Leaning on the Land.

More and more communities are considering reviving an old tax idea that's been tried in only a few places.

The Market-Frankford rail line curves past an empty lot in Millbourne, Pa., a piece of land that marks both the rise and fall of the small borough just west of Philadelphia.

A Sears store once stood on the lot. Taxes collected from the store's real estate enriched the treasury of the borough for more than 60 years. The store's tax payments were the single largest source of revenue for Millbourne, enough for its 1,200 residents to have their own full-time police force. But in 1989, Sears decamped from Millbourne, moving one town over to the much larger and more affluent Upper Darby.

Like most municipalities, Millbourne relied heavily on property taxes. The city taxed land and the buildings on top of the land at the same rate, which is typical for cities across the country. And the Sears store was the largest structure in town on the largest parcel—17 acres. "For many years," says Millbourne Mayor Tom Kramer, "that area of land was the meat and potatoes of the borough." But when Sears closed and the building was demolished, Millbourne's property tax revenue all but evaporated.

Millbourne fell into financial ruin. Five years after the store closed, the borough was designated as financially distressed by the state. That made it eligible for additional financial support and debt restructuring, but it was no help to the community's reputation or self-image. The mark would remain on Millbourne's back for 21 years.

The town was unable to lure in new development with tax breaks, so to avoid financial ruin, it leaned on its homeowners to fill the gap in municipal finances. Tax bills skyrocketed between 1993 and 2014. But city leaders ultimately realized the long-term vitality of Millbourne could not be financed by single-family homeowners. High taxes would eventually chase residents away. At the very least, continued increases to property taxes could spark a tax revolt like those that challenged high property rates in California in the 1970s and, closer to home, costly reassessments in Pittsburgh in 2001.

Where Sears once stood, weeds and wildlife have taken over. And from the train platform, the empty lot remains an eyesore in Millbourne. But the gash in the borough's finances has been mended. The town turned to an old yet radical idea to raise revenue. It enacted a land value tax, levying high rates on the land itself and none at all on the structures built there. The tax burden was shifted. Homeowners saw their tax bills cut nearly by a third. Meanwhile, the Sears property, which still swallows up more than a third of the land in the city, saw its tax bill double.

The land value tax, a 19th-century idea, not only raised necessary funds to keep the city afloat financially, but, as intended, forced landowners to make more productive use of other large properties. A former car dealership and a bowling alley, the second and third largest parcels in Millbourne, are now under development. "It's sort of a stick-and-carrot approach," Kramer says.

It’s not an approach that many cities are using at the moment. But it’s an idea that quite a few local governments, most but not all of them in Pennsylvania, are starting to think about.

Property taxes have been levied since the Middle Ages, but generally not in the most efficient manner. Medieval European kings sent tax collectors out to count the number of hearths in private homes, assuming the tally was the best approximation of how many people lived in the house. In 17th-century England, tax collectors counted windows. The idea was that the more windows a property had, the more valuable the property. This clumsy assessment was easily evaded. Property owners simply bricked their windows up. The legacy of this practice can still be seen in London and other industrial centers in England. It had detrimental health implications when the Industrial Revolution drew thousands from the country into the city, where they were often forced to live in windowless buildings with poor circulation.

Meanwhile in the United States, land acquisition was making even some of the Founding Fathers extremely wealthy. George Washington amassed a huge fortune through land speculation across colonies and frontiers. “Tax policy has always encouraged land speculators,” says Ed Dodson, a former market analyst with Fannie Mae and professor at Temple University. “It makes it easy for speculators to acquire and hold land and wait for public-private partnerships to come along with funds to pay them their profit for speculating.”

In 1879, the journalist and political economist Henry George wrote Progress and Poverty, a book challenging the notion that land speculation should reap such large profits. George suggested levying high taxes on land itself, and freeing improvements on the land from taxation. The land taxes would be high enough that an owner would either convert the land into a profit-making enterprise or sell it to someone who would. “The economic value of bare land does not derive from the actions of the owner,” says Joan Youngman, a senior fellow at the Lincoln Institute of Land Policy. “A piece of bare land has value because of the growth of society and the activities around it.” Large landowners, she says, are actually engaging in a form of rent-seeking, buying and sitting on a piece of land at virtually no cost to themselves and waiting for the opportune time to sell after making little or no investment.

George wanted to break that cycle, and his theory was put to the test in the early 20th century in Pennsylvania, when it was used in an effort to break up large undeveloped tracts of land owned by the state’s steel barons, notably Andrew Carnegie and Henry Clay Frick. The state adopted legislation allowing its cities to adopt a land value tax. A handful of them did. Most of them weren’t the pure Henry George variety, under which developed structures escaped any taxation at all. They tended to be two-tiered systems, with buildings taxed but at a much lower rate than land.

Pittsburgh was one of the early adopters. The result was the development of affordable homes for many of the workers in Carnegie’s steel mills. Land value taxes grew in popularity in Pennsylvania well into the mid-1900s. But there was a serious problem. Municipalities seldom bothered to reassess the value of the land. Pittsburgh had to scrap the tax in 2001 after a backlash against land value reassessments sparked outrage from homeowners. “Pittsburgh went too long without revaluing,” Youngman says. “If you fail to revalue, you’ll have a revolt because you get sticker shock.”

And even though the city had a land value tax system from 1913 to 2001, Pittsburgh still saw the gradual decline of its industrial base in the second half of the 20th century. Steel mills slowed their output after their postwar boom. The accompanying decline in tax revenue wasn’t so much a failure of the land tax system as a failure of local industries to keep pace with foreign competitors as steel-making advanced. Some critics felt the land tax was unjustly blamed for the economic collapse.

The land value tax didn't fail Pittsburgh as much as the political system did. For decades, city leaders balked at tax assessments, which had been lagging behind the real value of land since the 1940s. Rather than adjust the land assessments to match property values, the city instituted a property tax in 1954 to fill gaps in the budget. As residents continued to leave the city, its tax base continued to dwindle. Yet Pittsburgh's leaders could not muster the political will to reassess land values. By the mid-1990s, though, the city was forced to reassess property values to help pay for services. When the assessments for 2000-2001 came back, land value taxes jumped 81 percent and taxes on buildings by 43 percent. The new valuations were in line with the actual appreciation of the land. But affluent Pittsburgh residents angered by the steep increases rejected them and filed thousands of tax appeals. The city scrapped its land value tax. "The 2001 abandonment of the split-rate in Pittsburgh," University of Pennsylvania professor Mark A. Hughes wrote in 2005, "is a compelling example of the limited role that evidence often plays in policy decisions."

But Pittsburgh didn't abandon the tax idea completely. Since 1997, the city has used a pure land value tax to assess property within the confines of its central business district. After the Great Recession, downtown construction picked up. In the last 10 years, $8.5 billion in development has either been constructed or planned, according to a report by the Pittsburgh Downtown Partnership.

Meanwhile, California was confronting some of the same problems, but with a different outcome. As the state boomed after World War II, its population tripled. With that rapid growth came a housing crunch that led to rapidly increasing residential property taxes. A tax revolt broke out in the 1970s, and in 1978, voters approved Proposition 13, a ballot measure that rewrote the property tax system in the state. Property taxes were assessed at no more than 1 percent of residential or commercial building value and could only increase 2 percent per year.

Had the property tax reductions been accompanied by a significant land tax, George's theories might have been given a meaningful test. But land taxes were also kept low, which didn't promote the best use of property. With property taxes strictly limited, municipalities scrambled to attract car dealers, shopping malls and even parking lots to produce sales tax receipts. Improvements to the land were minimal, and the land itself brought in very little. One of the biggest losers was the state treasury.

But the biggest victim of all was the state's school system. Prop. 13 constricted the main source for school revenue. The largest state in the nation, with by far the largest economy, fell to 41st in per pupil spending. Recently, some school districts in the state have turned to a revenue scheme almost akin to George's land value tax. They are placing a flat tax on each parcel of land within a school district boundary, regardless of the improvements made on the land. The city of Oakland began imposing a vacant land tax earlier this year. It taxes owners of vacant lots $6,000 per year, and vacant condominiums $3,000 per year. The money will be used to address affordable housing and homelessness.

While California was struggling with its property tax system, some Pennsylvania cities still depended on a land tax. Harrisburg, the state capital, was using the land tax as a way of revitalizing its economy. In 1975, as industrial decline and white flight gripped Pennsylvania's rust belt, Harrisburg adopted its two-tiered land value tax. It took some time, but city leaders insisted that taxing vacant land rather than development would revitalize the downtown. There's some evidence they were right. Between the early 1980s and the early 2000s, the number of vacant buildings declined from more than 4,000 to about 500, and the number of businesses increased more than fourfold. Other Pennsylvania cities have followed Harrisburg's lead.

Aliquippa is one of them. A small working-class town west of Pittsburgh along the Ohio River, it was once home to Jones and Laughlin Steel. The J&L plant supported the town and its residents until it shuttered in the 1980s, leaving many of the workers without jobs and the town short on resources.

Overnight, the city lost 30 percent of its tax revenue. “The amount of vacant land from the demolition of steel plants,” says Joshua Vincent, president of the Center for the Study of Economics, “put extra pressure on out-of-work steel workers and businesses on Main Street.” In 1988, Aliquippa adopted a land value tax. From that point on, land was taxed at more than seven times the rate of buildings. The impact was immediate. Tax revenue from land alone jumped from less than one-fifth of city tax revenues to more than 80 percent. It was so successful that the school district followed suit in 1993.

Tom Kramer became mayor of Millbourne in 2009, as the town was slowly emerging from economic distress. He had seen the community’s decline first-hand, arriving just as the Sears facility had closed. It was a chance meeting with Dodson, the Temple University professor, that convinced him that a land value tax would be the right fit for Millbourne. Kramer was open to any ideas that would generate the revenue necessary to save the town fiscally, without placing any more burden on single-family homeowners. “The most important thing we needed to do,” Kramer says, “was cut the residents’ taxes.”

Kramer faced strong headwinds from real estate interests. Even when the local political climate supports a land value tax, adoption is difficult. In Pennsylvania, as in most states, state law severely limits the ability of a municipality to make major changes to how it collects taxes. But Pennsylvania may be a straw in the wind.

Cities in most of the country have been forced for decades to compete with each other in offering lucrative tax breaks to lure in developers and businesses. Those schemes leave local governments short on cash to build and maintain infrastructure and services needed for commerce. “Giving these picayune tax breaks makes no sense,” Vincent says. In the end, he believes, cities are repeating the mistakes of decades past. “The thing that cities want is someone to build the homes and offices,” he says. “And the city is taxing the good part, the building itself.” What it needs to tax, in his view, as in George’s view more than a century ago, is the fundamental value of the land.

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