LOCAL REVENUE FOR HARD TIMES

by Philip Finkelstein

Fashion is a luxury enterprise. Following the mode is something for folks who can afford the latest, to wear, to eat, or in government. When the coffers were full, fashions moved quickly from Washington to State Capitols to City Halls and back. We all needed the latest, whether it was PPBS, OMB, Cabinet-style government, citizen participation. Some dictates, like zero-based budgeting, sold as poorly as the Nehru jacket, while others, like tight jeans, are tried on by almost everyone whether they fit or not.

In this latter category, peddled among others by the otherwise sensible Advisory Commission on Intergovernmental Relations (ACIR), the dictum is that all governments should be broadly based on a variety of revenue sources. With an appeal as rational seeming as that of a balanced diet, the fashion of trying any revenue measure at any level of government found wide favor when the going was good. Income tax became the rule at the state level and at the local level was no longer so exceptional. Payrolls, transactions, special and general excises on any and all property and goods could be levied anytime, anywhere. No jurisdiction could be taken seriously if it had to rely on that old standby, the real property tax, unrelieved by a progressive accessory. As long as the going was good, the notion of a balanced revenue source received little scrutiny, let alone criticism. Some urbanists even suggested that local tax and debt limits be extended beyond the property tax base and some, as we know in New York City, just went ahead and did it, in effect, living without limits on debt or taxes simply because no one, in the public or private finance sectors, had said that it could not be done.

Now that the city is in substantial fiscal-if not physical-repair, we may do well to recall how it all fell apart. The Urban Development Corporation took on projects with only a moral authority but no fiscal base for debt, with the state's then imperial leadership in acquiescence. The city sold short-term debt in anticipation of taxes it could not collect and revenue it could not safely count on. There was reliance on a greater, broader, more varied base than any state or local government, however big and powerful could justify.

But there are certain kinds of revenues that are not and should not be available to certain levels of government and can be used only at the greatest risk. Sources with a great deal of mobility are obviously inappropriate for a locality. Similarly, resources whose incidence is highly local may be inappropriate for a higher level whose claim to their use is at least debatable. One example of the latter is the bitter dispute between Canada and its Western provinces over their mineral and energy wealth. An object lesson in the former is the way New York City and State, together with Massachusetts, have contrived by their high taxes on personal income to create that convenient haven between them known as Connecticut where successive progressive administrations have been clever enough to resist that fashion in tax policy.

Now that localities are faced with harder times, at least with the prospect of fewer funds from Washington and their states, it may be useful to examine some of the options they can exercise by themselves. The first principle, indeed the underlying theme which should not have to be but sadly bears repeating, is that no tax should be imposed on anything that can readily and legitimately escape jurisdiction. In its extremis, New York City got legislative authority for an estate tax, with the fully predictable consequence that anyone wealthy enough to choose a final residence did so-elsewhere-and the silly tax was promptly appealed.

Adequacy and growth potential are major standards for revenue sources. Is the source too small or too volatile, or is it stable enough to be counted on and provide more when necessary? It is instructive that throughout its travail and now into its recovery, New York City has been able to rely basically on its property tax for an increasing percentage of locally derived revenue. Indeed, the more recent growth in that base, with the Manhattan building boom, has, more than any other factor, contributed to the present surplus in the city's budget. Now the city is questioning whether it needs to offer more building incentives, like J-51, because the property tax has become too good to give away. While retail sales and stock transfers, along with personal income, have also demonstrated growth, particularly with inflation, the property tax has been subject to fewer fluctuations and a more dependable growth rate. It is by far the biggest money maker the city has, belying predictions not much more than a decade ago of its ultimate demise.

Following availability, adequacy and growth, there is the question of appropriateness of revenue sources for the purposes of expenditures. Now we know that budgeteers are not terribly concerned with relating where it's coming from to where it's going. As long as it's there, and more or less in balance, it need not matter if the revenue side and the expenditure side are unrelated. But in fact, and in good economic, social and political theory, there is every reason to relate a revenue source to expenditure need. The best argument for transferring all income redistribution to the federal level is that the resources of the income tax are absolutely essential for such purpose. Indeed, the very imposition of that tax, properly administered, furthers the redistributive effect. For much the same reasons, local expenditures should be derived from a local revenue base. The services of local government—police, fire protection, schools—all have the effect, one way or another, of enhancing the value and the desirability of the community. It is fair that the resource most benefited by those services be tapped to pay the most for them. We need not resort to special assessment districts, except where the service is itself special and the beneficiaries limited, like water and sewer districts, like historically successful California irrigation districts. Perhaps we can add to that a transportation district, or better still, simply assess the value of land as it is enhanced by local and regional services, including mass transit and other amenities of access and utility. Appropriate taxation should therefore mean a tax whose imposition actually furthers the goals for which its use is projected. A tax on location values helps support, protect and enhance those very values. To the extent that local property taxes rely on location values, that is good land assessments, the property tax is probably the best local revenue source. To the extent that localities fail to assess land but instead look to new buildings or transactions as a way of increasing their base of ratables, the property tax is a poor means because it punishes the very values it seeks to build, such as good housing, good communities, well-maintained improvements and new development.

Fashions tend to be cyclical. For governments at all levels, we are being told in Washington that less is going to have to be more and that small may be, if not exactly beautiful, at least desirable. As one who has never bought the decentralist dogma, I am nevertheless persuaded that some of its principles are worth trying. The notion of appropriate technology or even appropriate size, the right tool for the job, has a direct parallel here. There is a right revenue source for local government and it is the only one that cannot escape its jurisdiction, the one with the best chance of stability and growth as a base, and the only one appropriate for the services its proceeds would provide. The tax on land values is therefore the appropriate tax and may even come back into fashion after all these years of neglect.