

Proposition 13: The Anti-Georgist Tax Reform Measure Falsely Touted as a Populist Victory

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Abstract

This article examines the anti-democratic consequences of California's Proposition 13, which capped property taxes in the Golden State at 1 percent market value. It also challenges the populist origin story of Proposition 13, showing instead the influence of money and political capital in its passage. Finally, this article suggests how to reform the property tax system in California along more Georgist lines.

Forty years ago this June, California voters made a foolish decision that radically altered the state's public revenue system to the detriment of local communities and new homeowners. Eager for tax relief, voters in the Golden State overwhelmingly approved a citizen's initiative that capped property taxes at 1 percent of the 1975-6 market value and prohibited the taxable value of property from increasing more than 2 percent, or the cost of inflation, per year. Additionally, rather than reassessing property at market rates each year, reassessment only occurs when property changes ownership.

Tax relief was not all that the measure provided, nor was it the central purpose of the initiative's co-authors Howard Jarvis and Paul Gann. Proposition 13 (People's Initiative to Limit Property Taxation) also restricted the taxing authority of local and state governments by requiring a two-thirds majority of both houses of the California Legislature for state tax increases, and a two-thirds majority of all voters for tax increases or any new special taxes levied at the local level. This two-pronged assault on the state's public revenue system earned Proposition 13 national recognition as a catalyst for the populist tax revolt and fiscal limitation movement that swept across the nation in the late-1970s.

Forty years later, the lingering impacts of Proposition 13 and its “populist” origin story demand examination. This study is particularly pertinent in the wake of Donald Trump’s election and the passage of the Republican-controlled Congress’ new tax bill—two prime examples of how politicians misappropriate the term “populism” to dupe taxpayers into subsidizing the lifestyles of the wealthy.

Henry George exerted a significant influence on the populist uprisings of the 1890s and 1900s that ushered in the initiative, referendum, and recall. Ironically, George’s supporters so-dominated the direct democracy crusade, that in some states such as Ohio, the citizens initiative passed only with the restriction that it could not be used to enact George’s single tax on land values. As demonstrated by the case in California, however, quite the opposite proved true: it’s difficult to imagine a tax reform bill more “anti-Georgist” than Proposition 13. And yet, an investigation of its impact and origins might reveal a few lessons for how best (and how best not) to reform the property tax, which for a variety of reasons, remains the best vehicle for implementing a Georgist political economy.

Proposition 13’s Anti-Democratic Impacts

While Proposition 13 has kept property taxes low, it has failed to prevent state and local governments from enacting new or increased taxes. In fact, the perennial budget shortfalls facing state and local governments in the decades since 1978 have prompted the adoption of new types of taxes and fees that are both anti-democratic and burdensome to the very people Proposition 13 tried to protect—homeowners.

Prior to 1978, property taxes in California hovered just below 3 percent of market rate and accounted for 90 percent of the total revenue raised by city and county governments. Today, while property tax rates vary quite a bit throughout the state depending on how many times a

specific piece of property has changed ownership, the average rate is 0.81 percent of market value. The national average is 1.1 percent.ⁱ

While Proposition 13 lowered the taxes for all property owners, it granted the greatest savings to those with higher incomes. This is in large measure because the 1 percent rate cap is tied to the date of purchase rather than the value of the property or the owner’s ability to pay. Warren Buffet most clearly illustrated the absurdity of this system in a 2004 letter to the editor of the *Wall Street Journal*. Buffet presented data (figure 1) on three houses he owns, two in Laguna Beach, California and one in Omaha, Nebraska.ⁱⁱ

Figure 1

House (year of purchase)	Market Value (2003)	Property Taxes (2003)	Taxes as a share of market value (2003)
Laguna Beach (1970)	\$4,000,000	\$2,264	.0566
Laguna Beach (1990)	\$2,000,000	\$12,003	.6001
Omaha	\$500,000	\$14,401	2.88

As the table above makes clear, Buffet pays the *least* amount of property taxes on the house with the *highest* market value. Buffet did nothing to earn that rate. By sheer luck, Buffet benefited from a measure he wasn’t even eligible to vote for.

Property tax revenue fell by \$7 billion the first year Proposition 13 went into effect. To prevent total chaos, the State Legislature provided \$4 billion in direct aid and a \$1 billion emergency loan to local governments. The State also assumed responsibility for the disbursement of property tax revenue to public school districts. To determine the share each local government received under the new law, the State directed county auditors to calculate how

much property tax revenue each local jurisdiction received prior to Proposition 13. The State then used this value to determine what percentage of the new revenue collected each district would receive. If a particular school district received \$150,000 in a county that raised \$1.5 million from property taxes prior to 1978, under Proposition 13, this school would still receive 10 percent of the revenue collected from the property tax in that county.ⁱⁱⁱ

When the total collected revenue fell, however, it didn't matter much that the percentage remained the same; schools lost money. Neither schools nor fire departments nor any other public service mattered much to the proponents of Proposition 13. What mattered most to the initiative's authors was limiting the government's ability to raise taxes. In fact, Jarvis was once quoted as saying, "The most important thing in this country is not the school system, nor the police department, nor the fire department. The right to preserve, the right to have property in this country, the right to have a home in this country—that's important."^{iv}

Ironically, Proposition 13 has made homeownership much less attainable in California. To recover lost revenue, local governments sought increased funding from the state and began implementing new "impact" or "development fees" that circumvented the amendment's 2/3 majority requirement for new or increased taxes. Typically, these fees cover the costs associated with new residential developments such as the building of new roads, transit services, storm water drainage systems, firehouses, and public parks. According to the Legislative Analyst, impact fees are roughly three times higher in California than other states and have increased 150 percent since 1991.^v

In addition to impact fees, local governments have increasingly relied on parcel taxes and "Mello Roos" assessments to finance development. Although subject to 2/3 voter approval, these taxes are easier to pass because the voters in the districts subject to the assessments are

developers who approve the new taxes before construction is complete. The developers then pass the new taxes onto the new homeowners. Mello Roos and parcel taxes are not subject to the 1 percent tax rate mandated by Proposition 13 because they are levied at a flat rate on every type of property in the district where they are passed, regardless of market value. In some areas of California, Mello Roos and parcel taxes add several thousands of dollars to a homeowner's annual tax bill.

Both local and state governments also have increased sales taxes in the wake of Proposition 13. Since 1978, at least two-thirds of the State Legislature has voted to increase California's sales tax 10 times. With a base rate of 7.25 percent, California has the highest sales tax in the nation. In some California cities such as Long Beach, the rate exceeds 10 percent.^{vi}

Sales and other types of use taxes are among the most regressive because they fail to consider the taxpayer's ability to pay. Levied at a flat rate, these taxes take a greater percentage of income from lower-income groups than from those in higher-income brackets. According to the Institute on Taxation and Economic Policy, in 2015, Californians with incomes in the bottom 20 percent paid an average of 6.8 percent of their income in sales and excise taxes whereas those in the top 1 percent paid only .08 percent of their total income in sales and excise taxes.^{vii}

Aside from its impact on taxation, Proposition 13 also is responsible for at least two other anti-democratic trends in California. These include the discouragement of local government formation and declining home ownership rates among the young and those in the lower and middle income brackets. Cities and counties formed after 1978 do not receive a share of the state's 1 percent property tax. As a result, local government formation has not kept pace with population growth. While also present at the national level, this trend is much more pronounced

in California where local governments serve an average of 11,000 residents. The national average is 6,000 residents per local government.^{viii}

Proposition 13, as the case of Buffet's two Laguna Beach homes makes clear, provides a huge incentive not to sell property purchased before 1978. This coupled with new development fees has contributed to a housing shortage in California and encouraged the speculative behavior Henry George denounced more than a century ago. Less than a decade after one of the worst real estate market crashes in the nation's history, experts warn that California is headed for another housing bubble. Last fall, the median home price in Southern California reached \$505,000, tying the record high set in September 2007 shortly before the crash.^{ix}

Proposition 13's Not so Populist Origins

The conventional analysis of the origins and success of Proposition 13, proffered by both academics and journalists, has tended to overstate the grassroots and populist elements of the campaign and undervalue the influence of Jarvis's money and support from established political interests. Robert Kuttner, a columnist for *Business Week* and later, founder of the *American Prospect*, famously described Proposition 13 as a "revolt of the haves." In a book by the same title, Kuttner described the movement that gave rise to Proposition 13 as "an authentic mass protest brought on by economic grievances." Pointing to broad support for the initiative across a diverse socio-economic spectrum, most accounts fail to acknowledge the role of luck and a favorable political climate.^x

Unlike in previous years, the mood of the California electorate in 1977-78, was ideal for entertaining a radical tax cut. Property values were soaring and despite a \$5 billion surplus, the California legislature had failed to pass any tax relief measures. At the time, Californians faced the third highest per capita taxation rates in the nation. (Today, the state ranks eighth). Polls

conducted the year Proposition 13 passed found that a majority of Californians believed their property taxes were too high and that both state and local governments were inefficient.^{xi}

Aside from an agreeable public mood, the Proposition 13 campaign benefited heavily from money and political influence. Although he liked to pose as a political outsider fighting for the people, Jarvis was wealthy and politically well-connected. Jarvis first began his anti-tax crusade in 1968, just six years after he retired from business with close to \$1 million. As president of the United Organization of Taxpayers (UOT), Jarvis spearheaded four failed signature-gathering campaigns for a property tax limitation amendment before 1978. Each time, Jarvis came up short of half a million signatures or 5 percent of the signatures of registered voters required for a citizen's initiative to qualify for state ballot. In 1962, Jarvis ran unsuccessfully for the Republican nomination for U.S. Senate.^{xii}

When his property tax limitation scheme finally qualified for the ballot in the early months of 1978, Jarvis and his co-sponsor Paul Gann recruited (and paid for) the expertise of political heavyweights. These included Roland Vincent who had managed George Wallace's 1976 presidential bid in California and at least three separate fundraising and marketing firms—the Romagen Corporation, Below, Tobe & Associates, and Butcher-Forde Consulting. He paid each group over \$100,000 (over \$380,000 today) during the course of the campaign. Additionally, the Proposition 13 campaign benefitted from the support of the Los Angeles Apartment Owners Association (LAAOA), for which Jarvis served as executive director from 1972 through 1978.^{xiii}

The Proposition 13 campaign enjoyed a fair amount of good luck. Proposition 13 qualified for the primary election in June. That May, Los Angeles County assessor Alexander Pope decided to release the year's tax bills early. Historically, property assessments were not

released until July. The bills reflected the bloated price index of the period, accurately dubbed the decade of the “Great Inflation.” In some areas, property taxes had increased by more than \$3,000 in a three-year period. Other assessors followed Pope’s lead and released the new and increased tax bills in their counties, further fomenting support for Proposition 13 across the state.^{xiv}

Another bout of good fortune the Proposition 13 campaign enjoyed stemmed from the wholly inadequate campaign run on behalf of the property tax reform measure sponsored by the California Legislature. Known as the Behr bill, state lawmakers passed this tax relief measure only after Jarvis’s initiative had qualified for the ballot. The Behr bill called separate tax rates for residential and commercial property, and as a result, also had to be placed before voters per the requirements of the California Constitution.^{xv}

The Behr bill would have been much better for California’s long term fiscal health and democratic system. The bill proposed a 30 percent cut in property taxes through differential rates on commercial and residential properties. It capped the rate increase on property to the cost of inflation and increased the income limit for senior citizens and low-income homeowners who require state assistance to pay property taxes. Finally, unlike Proposition 13, the Behr Bill (which later became Proposition 8) included a renter’s rebate in the form of an income tax credit, which also extended to those on welfare.^{xvi}

One of the greatest weaknesses of the Proposition 8 campaign was its failure to exploit Jarvis’s political background or the negative impact of Proposition 13 on public school funding. Instead, the dominant message of the Proposition 8 campaign was the overly broad statement that Proposition 13 would cost too much. With a state budget surplus of \$5 billion, California voters did not respond well to this message. The Proposition 8 campaign also failed to capitalize

on the fact Proposition 13 lacked any sort of tangible relief to renters. Whereas the backers of Proposition 13 could offer only personal reassurance that landlords would *likely* pass on the savings from lower property taxes, the supporters of Proposition 8 had a renters rebate written into the text of the measure.

Proposition 13's Lessons for a Georgist Reformer

In August 1978, Mason Gaffney published a prescient analysis of Proposition 13 and its likely impact on the state's fiscal health. Contrary to what Jarvis and other proponents of Proposition 13 claimed, Gaffney rightly predicted that reduced property taxes would not be passed to renters through lower rents nor, more importantly, would housing become cheaper in California. Gaffney also recommended two important steps to convince the public to overturn Proposition 13 in favor of a property tax more aligned with Georgist values. Both steps remain relevant today.

The first step Gaffney recommended was to publish data on the concentration of land and real estate ownership in the state. In 1978 most Californians failed to realize that as much as 50 percent of the taxable property in California was absentee-owned. Much of this property, particularly expansive ranches, vineyards, and Hollywood estates also is among the most valuable. In 1997, Gaffney pointed out that the Santa Fe-Southern Pacific Corporation, headquartered in Chicago, owns roughly 2.4 million acres in California, much of it in pricey Southern California. By exempting out-of-state owners from property taxation, Californians deprive their communities of an enormous source of revenue.^{xvii}

The second step Gaffney recommended was to show how “strikingly little” of Proposition 13 tax relief reaches renters in the state—something the Proposition 8 team failed to do before the election. Proposition 13 has discouraged homebuilding and incentivized holding

onto properties purchased before 1978 resulting in perennial housing shortages. These shortages, among other factors, have led to some of the highest housing costs in the nation and one of the lowest rates of ownership. With only 54 percent of households owning their own residence, California ranks 49th in homeownership. Only New York has a higher percentage of renters.^{xviii}

Despite Jarvis and Gann's claims that the tax savings from Proposition 13 would be passed along to renters, the very opposite proved true. According to the Legislative Analyst's Office, the greatest tax relief from Proposition 13 extends to those whose incomes are over \$80,000 per year. The incomes of most renters—and most Californians, for that matter—fall well below this amount. Furthermore, Proposition 13 failed to create a legal (or economic) motive for landlords to charge anything below the market rate for rent. With the median price for a 2-bedroom dwelling in at \$1,820, California renters face the second highest rates in the nation. Only Hawaii boasts higher rental prices.^{xix}

Presented with the statistics on the concentration of land ownership and the lack of tax relief for renters (or most homeowners), Californians might consider a Georgist-type reform to Proposition 13. In fact, one is already in the works. A coalition of public school, community, and housing reform advocates are gathering signatures to qualify a measure on the November 2018 ballot that would create a "split roll" property tax system. If passed, commercial and industrial properties would be reassessed every three years while residential properties would only be reassessed when sold. Although the initiative fails to raise the property tax rate or distinguish between land and building value, increasing real estate assessments, even if only on large corporate-owned property, is a good first step.^{xx}

A better reform would require annual assessments of all types of property and discriminate between improved and non-improved land. Furthermore, a better "split role"

taxation system would differentiate between land and building value, similar to the assessment processes in several cities in other parts of the country, particularly in Pennsylvania. The tendency of Californians to cling to Proposition 13 and the false benefits peddled by its proponents make any efforts to reform property taxation particularly difficult.

ⁱ Legislative Analyst Office. *Common Claims about Proposition 13* (2016). <http://www.lao.ca.gov/reports/2016/3497/common-claims-prop13-091916.pdf>

ⁱⁱ http://www.wealthandwant.com/docs/Buffett_Prop13.html

ⁱⁱⁱ Joan C. Baratz and Jay H. Moskowitz, "Proposition 13: How and Why it Happened," *The Phi Delta Kappan* 60:1 (1978): 9-11.

^{iv} Quoted in Clyde Haberman, "The California Ballot Measure that Inspired a Tax Revolt," *The New York Times* (October 16, 2016). <https://www.nytimes.com/2016/10/17/us/the-california-ballot-measure-that-inspired-a-tax-revolt.html>

^v Legislative Analyst Office. *Common Claims about Proposition 13* (2016). <http://www.lao.ca.gov/reports/2016/3497/common-claims-prop13-091916.pdf>

^{vi} Jared Walczak and Scot Drenkard, "State and Local Sales Tax Rates in 2017." <https://taxfoundation.org/state-and-local-sales-tax-rates-in-2017/>. While, Louisiana has the highest combined state and local sales tax rate, but California has the highest base rate.

^{vii} Institute on Taxation and Economic Policy, "Who Pays? State & Local Taxes in 2015." <https://itep.org/whopays/california/>

^{viii} Legislative Analyst Office. *Common Claims about Proposition 13* (2016). <http://www.lao.ca.gov/reports/2016/3497/common-claims-prop13-091916.pdf>

^{ix} Andrew Khouri, "Home prices in Southern California reach bubble-era highs," *The Los Angeles Times* (October 24, 2017). <http://www.latimes.com/business/la-fi-home-prices-20171024-story.html>

^x Robert Kuttner, *Revolt of the Haves: Tax Rebellions and Hard Times* (Simon & Schuster, 1980); quoted in Daniel A. Smith, "Howard Jarvis, Populist Entrepreneur: Reevaluating the Causes of Proposition 13," *Social Science History* 23:2 (1999): 173-210.

^{xi} Joan C. Baratz and Jay H. Moskowitz, "Proposition 13: How and Why it Happened," *The Phi Delta Kappan* 60:1 (1978): 9-11.

^{xii} Smith, "Howard Jarvis, Populist Entrepreneur," 177-180.

^{xiii} *Ibid.*, 182-186.

^{xiv} Baratz and Moskowitz, "Proposition 13," 10.

^{xv} *Ibid.*

^{xvi} Smith, "Howard Jarvis, Populist Entrepreneur," 182.

^{xvii} Mason Gaffney, “Proposition 13: An Alternative Reform” (1978).
<http://masongaffney.org/blog/index.php/1978/01/proposition-13-an-alternative-reform/>

^{xviii} <https://www.census.gov/housing/hvs/data/rates.html>

^{xix} <https://www.apartmentlist.com/rentonomics/rental-data/>

^{xx} John Fensterwald, “Initiative backers betting 2018 will be the year to take on California’s Proposition 13.”
<https://edsource.org/2018/initiative-backers-betting-2018-will-be-the-year-to-take-on-californias-proposition-13/592605> See also, Liam Dillon, “A Major Change to Proposition 13 takes its First Step Toward the 2018 Ballot.”
The Los Angeles Times, (December 15, 2017). <http://www.latimes.com/politics/essential/la-pol-ca-essential-politics-updates-a-major-change-to-proposition-13-takes-1513368938-htmstory.html>