

PRINCIPLES OF SOUND TAX THEORY
AS HAVE EVOLVED OVER 200 AND MORE YEARS
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Tax theorists typically measure revenue structures according to the criteria of economic neutrality, efficiency, equity, administrability, simplicity, stability, and sufficiency. These are explained in turn.

Tax **neutrality** refers to the influence (or absence of such) that any particular design has on economic behavior. Typically taxes are perceived as a damp on economic activity - taxing income reduces the incentive to work, taxing sales discourages retail transactions, and taxing savings reduces the propensity to save. The more a tax is perceived to be neutral, the less the identifiable distortions it imposes on the economy. The common assumption of most tax theorists is that all taxes impose distortions; it's simply a matter of which ones are least burdensome to economic health. A tax which imposes no distortions is ideally best. Most of our environmental problems stem from the fact that our tax designs impose distortions on our economies.

Tax **efficiency** is much like tax neutrality, and is the measure of how much shifting of behavior it imposes, resulting in what is called "excess burden," or "deadweight loss" on the economy. Tax economists usually hold that the best taxes are those that are shifted little if at all. Because the elasticities (a technical word for the slope of supply and demand curves) of each are very different, a tax on land values and a tax on improvement values have very contrastive effects on socio-economic choices. Using a tax base that has little or zero elasticity is the best way of assuring that taxes are not shifted. Zero elasticity is another way of saying fixed supply, as, earlier noted, land is.

The principle of **equity** is central to any discussion of tax design. Tax design requires concern with both what is fair and the extent to which it must sometimes be compromised to satisfy the other principal criteria. Fairness can be evaluated according to what is termed "horizontal equity" - the extent to which those in similar circumstances will pay similar tax burdens, and "vertical equity" - how well those in different classes bear different burdens in the tax structure. It is this latter perspective that leads to the use of terms like "proportional," "progressive," and "regressive" in referring to tax structures. A tax is progressive with respect to income if the ratio of tax revenue to income rises when moving up the income scale, proportional if the ratio is constant, and regressive if the ratio declines.

There is an ancillary question of whether taxing to reach greater equity should employ measures of income or of wealth, difficult as this is to measure. Such questions of equity are a matter particularly central when discussing the property tax. This is because, as earlier noted, people capitalize their income in the course of a lifetime - frequently in property. Although claims are often made to the contrary and really comprehensive studies have yet to be done, the consensus opinion

among experts now is that the property tax is really highly progressive, especially for the land component.

Administrability refers to the ease with which a tax can be administered and collected. Taxes which distort the economy are inefficient but so are taxes that cost lots to administer. This is measured not only in the direct costs of tax avoidance and accounting expenses, but in the level of evasion and cheating, and by the cost of government auditing and policing. When the taxpaying public perceives that a tax is easily evaded, cumbersome, and unfair, it loses its legitimacy and calls government itself into question.

This is why the principle of **simplicity** is important: The more complex the tax design, the more lawyers and accountants will find loopholes, encourage the appearance of unfairness, and drive up the cost of its administration. People know that with simple taxes other parties are also paying their fair share, and all this enhances the legitimacy and therefore the compliance of the tax system. In recent years it has become possible in principle to assess land value by computer algorithms (called computer-assisted mass appraisal, or CAMA), obviating the need for assessors altogether. Isobars can be drawn on maps showing land values similar to how elevations in land topography are shown on geographic maps.

Stability refers to the ability of a tax to produce revenue in the face of changing economic circumstances. Income and sales taxes, for example, vary greatly according to phases in the economic cycle; the property tax, in contrast, is highly stable regardless of the state of the economy. This is one reason why school administrators have typically been supportive of using the property tax base rather than some other tax to support school services.

In assessing the value of a tax it is also important, of course, to understand its potential to bring in revenue for the purposes of government, usually deemed revenue **sufficiency**. Income, sales and property taxes, along with corporation taxes to a lesser extent, have come to be regarded as the workhorses of the American revenue structure. But, as anti-tax politicians are quick to note, the higher these taxes are, the more they impose a drag on the economy. This is why one should ponder whether to consider raising taxes which have demonstrable distorting effects.

In contrast, a tax on land value alone, which is totally neutral, measures up so well that it looks like the perfect tax! These criteria support the claim that taxing land alone is a more appropriate solution to spatial configuration issues and to tax issues than any other remedy.