. There are two important exemptions - first it does not apply to holiday homes provided the owner lives in the property for at least a month a year and has a permanent home elsewhere, and second, properties under development have a two-year window where the tax does not apply. It continues: The tax was first imposed in Melbourne city areas in 2018, and will apply to all regions as from 2025. In principle, there is much to like about a vacant land tax: it discourages long term land banking and encourages the early development of residential land - this should take some pressure off house prices and, in New Zealand, put an end to what has been a tax-free ride for land bankers; by encouraging renting, it should ease pressures in the rental market - this would have a deflationary impact on rents and help the RBNZ to reduce interest rates; it has no adverse effects on the productive side of the economy as it does not apply to industrial or rural land - on the contrary, it should nudge capital into the productive side; it is highly progressive as only the very well off will hold vacant residential land as an asset, or more than one holiday home; it does not require a new data base of values - all that data is already there in Councils' rating data bases; unlike a capital gains tax (or at least a soft CGT that only catches assets acquired after the date the tax is introduced) it produces revenue immediately, not revenue in 5-10 years hence; it can easily be flexed and adjusted both in terms of the annual rate, and the time of its introduction - it can also be capped, either permanently or for an introductory period. The author concludes: I hope our new government takes a close look at the Victorian experience.

And finally, there was consternation when it was found that, as France switches to a new tax regime for property taxes, several children have mistakenly been sent tax bills for second homes! Officials deal with up to 440,000 *taxe d'habitation* bill disputes every year - most of which concern taxpayers who have recently moved house without updating details on their tax declarations. This year there is an added complication as it is the first year of the new *taxe d'habitation* regime, under which only second-home owners pay the tax. Examples quoted in French newspapers include an 11-year-old child from Le Havre who was sent a *taxe d'habitation* bill for €1,197 on a second home and a 13-year-old in the Lyon region who was sent a bill for €2,467. An official for the *Direction Générale des Finances Publiques* said that the children's names had been picked up by the tax authorities' IT systems by mistake. He said, "We deal with 39 million tax households, 24 million property owners, and 4 four million *taxe d'habition* notices for second homes each year, and this type of error can occur". Sacré bleu!

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