HENRY GEORGE
SCHOOL OF SOCIAL SCIENCE
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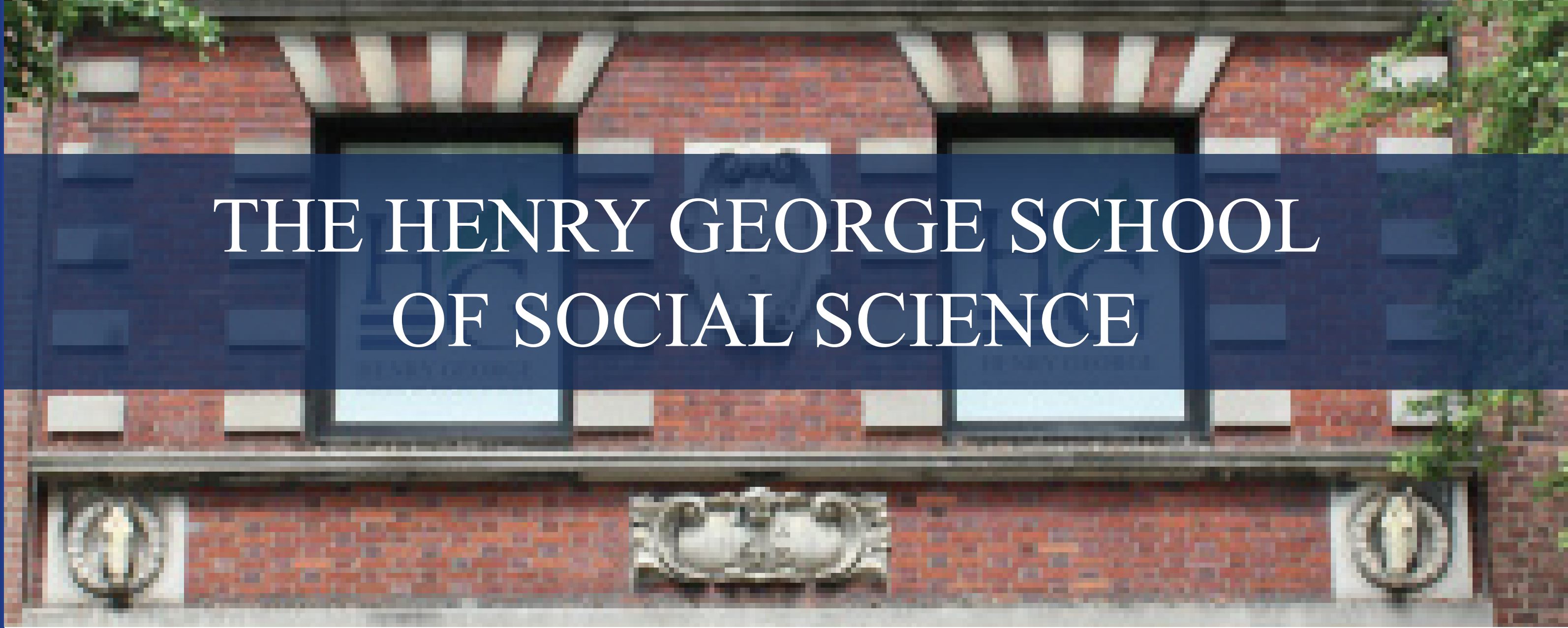
To Plug Budget Hole, San Francisco Should Look to the Past

By Ibrahima Drame and Alan Tonelson



THE HENRY GEORGE SCHOOL OF SOCIAL SCIENCE

The primary mission of our school is to educate the public on the intellectual legacy of Henry George, a pioneering political economist and reformer, to create a more productive national economy that encourages inclusive prosperity.

"Social reform is not to be secured by noise and shouting … but by the awakening of thought and the progress of ideas."

- Henry George
New York, 1883

About the Authors

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INTRODUCTION

Although its economy and therefore budget situation have brightened faster than expected since the worst of the Covid 19 pandemic, and the new American Rescue Act will actually wipe out most of its short-term deficit, like most American states and cities, San Francisco's fiscal challenges are far from over. Indeed, without major policy changes, the city can expect a future dominated by bad financial choices for controlling its chronic budget shortfalls: broad-brush growth-killing tax hikes, deep services cuts, or some combination of both. Just as important, the resulting vise will do little more than keep San Francisco running in place. Most hopes for addressing pressing unmet needs will be squeezed out.

Fortunately, the city can greatly strengthen its municipal finances and lay the foundation for enhanced, sustainable, and inclusive prosperity with a taxation strategy championed by the late-19th century American economist – and one-time San Franciscan – Henry George. Indeed, implementing George's land-value tax (LVT) can accomplish those goals without requiring a penny of federal aid. Moreover, at the right levels, the LVT can permit many and even all other city and state taxes to be cut and even abolished while still allowing spending to rise.

THE LAND-VALUE TAX

The land tax was the centerpiece of George's 1879 tome *Progress and Poverty*[1] – a monster best seller for decades after its publication. The author argued that Gilded Age America was failing to use its great wealth and recent scientific advances to create broad-based opportunity largely due to the gross under-taxation of land.

George understood that the value of land per se stems from its location near schools, hospitals, businesses and the like – not because of the genius or talents of its owners. But meager traditional property or land taxes grossly over-rewarded the income it created. As a result, holdings of land – whether developed or not – were key foundations of myriad equally unearned Gilded Age fortunes. In addition, by treating undeveloped and developed land equally, this approach to taxation created no incentives whatever to use land productively and represented an utterly squandered opportunity both to boost healthy growth and widen opportunity.

Therefore, George reasoned, steeper taxes on undeveloped land that reflected its real value, while exempting any improvements made by owners (like building housing or creating businesses) would either break up or shrink bloated land holdings and the resulting fortunes, foster development, and increase the affordability of property for many more entrepreneurs – or some combination of all three.

America uses much more of its land productively than in George's time, but evidence abounds that, if anything, it's valued and taxed at least as lightly . Therefore, a levy reflecting its genuine importance to owners would be just the revenue jackpot hard-pressed city and state governments need, and San Francisco is no exception.

SAN FRANCISCO'S STILL TROUBLED FINANCES

Even before the American Rescue Act became law, a surprisingly strong recovery from last year's pandemic-induced recession and shutdowns, along with previous tranches of federal aid, had brought

1. A free digital copy of George's best seller is available at: https://oll.libertyfund.org/titles/george-progress-and-poverty
2. See 2020 study by the Lincoln Institute of Land Policy "50-State Property Tax Comparison Study: For Taxes Paid in 2019". https://www.lincolninst.edu/sites/default/files/pubfiles/50-state-property-tax-comparison-for-2019_full.pdf

San Francisco meaningful financial relief. By late February, weeks before the decisive stimulus act votes, the City Controller forecast that a budget deficit for the current fiscal year previously estimated at $115 million would become a surplus of $125 million[3].

Consequently, the two-year budget gap originally feared to hit $653 million[4] (out of two-year spending total of $26 billion[5]) would come in at $528 million[6].

Thanks to the American Rescue Act, San Francisco will receive $464.98 million[7] in federal funds this fiscal year and next. Presumably, economic recovery will continue as well. But as the Controller's office noted in January,

"Even with assumed recovery of the City's revenues over the five-year period [through fiscal 2025-26], the City is facing a persistent structural deficit over the next five years, due in part to rising employee costs, increasing voter mandated commitments through baselines and set-asides, growing required contributions to support existing entitlement programs, and growing citywide operating costs."

As a result, "To ensure the City is able to maintain services and respond to future economic weakness, the City must slow its projected expenditure growth by making trade-offs and responsible budget decisions." But San Francisco could finance significantly greater ambitions in a fiscally responsible way by adopting the Land-Value Tax.

THE LVT EFFECT

The key to generating the resources San Francisco needs without excessively burdening both consumers and businesses with new levies is understanding how severely undervalued, and therefore under-taxed its land is.

Given the city's long torrid housing market (at least until the pandemic's arrival), this undervaluation claim may seem puzzling. But compelling evidence makes clear that San Francisco property taxes have stayed at bargain basement levels for many years.

Nowadays, property levies generate about 37.28 percent (or about $2.07 billion[8]) of San Francisco's total revenue, and 61.08 percent of all the city's receipts. But these taxes are based on an assessment that values San Francisco's land at only $260 billion[9] (as of 2018), and the per dollar rate is only 1.18 percent.

Yet according to an authoritative study, the real market value of the city's land was a much higher $622 billion[10] – and that was back in 2006. Since then, of course, all the evidence shows that it's skyrocketed, and still-surging housing prices make clear this trend has continued even through the pandemic.

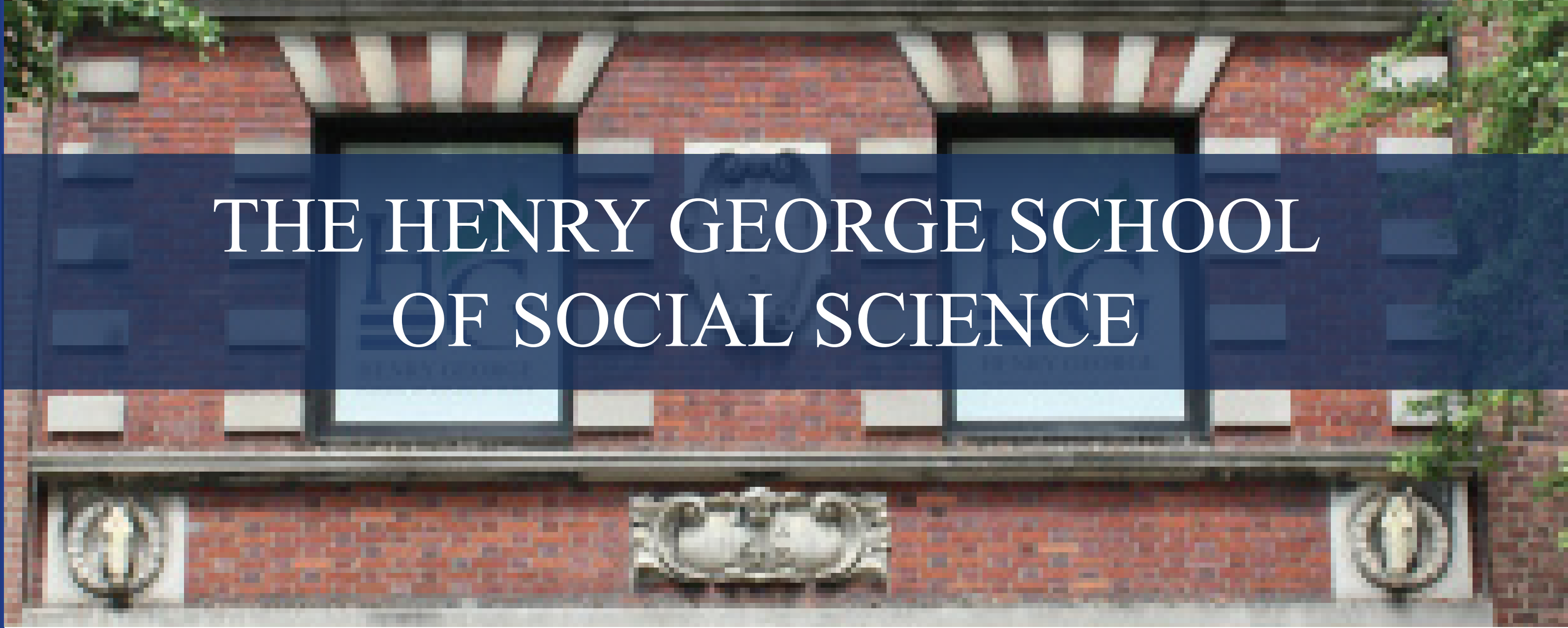
3. Sabatini, J. "Unexpected surplus gives city budget a boost". https://www.sfexaminer.com/news/unexpected-surplus-gives-city-budget-a-boost/
4. Sabatini, J. "Breed asks departments for 7.5 percent budget cuts". https://www.sfexaminer.com/news/breed-asks departments-for-7-5-percent-in-budget-cuts/
5. See this report from CBS Local "Mayor Breed Signs SF's $13.6 Billion Budget For 2020-2021". https://sanfrancisco.cbslocal.com/2020/10/02/mayor-breed-signs-sfs-13-6-billion-budget-for-2020-2021/
6. Varghese, R. "San Francisco's Budget Gap Narrows from Property Tax Gains". https://www.bnnbloomberg.ca/san-francisco-s-budget-gap-narrows-from-property-tax-gains-1.1563160
7. See https://www.nlc.org/wp-content/uploads/2021/02/State-and-Local-Allocation-Output-03.08.21.xlsx
8. See San Francisco City's Five-Year Financial Plan. https://sfcontroller.org/sites/default/files/Documents/Budget/FY2020-21%20through%20FY2023-24%20Joint%20Report%20FINAL.pdf
9. See November 19, 2018 Statement from the Office of the Assessor-Recorder. Available at: https://sfassessor.org/news/strength-property-tax-helps-sf-recognize-415-million-additional-funding
10. Florida, R. "The Staggering Value of Urban Land". Available at: https://www.bloomberg.com/news/articles/2017-11-02/america-s-urban-land-is-worth-a-staggering-amount

Therefore, if the city taxed land even according to its $622 billion 2006 value at the same 1.18 percent, the revenue haul would be not 2020's estimated $2.12 billion, but $5.09 billion. The $2.97 billion difference is more than 5.6 times bigger than San Francisco's $528 million budget for this fiscal year and the next, meaning that the city could balance its books by imposing the LVT – all the while actually cutting other levies dramatically. This prospect, crucially, should appeal strongly to backers of Proposition 13 – whose revamping or rescinding would no doubt be needed to enable the LVT's approval. And depending on its actual level, progressives would be pleased that the city could still spend some or all of its windfall on whatever social, economic, cultural, or environmental goals it wished.

It's true that not all city land is taxable or should be taxed. But assume that for various reasons (e.g., non-profit organization ownership, public recreation), 20 percent of the state's land is tax exempt. If the remaining taxable land – valued at just under $500 billion by the 2006 measures – were taxed at that 1.18 percent rate, the revenue take would still be $4.07 billion.

That sum would be $1.95 billion greater than under current assessments, and 3.7 times the size of the city's current annual deficit. In fact, the $4.07 billion LVT intake amounts to more than 73 percent of all San Francisco's current tax receipts. Thus, if the city wanted to maintain its current level of services, the LVT bonanza could enable it to eliminate or reduce numerous other taxes. Alternatively, San Francisco would have an extra $1.95 billion to provide new services needed or desired by its inhabitants.

At a time of ongoing financial stress and facing major recovery questions, San Francisco and other big U.S. cities are sitting on privately held wealth truly deserving the term "gold mine." All that's needed to unlock it for the public good is to use the key created by Henry George more than a century ago.



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