

HOUSING THE HOMELESS

For the past year or so considerable attention has focused on the plight of America's urban homeless. Last May, the "Hands Across America" fundraiser to combat hunger and homelessness attracted the participation of some 5 million Americans. More recently, television, newspapers and magazines have portrayed in graphic terms the cruel existence led by many homeless people in America's cities. Probably anyone who has followed television news programs this season has seen portraits of the bedraggled seeking refuge in overcrowded shelters, subways, alleyways, abandoned buildings, or huddled over sidewalk grates that promise some protection against the cold.

A precise census of the Nation's homeless (with respect to social characteristics as well as numbers) would be impossible to take. Estimates of people "on the street" today range anywhere from 250,000 to more than 2 million nationwide. In New York City alone, it is reported that 50,000 currently are without permanent housing. Whatever their numbers, no one can question that life without housing often is desperate and dangerous.

Many of today's homeless no doubt are people who chronically have been unable to provide for themselves. Tens of thousands are formerly institutionalized persons who have been returned to society and probably would have difficulty finding housing in the best of circumstances. Thousands of others are "homeless" for personal reasons — family disagreements, legal problems, temporary job dislocations, and the like. But many others apparently are working people who nevertheless simply do not have the resources to pay for expensive housing in urban centers.

Statistics of the "homeless" *per se* actually fail to describe the extent of the urban "housing problem." Those data ignore the millions who now live in slum tenements. They also ignore the millions of America's "other homeless": namely, the working men and women who want to purchase homes but cannot afford to at current housing prices (which in many parts of the country continue to increase much faster than the general price level). The fundamental problem for these families is that they have been priced out of the housing market.

Plainly, the majority of those without adequate housing have not been helped by the billions of dollars spent over the past generation on government housing programs of one kind or another. Plans to warehouse "the poor" in dismal high rise projects backfired: those "projects" now are among the worst of urban slums. Even so, in some cities thousands are said to have their names on waiting lists for public housing that is spoken for 20 years in advance. By 1990, it is estimated that there could be a shortage of upwards of 2 million housing units that are affordable to low-income families.

Despite the obvious failures of publicly funded "low-cost" housing programs, the response of most politicians and public and private social workers to the scarcity of affordable housing for lower- and middle-income families has been to call for more public housing, more Federal aid for shelters, and extension of welfare benefits such as food stamps and Medicaid to persons "without an address."

As in the past, such spending would fail to solve the problem. The conditions of homelessness described by the media today prevail in spite of the expenditure during the past 4 decades of tens of billions of taxpayers' funds through Federal urban renewal programs, revenue sharing programs, housing programs, and the like. As we discuss below, the availability of housing actually has decreased where government intervention has been greatest. To the extent that the problems of the homeless reflect a misallocation of resources, "throwing more dollars at the problem" is unlikely to prove effective. As with so many policy questions, a more useful approach would be to reduce the ways in which government fosters the misuse of resources in the first place.

GOVERNMENT POLICY IS THE PROBLEM

It would require a lengthy volume to relate in detail the chronicle of disappointment that has resulted from numerous Federal, state, and local policies undertaken to "keep housing affordable." However, the most appalling failure — in New York City — provides lessons that ought to be heeded by anyone genuinely interested in solving the housing

problem. In New York City, where some of the most stringent controls over the use of residential property in the United States apply, government policies *have* had several effects. But none of them is consistent with the intent to provide greater access to housing for New York City residents.

Rather, the chief results of New York's planned housing market have been: 1) the deterioration and abandonment of tens of thousands of residential units, many of them in formerly elegant structures, and an accompanying enormous increase in market rents; 2) the perpetuation of housing privileges among middle and upper-middle class leaseholders of rent-controlled properties (so precious are these privileges that, in the words of one observer, the "rights to a rent-controlled apartment can start a blood feud"); 3) the *de facto* sentencing of lower-income families without privileged leaseholds to slum housing or "homelessness"; 4) the growth of a socialist municipal bureaucracy with dictatorial powers over property and property owners (the city government is now New York City's largest landlord – and largest "slumlord" by far); 5) a vigorous and corrupt residential rental blackmarket actively supported by New York City's Housing Court; 6) increasing bankruptcy among small landlords; and 7) ironically most distressing, the growth of an apparent disdain among New Yorkers for all landlords and for private property in general.

The surreal response of New York's housing authorities to the proliferation of "bombed out" neighborhoods where proud buildings once stood – to paste vinyl decals depicting homey scenes (with curtains, flower boxes, and human silhouettes) over the boarded windows of gutted buildings – only begins to suggest the extent of the housing fraud that has been perpetrated on the New York public by local authorities.

The history of New York City's housing debacle has been documented in two recent studies that depart from the usual reportage of "homelessness."* By directing their inquiries to the different interests of the players in New York's residential housing game, they describe in detail the ways that controls over residential rents have distorted usual market processes and given rise to new, often extra-legal or illegal, markets that are less efficient and far less equitable than are open housing markets.

In this distorted market structure, contracts often are written not between "landlords" and "tenants," but between any variety of parties who may

possess an interest in a property. Leaseholders set the going rate for sublets on rent-controlled apartments via off-the-record "key payments" (bribes). "Tenants' rights" associations, empowered by the courts to administer a building, are given license to command rents and provide no services (the owner remains responsible for essential services even though he or she receives no rent during the administration) – all the while collecting an "administration fee" from the city. Even squatters with no legal rights whatsoever to ownership or tenancy are encouraged by the (misnamed) Department of Housing Preservation and Development (HPD) to exercise proprietary rights over other squatter tenants. HPD actually advertises this last form of "tenant ownership" over private ownership as the solution to New York's housing problem.

In short, where residential property in New York City is concerned, in thousands of cases anarchy prevails – aided and abetted by avowedly socialist city planners who are hastening the retrogression toward pre-contractual, tribal-like property arrangements. The only property rights that exist for those forced to deal with the HPD are "rights" bestowed at the whim of the bureaucrats.

Of course, New York City's housing situation is an extreme example of how government has fostered the misuse of resources, and, if reports of popular attitudes toward landlords and private property rights there are anywhere near accurate, there would seem to be little hope that things soon will change for the better. At this juncture, given the state of public opinion and the entrenched interests of housing bureaucrats and the privileged elite, it is hard to see what is to prevent New York's housing crisis from getting even worse and the problem of "homelessness" even more desperate.

One would hope, on the other hand, that New York's experience with property restrictions might serve as a warning to other communities where momentum may be building for similar government intervention in local markets. It is gratifying that the worst abuses of New York's rent-control regime finally are receiving some exposure. Yet the recent investigations have shed light on only the most blatantly regressive effects of a particular housing policy, rent control. Many other facets of government policy, notably environmental policy and property tax structure, influence the use of resources that could be applied to providing improved housing for "rich" and "poor" alike in many American communities. Moreover, while such investigative studies may illuminate the negative effects of present policy, they do little to point the way toward genuine long-term reform.

In this last respect, we think renewed attention ought to be given to a plan for better utilizing real-property resources that has been suggested for more than 100 years: reform property taxes in order to convert them into an effective means of promoting accelerated economic growth – especially in new construction – and of eliminating any

* See William Tucker, "Moscow on the Hudson," *The American Spectator*, July 1986, pp. 19-21, and "Homeless People, Peopleless Homes," *Ibid.*, February 1987, pp. 18-21. These two reports are excerpted from a larger study that Mr. Tucker, who recently spoke to an AIER audience about his research, is completing on New York's rent-control regime. See also Peter Weber, "Scenes From the Squatting Life," *National Review*, February 27, 1987, pp. 28-32, which describes New York's urban "homesteaders'" unconventional attempts to fashion living space out of the rent-control rubble.

special privilege associated with real estate ownership *per se*. For many years we have advised that, accompanied by the elimination of outright restrictions such as rent control, such a tax reform might not only remove barriers to housing the urban destitute (as well as the millions now living in slum tenements), but it could also make homeownership more available to the millions of working men and women who currently are priced out of the market for new homes.

AN "OLD" IDEA FOR TODAY

In brief, a helpful property tax reform would follow the proposal outlined by the economist and social philosopher Henry George in his seminal work *Progress and Poverty* (first published in 1879). As present-day followers of Georgist principles argue, under the provisions of current real estate tax regulations, maintenance and improvements to old structures (such as found throughout the slums of New York City) and construction of new buildings are discouraged by high taxes on such activities. That is, by improving their structures or adding new structures, owners simply invite a higher assessment and tax on their property.

Similarly, low taxation of land in relation to taxation of improvements fosters underutilization of land and a reluctance to construct and maintain improvements. That the supply of land is limited ensures that as population and economic activity increase, demand for land and thus prices will increase.* Low relative taxes on site values enable owners to leave sites idle or in uneconomic use. The smaller the land tax, which in the absence of coercive regulations is the only direct cost to owners, the less incentive they have to use land productively or to sell it to someone who will. Yet, as general population increases and economic growth result in a higher price for land, the private owner reaps the return on publicly created value.

Thus, a *de facto* subsidy is provided by payers of the larger tax on improvements to land. And the higher these taxes are, the more property owners are penalized for putting land to better use. Where taxes on improvements are much higher than taxes on land, owners are encouraged to forego maintenance and "pocket" both the receipts that would be spent for upkeep and the tax savings attending lower assessments as structures deteriorate.

What can be done to reform this deleterious tax structure? Current advocates of a Georgist property tax reform argue that state and local governments should legislate changes in order to tax site values at higher rates than improvements. They say

* In this discussion, "prices" refers to real prices, not depreciating paper-currency prices. "Site" and "land" are used interchangeably and designate the value of unimproved sites or raw land. Improvements to the site — even those so basic as drainage ditches, filling, recontouring, and the like — require an "investment" of labor or capital and for ease of discussion are included in "construction" herein.

that land-value taxation not only would encourage development of unimproved land and better maintenance of existing improvements, but also would eliminate the special privilege associated with rising values of land. (This observation applies equally to the privileges conveyed to the holders of *leases* on New York City rent-controlled property, since the inflated rental values of such properties accruing from the underutilization of slum properties are passed through to leaseholders as below-market rents that are negotiable to sublets.)

As Henry George argued in *Progress and Poverty*, those taxes necessary to finance warranted expenditures for common purposes ought *not* to be levied against either earned income or productive capital improvements that contribute to the creation of wealth or are themselves articles of production. Income taxes rob producers of the deserved rewards for their efforts. And taxes on either commodities or capital improvements discourage the creation of wealth. Land taxation, on the other hand, expropriates none of the rewards of labor but instead exacts a "benefits fee" of land rent that derives in large part from publicly financed projects such as roads, sewers, water lines, lights, and such that have increased the economic value of the land. In this respect, it is not a tax at all but a public charge for services rendered.

VISIONARY DREAM OR PRACTICAL ALTERNATIVE?

Is this idea simply a visionary dream? Even though its critics generally agree that land-value taxation would not retard production and distribution of privately created wealth, many are simply not persuaded that such a system of taxation is either feasible or equitable. They claim that there is no conclusive evidence that land-value taxation would accomplish what its proponents assert. They protest that there is no way in practice to distinguish site (location) value from improvement value of land. They say the present landowners have invested so much in already high-priced land that to expropriate land rents now would be grossly unjust. They suggest that a land tax would further increase land prices. And they argue that such a tax would force retired persons (and others on fixed incomes) in prime locations from their homes. In sum, critics claim that land-value taxation may be fine in theory, but it would not work in the United States today.†

In our view, these reservations and objections have plausibility. Proponents of site-value taxation have not yet presented a clearly persuasive case. More work needs to be done, and such property-tax changes as Proposition 13 in California and Proposition 2½ in Massachusetts offer fertile areas

† For a more extensive discussion of the criticisms of Georgist proposals and procedures for testing the effects of land-value taxation, see "Testing Pro-Growth Property Taxes," *Economic Education Bulletin*, February 1985.

for study. (Preliminary data for Massachusetts strongly suggest that developments there are following Georgist expectations: the property tax cap has forced many localities to increase significantly valuations on land relative to improvements, and residential construction recently has assumed "boom" proportions.) But objections always will be possible, and site-value taxation should not be judged against some imagined higher standard of efficient implementation than alternative forms of taxation.

On balance, it is hard to see how greater taxation of site values would pose problems that are much different from those already confronting real-property tax assessors (or other tax authorities, for that matter). They already must distinguish between value of land and value of improvements in their computation of general property taxes. As for the argument that land prices would rise even further — pricing even more people out — the opposite seems more likely. The market value of each site or unimproved parcel of land reflects two things: the expected gross rent from the site and the tax on the site. An increase in the tax on a site would *not* increase its gross rent or usefulness, but it would *decrease* the net rent of the site by the amount of the additional tax — and so pressure prices downward. (In New York, where rent controls impose a huge *de facto* tax on improvements, it is hard to see how any but the most privileged would see the costs of their housing increase.)

The objection that present landowners who have paid high prices for their land would be unfairly deprived of anticipated rents has some merit. But land-tax proponent C. Lowell Harriss does not see this as an insurmountable obstacle. "Gradual change can accomplish much over the years," he observes, and thus argues for phasing in land taxation over many years. Indeed, even though complete data are lacking, the experiences of a number of cities in Pennsylvania suggest that gradual introduction of the land tax can be accomplished without severe disruptions.

Any threat that land taxation might pose to elderly homeowners likewise can be overcome through some form of deferred assessments. Payment of the full tax on such land could be deferred until the equity in the property was realized in actual sale. Such a system already operates in some states such as California, where under the provisions of the Senior Citizens Property Tax Postponement Law, retired homeowners may delay payment of the local property tax until the sale of the property — either when the owner decides to move or after settlement of the estate following death. In this situation, the owner is not deprived of the land, nor is the community denied its claim to the value of the land.*

HOUSING MARKETS DEPEND ON NEW CONSTRUCTION

The point lost on virtually all advocates of subsidized housing for "the poor" that is captured so simply by the Georgist reform is that greater access to housing for lower-income groups usually depends on new construction designed for middle- and upper-income families. In an unfettered residential market, "affordable housing" for the financially less-well-off is made available as those who already have housing move to new homes. In cities, apartments in older buildings become available when their occupants "move up" to new housing (luxury apartments, condos, and the like). In the suburbs and nonmetropolitan regions, "starter homes" become available to first-time buyers when previous homeowners move to new homes. Plainly, government policies that simultaneously discourage new construction and the maintenance of existing structures deal a double blow to those entering the housing market.

* Readers who wish to receive regular reports on land-value taxation may write to the Center for the Study of Economics, 2000 Century Plaza, Suite 238, Columbia, MD 21044. That organization publishes *Incentive Taxation*, which is devoted entirely to discussion of land tax issues.

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