A Letter To Mr. & Mrs. Taxpayer

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A Letter To Mr. And Mrs. Taxpayer

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Preface

The Department of Agricultural Economics of MAFES and of the College of Agriculture of Mississippi State University has a modest research effort under way in the area of taxation. The focus of this effort is to provide information to help acquaint the citizens and public officials of Mississippi with the current situation, some of the alternatives available, and the likely effect of these alternatives.

The intent of this publication is to introduce a planned series of publications on taxation by sharing with readers the experiences of other states and the opinions of tax authorities abstracted from the literature. Its contents should by no means be construed as recommendations.

The second publication of the series is now being printed as MAFES Bulletin 820. The authors, Agricultural Economist Fred H. Tyner and former Graduate Assistant Jerry W. Grace, explore the effect of property assessment equalization on county revenues, millage rates and homestead exemption.

Two MAFES Bulletins to be published in the near future will present the results of studies of farmland property taxes based on use-value assessment and the economic aspects of alternatives to the property tax as a means of financing public education. Associate Agricultural Economist James H. Simpson and former Graduate Assistant Stanley A. Herren conducted the research on use-value assessment; Agricultural Economist Fred H. Tyner and former Graduate Assistant Fred D. Robertson studied the means of financing public education.

Verner G. Hurt, Head
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You have for some time now been asking some extremely difficult and important questions about the property tax. The problems with which you are concerned are not peculiar to your own county or community; other counties and communities in Mississippi and in all other states have similar problems and an increasing number of concerned citizens throughout the Nation are posing the same or similar questions.

The growing public interest in that I choose to call the “Property Tax Crisis” has generated nominal support for taxation research and as led to tax seminars in a number of states. Unfortunately, the hard core facts essential to solving the problems surrounding the property tax either have not been determined or have not been assembled into a format designed to provide the answers needed. Published seminar proceedings and research results do, however, provide useful guidelines for those seeking ways to improve the property tax.

Three basic questions must be answered in providing and financing public services:

1. Which public services should logically be provided by local, state and Federal governments in sparsely populated areas, in metropolitan areas and in the country in-between?
2. What level of spending is necessary to provide “adequate” facilities and services?
3. How should the cost of public services be allocated among citizens of the community, state and nation?

Our approach to answering these questions has been to call upon all levels of government to meet citizens’ expanding public service demands. Through the political process, we have created a very complex federal system with many units of government and a host of elected and appointed public officials. Responsibility for supplying and financing public services is shared among these governments through a wide variety of programs and techniques. Stresses have developed which threaten the system but which will lead to major changes, especially in methods of financing public services. (9, pp. 2 & 3)*

Real property taxation undergirds but is only part of the whole of local government revenues. The complexity of the tax structure becomes apparent when one takes real property taxation in the cities, towns and 82 counties of the State and combines it with the multiple government revenue-sharing programs financed by excise, sales and income taxes.

Meeting the public interest of quality education and other public services raises a fundamental question: How to adjust the over-all tax structure of the state and local governments to provide more equitable taxation, including real property taxation, in response to social and economic adjustment from a changing technology,

— the car
— the industrial park
— the shopping center, and
— the shifting comparative advantage of land uses, especially against the intensively used inner city area and the extensively used farm and open space lands? (7, p. 10)

Some of the more important issues involved in adjusting the over-all tax structure may be posed as questions:

1. Where should money needed to support the local government work-load come from? The property tax? Other local taxes? If so, what taxes? Local fees and charges? State aid? Federal aid? Other sources?
2. Are there too many or too few local governments to tax and spend efficiently in response to public demand? If so, how should they be changed?
3. Can and do local governments collect taxes as fairly and efficiently as the state or Federal Governments?
4. Can they perform their functions or work-load as productively and responsively to public demand as the state or Federal Government? How could they improve?
5. Should the state or Federal Governments take over and administer more, or less, of the local work-load, such as education, highways, welfare? How would this affect local, state and national taxes?
6. Where should state money come from to support state operations and state aid to local government?
7. How could state governments be improved?
8. Where should Federal money come from to support Federal operations and Federal aid to states?
9. How could the Federal Government be improved? (6, p. 4)

Turn now to the question, what are the requirements of a “good tax”? To some people the only “good tax” is a tax somebody else will pay. I do not believe that this reflects the attitude of most taxpayers. Your statement that farmers expect to pay taxes but do not want to be abused is, in my judgment, a fair assessment of the feeling of taxpayers generally. Resistance to local and state tax increases does, however, arise when

*Numbers in parentheses refer to the sources of quotations used in this letter. This one, for example, refers to pages 2 and 3 of reference number 9 of the Literature Cited at the end of the letter.
taxpayers believe that they bear more than their fair share of the cost of government, that they receive relatively few of the public services provided by their tax dollars, or that their tax burden is grossly unrelated to their ability to pay.  

Suggested sets of criteria for evaluating tax measures have been with us at least since Adam Smith’s famous canons: Equity, certainty, convenience and economy. These canons are still relevant nearly 200 years later, if interpreted carefully. One of the better modern interpretations that I have come across states that a good tax system should:

1. Distribute the cost of government with reasonable fairness among all people who receive benefits from government services and who have taxing ability;
2. Be readily understood by the taxpayer and as convenient for him to pay as possible;
3. Be relatively easy to administer to minimize administrative complications;
4. Be difficult to evade or avoid;
5. Provide adequate revenue for the needs of local, state, and Federal Government;
6. Be flexible enough to meet changing conditions;
7. Be widely shared;
8. Interfere as little as possible with the private production of wealth.

People always have strong opinions about their taxes, opinions that reflect what they see in their community. Over time these opinions become beliefs—judgments considered facts. An increasing number of people hold these beliefs about the real property tax:

- That it is being overworked.
- That it does not meet the equity norms established for public finance. To wit:
  - A tax should be just.
  - It should be levied in accordance with the ability to pay.
  - It should be difficult to evade.
  - It should be uniformly applied within classes.
  - It should be clearly spelled out in laws. (7, p. 4)

The property tax has long been condemned as a “poor” tax. Its weaknesses have been well summarized by Ronald Welch: “—The property tax is the most unpopular of all major taxes now employed in the United States. It is under attack from all sides. It is denounced by welfare economists as our most regressive major tax, by businessmen as the most inflexible tax, by farmers as our most unfair tax, by the aged as our tax least related to ability to pay, by guardians of the law as our most ineptly administered tax, and by conscious or instinctive disciples of Henry George as our most regressive tax. Despite these inherent weaknesses, it will not be abandoned so long as local governments exist. Improvements in its administration, although possible and desirable, cannot make this a ‘good’ tax in terms of accepted principles of public finance. In my opinion, its use should be restricted primarily to property-related services but not so narrowly defined as to exclude activities which maintain or increase property values, e.g., paying off bonds for certain capital improvements.” (9, pp. 6 & 7. I added the emphasis because I heartily concur.)

The central problem in real property taxation is the capacity of the tax to provide adequate revenue to finance minimum needs of a community, whether city, town or county. Equitable and efficient taxation requires that a state-local revenue sharing system reflect some maximum limit on property taxation. A system must be developed that will take into account and reflect changes in social and economic development. Moreover, it must provide an amount of revenue adequate to finance an acceptable level of quality public services in all local governments. Such a system would equitably serve people in our cities and our most rural counties. (7, p. 23)

Professor Donald Epp has said: My suggestions follow:

My suggestions that follow are not addressed to the immediate problem of farmers faced with rapidly increasing property tax burdens. Rather, I am suggesting some ideas that may provide food for thought on how we might attack the general problem that gives rise to the specific problem of high taxes on farmland.

First, I would suggest shifting services that are national in nature to the national administrative level. Because of the great geographic mobility of people on a day, education and welfare are obvious candidates for state national financing and administration. This, of course, does not preclude local administration of offices and advisory bodies. It suggests only that these services are not a strictly local responsibility and should not be financed by strictly local taxes.

Second, where a governmental provided service is obvious, oriented to serve a specific group should be financed by user charge. An example of such a service is the municipal water supply agency. (pp. 85 & 86)

Virtually all tax economist recommend shifting support of local schools to consumption and income taxes. A strong argument can be made for this. Why, for instance, should a rural property owner bear a disproportional share of the cost of educating rural youth, when, for the most part, it is
Legislation granting special property tax exemptions involves states in property tax administration. In my opinion, this is an area in which states should not be involved but one in which they will continue to be involved so long as they must reimburse local governments for revenue lost as a result of exemptions. For example, even though the state government of Mississippi now levies only a four mill tax on all taxable property in the state, the State Tax Commission has the duty to see that the assessments of the various classes of property in the several counties of the state are reasonably equal and uniform throughout the state and that all property is assessed as nearly as possible at its true value.

Professor Harry Case has written: Mississippi’s laws regarding taxation of property, if followed, are certainly adequate to bring about uniform and equal taxation throughout the state. The major questions that should be asked at this point are whether uniformity and equality should be the major criteria and, if so, are our laws being administered in a manner that brings about such uniform and equal taxation. Obviously, a field study will have to be conducted to answer the latter question. (2, p. 5, emphasis added)

The most readily identifiable major tax subsidy in Mississippi is the Homestead Exemption. While, in the eyes of many, criticism of the Homestead Exemption is tantamount to an attack on the sanctity of motherhood, others feel that the Homestead Exemption is archaic and needs to be eliminated. If it is decided that some relief be granted to some groups of taxpayers (the elderly, for example) the relief could take the form of a credit against state income tax liability.

Advantages to be gained from the income tax credit approach include the following: The subsidy can be limited to those who finan-
cially need it. The cost of the subsidy is borne by the state government which granted the subsidy. The state government is able to utilize other tax sources than the property tax more efficiently than local governments. The tax base of financially hard-pressed local governments is maintained intact. Inequities between local governments caused by the unequal impact of property tax exemptions are avoided. Finally, it would enable the legislature to more accurately compare the costs of the subsidy with the benefits that might be derived. A more intelligent social policy decision would be possible. (3, p. 35)

Granting local governing bodies the authority to impose a local sales tax has serious implications for the property tax. The dense settlement pattern associated with cities and towns has been and still is giving way to a less dense settlement pattern, called suburbia. There settle the young, the advantaged, the affluent, the new industry and the shopping center...

Shopping centers seek customers from places other than suburbia, and they succeed. People drive out from the city and in from the rural areas to shop at the "biggest shopping center in the region"...

Both cities and rural areas subsidize suburbia through the sales tax. To offset the tax revenues transferred by citizens carrying on normal business activity, the city or the county or both may find it necessary to impose higher taxes on real property.

Suburbia creates other problems. Local county government is called upon to supply many urban-type public services to their new population, including education for their rapidly increasing school age population.

To meet their obligations, affected counties make huge investments in public facilities and incur large increases in operating expenditures.

Such counties have witnessed rapidly rising land values and enormous additions of structures. Despite this, per capita expenditures for public services have risen to heights where dependence upon the real property tax strains near the breaking point.

As this strain intensifies, so does discussion about equity and real property taxation. An extreme diversity of opinion is expressed, with newly settled suburbanites and long-time resident landowners arriving at different conclusions about the equity issue. Long-time residents do not believe their land should bear the cost of public services that new residents demand and local governments provide. (7, pp. 13, 14, 15, & 16)

The Mississippi Constitution provides that property shall be assessed for taxes in proportion to its true value (2, pp. 1 & 2). True value or cash value is usually interpreted to mean market value—what the property would sell for in a transaction between a willing buyer and a willing seller. Actual selling prices of comparable pieces of property are typically taken as the most reliable gauge of market value.

This presents a serious problem to farm landowners—because, as applied to farm properties in the rural-urban fringe area, this type of assessment results in valuations for tax purposes that are strongly influenced by sales of farm land for non-farm use. Farms that can support a market value of no more than a few hundred dollars an acre in agriculture may be valued at several thousand dollars an acre for taxation—if nearby lands have sold for sub-division or industrial purposes for that amount. (11, pp. 36 & 37)

Under the circumstances outlined the farmer has only two choices: sell his property or seek relief. To sell is not always an easy and profitable solution. Many people consider it unfair for the farmer should be forced out of the early stages of the suburban land boom and not be permitted to capture the full benefit of capital gains on the land he held all his life. At the same time is argued that there should be a tax on the sales price of real estate when it is sold. Why not have the seller give some of the increase in value to the sovereign, who in fact helped to increase his value providing services and facilities. (10, p. 75)

Professor Epp offers some cogent comments on this issue. ... great reliance should be placed on an income tax to finance general governmental expenditures at all levels--local, state and nation. To be most appropriate, the income base for these taxes needs to be broadly defined. In conjunction with an income tax, more extensive use should be made at state and local levels of capital gains tax. This tax is especially appropriate in instances where society has created the capital gains, such as the increase in property values due to urban expansion.

... to obtain the land-use pattern that preserve open space provide variety in the landscape. greater use must be made of zoning and public purchase. These methods of control in conjunction with comprehensive community planning provide more effective and long run control land use than do preferential taxing systems. (4, pp. 85 & 86)

All states face a tax problem: the urban-rural fringe—at least 1 states have taken action and ma

*This number had increased to 27 by 1971.
Acquisitions for a more equitable method of taxing farm property. Some of the various approaches include:

(a) Preferential assessment law.
(b) Zoning and planning.
(c) Land use control.
(d) Tax-deferral system.
(e) Sale of rights to develop.
(f) Easement.
(g) Taking schools off the property tax. (11, p. 39)

Any measure designed to provide tax relief for the farmer must be consistent with the existing institutional structure. Local units of government are "creatures of the state". They are dependent upon the state constitution, legislation and judicial decisions for their organization, powers, duties and methods of operation -- including the collection and spending of public funds. Choices in financing public services are limited in the short run by this legal framework. Most of the major changes recommended by tax authorities are not permitted by the existing legal framework in Mississippi.

The most obvious means of providing short run property tax relief is to improve property assessment and property tax administration. "The appraisal of property -- just as the verification of income tax or sales tax returns -- is a technical job which requires professional skill and knowledge... A long and disgraceful record as proven that local property tax administration except in rare circumstances will fail. Sporadic attempts at improvement by local initiative or under state stimulus have at best been temporarily successful. If we want property tax assessment to cease to be a political football then we must put it on a scientific basis. An increasing number of people are coming reluctantly to the conclusion that this will not be accomplished until the appraisal of property is divorced from local administration and made uniform by the same method by which intercounty utility property is appraised in most states -- under uniform standards on a state-wide basis. Home rule will be more effectively guaranteed by leaving the decision on tax rates in fact as well as in name to locally elected responsible bodies."

The South Carolina Constitution is similar to that of Mississippi in that the assessor must follow value for assessment purposes. Late in 1968 the President of the South Carolina Association of Assessing Officials proposed property tax relief for farmers in the urban-rural fringe as follows: Now what is the assessor's function with respect to legal requirements and how far can he go?

(1) He must follow value for assessment purposes; however, what value? I submit, one sale does not make the market and speculative sales are not necessarily market value.
(2) The value he should use in my opinion is somewhere between true agricultural value and speculative value.
(3) What factors should he consider (there are others)?
   1. Past sales prices of acreage.
   2. Current sales prices of acreage.
   3. Past history of actual development growth.
   4. Zoning and restrictions. If any.

From these factors, he can project how long it will take for the urban area to reach and need the acreage tract for development. The assessor must keep in mind that all the acreage cannot be developed at one time, and also, if all the acreage were put on the market at one time, then the value would be less. Based on his forecast for the future, he then can discount present values (actual market value) of acreage ready for development to the actual value that it has today, while the land waits until it is ready for development. In most cases, this value will be above agricultural value, and yet below speculative value.

This approach may not be fair to the farmer; however, it would comply with the law and would be uniform and equitable with the values on all other properties. (10, pp. 73 & 74)

This suggested assessment procedure would require a high level of competence of the tax assessor. Care should be exercised to assure that it is applied only to bona fide farmers. There should be appropriate safeguards to prevent the speculator from enjoying reduced taxes while he waits for his land values to appreciate.

Short run solutions to the "property tax crisis" fall into the category of minor corrections or palliative measures and will not do the job. As stated earlier in this letter, a major question that must be answered is: How should the over-all tax structure of the state and local governments be adjusted to provide more equitable taxation (including real property taxation) in response to social and economic adjustment. This, of course, will require modification of the existing legal institutions pertinent to taxation.

The problem is, however, broader than the tax issue. Commenting on use-value assessment as one means of providing property tax relief to farmers, Professor Epp has said: I do not intend to belittle the efforts being made to devise a program of property tax relief for farmers by addressing my suggestions to other related problems. I do hope, however, that people will realize the limitations in use-value assessment and will consider needed long range changes in the way we pay for governemntally provided services and in the way we control the patterns of land use. (4, p. 86)

We in Mississippi would do well
to heed the words of Raleigh Barlowe when he says: ...What do we want in Michigan? What do we want our southern counties to look like in another 10 or 20 years? Answers to these questions naturally involve value judgments. If we like the changing look of our countryside, or if our chief interest is in making money through real estate speculation, there obviously is little reason for concern. But if we are concerned about the blighting of prime agricultural areas by urban incursions, if we feel that our best agricultural lands should be protected for future food production purposes, if we feel that open spaces and the rural landscape around our cities should be protected as part of our environmental heritage, or if we feel that a more orderly and efficient process should govern the development of rural lands for urban-oriented uses, then we have genuine cause for concern.

I am very much concerned about what is happening. I feel that the time has come when the state of Michigan must act to protect its future. Many of our communities and counties already have planning commissions and zoning ordinances and we have state regulations that affect new subdivisions. The time has come, however, when we should start to plan on a statewide basis for how we want the state to look in the future, and then to act to bring about the necessary coordination of implementive efforts. (1, pp.17, 18, & 19)

Barlowe then adds: Some of the principal weaknesses of the straight use-value assessment and the deferred taxing arrangements as land-use directional measures can be corrected by coupling them with other types of land-use measures. An eligibility rule that limits use-value assessments to classes of land zoned for particular uses or a requirement that local planning agencies certify the eligible lands as primarily suited for the accepted uses has the beneficial effect of limiting the application of this taxing arrangement to the lands for which it was intended. Requirements that eligible owners secure given portions of their income from rural business pursuits or that they live on the land and not have incomes above some maximum level can keep these arrangements from becoming a boon to urban speculators. Some degree of permanence in the retention of the eligible lands in open-space uses can be achieved through the rigid administration of zoning ordinances, the establishment of statewide agricultural and conservation districts as in Hawaii, the creation of agricultural preserves as has been suggested in New York or through contracts with private owners involving development easements as has been tried in California. (1, p. 22)

A recapitulation of the above may be presented in the form of questions as follows:

1. Should the use of the property tax be restricted primarily to property-related services and funding of services that are national or statewide in nature (education and welfare, for example) be shifted to state and national levels? If so, what changes in legal institution will be required to accomplish this?
2. Should the Homestead Exemption and other property exemptions be terminated and a credit against the state income tax be granted to groups of taxpayers deemed as deserving of tax relief?
3. Should the authority of local governments to impose a sales tax be terminated?
4. Are changes in the constitution and the statutes needed to permit a more orderly and efficient development of rural lands through the use of taxation and land-use planning combination?

Many fiscal experts around the country would answer yes to each of the above questions, but would do so with serious reservations to what changes are needed. Research is needed to determine the economic effects of shifting large proportions of public expenditures to income and sales tax by removing them from property tax. Would the benefits capitalized into higher prices and land and other affected property? Some say that land values would skyrocket, that there would be a tremendous capital gain, and lead to a vast withholding of land from use and a lot of other dire consequences. What would be the shift tax incidence? It is quite obvious that the sales and income tax would have to be collected by the state and Federal Government. How would the legitimate local state and Federal interests be affected by the needed three-way sharing of revenue and responsibility? How would the citizens assure that the tax levy on property would really be reduced by an amount of the costs of services that are shifted to other forms of revenue? Would local special interest groups find other programs to absorb the initial reduction in property taxes? Many more questions could be asked. It is the skill of the researcher is needed not so much to invent new sources of tax revenue, but rather to determine the economic impact and incidence of proposed new systems, and the administrative structure needed to assure efficiency in the use of the tax dollar, equity among income groups, and fulfillment of the goals sought in the public's vice. (5, p. 28)
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