LAND VALUE TAXES AND WILMINGTON, DELAWARE:
A CASE STUDY†

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Wilmington is a city with a steady population of 72,000 in the northeastern corner of Delaware, 30 miles southwest of Philadelphia. The City has had some economic development successes in the past decade, attracting thousands of jobs in financial services and housing the legal support for the “Corporate Capital of the U.S.”

Some of these successes include a vibrant riverfront with outlet stores offering tax free shopping, a residential development of older, mostly vacant buildings near the Amtrak Station called the Ships’ Tavern District; the continuation of the development of MBNA (the world’s largest independent credit card lender) headquartered in downtown Wilmington, soon to occupy 1.75 million square feet of office space; and the conversion by the Buccini/Pollin Group of several older office buildings into luxury residential apartments and upscale restaurants. Wilmington is also the home office of AstraZeneca and the DuPont Company.

Nevertheless, Wilmington, like many other cities, now faces a fiscal crisis. Forty-two percent of the property in the city is tax-exempt, and eleven percent of the residential properties are either uninhabitable or uninhabited. Ten years ago the City faced a similar fiscal crisis, and some of the Mayor’s advisors (including this author) proposed using land value taxes instead of the traditional property tax. Mayor Daniel S. Frawley
accepted the recommendation and vowed to include it in his re-election campaign platform.

**Positive Economic Impacts**

The arguments that persuaded the Mayor included the following:

**Public Sector Actions Create Value.** Much of the price paid for land, especially urban land, reflects value given to that land by the government. These amenities provided by the public sector include schools, roads, utilities, zoning rules, and parks. By not properly taxing the land, this enhanced value is captured by the private owner. The resulting land value does not reflect the effort of the landowner but rather that of society and its institutions. A carefully formulated land value tax can capture these land values for the government.

Two identical pieces of land, one with a modern structure, and the other with a run-down building, will be taxed differently under most urban property tax schemes. The modern building will be taxed much more heavily, yet the governmental services required for the run-down building, such as police and fire protection, may actually exceed those necessary for the modern structure.

The single rate tax on all property actually provides incentives *not* to maintain a piece of property. If a building deteriorates because it hasn’t been kept up, the tax base is often lowered and the tax liability reduced.

**Efficiency and Growth.** Some economists have placed the efficiency costs of our current tax system as high as 40% of the revenue generated. These costs are the dis-incentive effects on economic activity caused by taxing the income of labor and man-
made capital. A tax on land values has no disincentive effects; the quantity of land is fixed and does not change. However, holding the land in an unimproved, non-income generating form becomes expensive with a land value tax. Under such a tax system, owning dilapidated buildings and vacant lots would carry high costs. Taxing improvements discourages owners from upgrading their buildings. Using lower, or zero taxes, on newer buildings and improvements of properties in poor repair encourages these upgrades. C. Lowell Harriss, long a proponent of land value taxes says “cities that urgently need to replace obsolete buildings paradoxically base much of their financing upon a tax that encourages owners to hold on to deteriorated structures and penalizes owners of new ones.”

Dick Netzer (1998) estimates that a 2.6% tax solely on land value throughout the United States would result in tax collections equal to those gathered by today’s property tax on land and structures. In addition, under such a land tax, as land is transferred to more profitable uses, that tax rate could fall as the land values increased.

**Discourage Speculative Land Holding.** When landowners expect price appreciation on the land held, under most property tax regimes, there is little penalty for owners letting their property deteriorate. Under a tax primarily on land values, owners would be forced to fix up their property so that it was an income-earning asset, or sell that property. Initially the higher land tax might cause the value of the land to fall, as owning the land constitutes an obligation to pay the higher tax, which would be capitalized by lowering the price.

**Improve the Health of Center Cities.** Urban sprawl into the surrounding suburbs could be reduced with a tax system that relies heavily on land value taxes. By
making each parcel of land within the city more productively utilized, there would be less incentive to work and live outside the city. This is especially important for an older city like Wilmington, where relatively healthy suburbs surround the city.

A similar point is that the stronger city center would reduce the shrinkage of the natural environment around the city, leaving more open spaces and greenways.

**Tool for Devolution of Government Functions.** Both in America and in many other countries around the world, the theory of having government services paid for at the level of government closest to the benefiting population has gained considerable strength. A healthy land value tax system would support this Hamilton-Tiebout model in the public finance literature. In an era of looming federal budget deficits, matching consumer preferences for government services with tax sources becomes even more attractive.

**Easy Assessments and Compliance.** Netzer estimates the compliance, administration, and evasion costs of land value taxes as 2% of revenue collections, compared with 30% for federal income taxes and 20% for state sales taxes. The assessment process would certainly be easier, more open, probably fairer, and would carry fewer grievances.

**Why Hasn’t Land Value Taxation Been Universally Adopted?**

**Political Power of Land Owners.** Since many politicians are land owners and involved with making decisions on land uses for many of their friends, they prefer not to disturb current property values, and especially not to impose high costs on land speculators. The politicians also are fearful that low-density users of land in valuable areas will have to bear higher tax burdens. Examples of such low-density users are car
dealerships, restaurants, some retail, and parking lots. Grandfathering their former tax liabilities or gradually phasing in the new higher land value taxes could partially offset the greater burden on these properties.

Most residential land owners would benefit from land based taxes. In a Drexel University study of Philadelphia this year, under a land value based tax system, 76% of households would see their property taxes reduced. The researchers found that land was 21% of the total value of land and buildings.  

Implementation Problems. Some economists find difficulties in assessing the value of land for non-residential urban uses, especially in central city locations. Mills argues that there isn’t a reliable mechanism for assessing land values in such regions. Others suggest ways to overcome these problems, as for example, by having a city purchase and demolish a building and selling the remaining land to increase the accuracy of land price assessments.  

Transition Costs. These costs exist, but in a city with a good land registration system, one that already separates the value of land from that of the structures, and in a city with a decent tax administration, these costs will be minimal. The property tax rolls in Wilmington did and still meet these criteria.

Empirical Evidence

Pittsburgh 1976-2001

Oates and Schwab (1997) have done the most careful analysis of the Pittsburgh experience with land value taxes. They studied the first fifteen years after the reduction of taxes on structures to one-fifth of that on land. They found that Pittsburgh’s building
activity had an unprecedented increase in the 1980s, “a striking outlier of the fourteen cities studied”. The real value of building permits grew 70% annually in the 1980s relative to the twenty-year period before the tax reform, and during the same period of time in thirteen of the fourteen cities studied, building permits declined. The increased building activity was confined to the City; the suburban Pittsburgh area, without the two-tier structure, saw a construction decline.

**Pittsburgh after 2001**

In 2000, Pittsburgh had a countywide reassessment of all property. Voters thought that if they could get the property tax on land assessment reduced to the lower tax rate on buildings, they would end up with lower property tax liabilities. So City Council removed the two rate graded tax system that had so successfully encouraged Pittsburgh’s redevelopment. Today, most residential and business property owners have higher tax burdens; since by using a single rate on both the land and buildings, the tax rate on buildings had to increase to generate sufficient revenue. Predictably, construction activity fell. Comparing the two years before rescission with the two years after (2001-2), pre-rescission construction spending was 21% higher than post-rescission. In both the U.S. and the suburbs of Pittsburgh, construction activity was higher in the two years 2001 and 2002.

**Other Cities and Countries**

Fourteen other cities in Pennsylvania have had very positive economic development results with two-tier property taxes, where the tax on improvements is only
a fraction of the tax on land. For example, Harrisburg saw its stock of vacant buildings 
decline from 4000 to 500 in the last two decades.\textsuperscript{11}

One of the Mayoral candidates in the Philadelphia November 2003 election, Sam 
Katz, publicly backed the land value tax, as recommended by the Philadelphia Tax 
Commission in 2002. He used this platform to appeal to the working class community, 
considered essential for his successful election. He was, however, not elected. 

More than 700 cities worldwide have successfully adopted the two-tier system of 
property taxes, including many in Australia and Eastern Europe. Fairfax, VA is also 
currently considering such a tax system.

\textbf{Back to Wilmington}

In 1994, the plan to restructure Wilmington’s property tax in order to shift the 
burden away from structures and toward land, was to be phased in over five years. This 
would have raised the rate on land to 0.04\% compared with the existing rate of 0.008\%. 
This would have increased the property tax revenue collected on land values by six fold, 
allowing for a significant reduction in the tax on buildings and perhaps a reduction of the 
City’s wage tax. 

Before the Mayor could run for re-election, he met a premature, sudden death, 
suffering a heart attack while playing basketball. The proposal was then dropped. The 
current tax rate in Wilmington on both land and buildings is 0.0131\% (or 1.31\% per $100 
of assessed value). Assuming the current residential tax base of $149 million on land and 
$810 million on buildings, using today’s anticipated revenue from the assessed residential 
real estate value of $11.6 million, the tax on buildings could be reduced to 0.0\% by only 
increasing the tax on land to 0.09\%. As in other cities where such tax structures have
been implemented, two thirds of the owners of residential properties would face lower tax bills. There would also be a residual of $1.8 million to help offset a portion of the additional burden that such a tax structure would impose on certain commercial establishments, such as auto dealerships, parking garages, and others with large footprints relative to their revenue generating ability.

Now with the new fiscal crisis, a creative form of land value taxation is under serious consideration. That form is a fine on all vacant dwellings. The fine is graduated and increases as the length of the vacancy increases. If the dwelling has been vacant for one year, the fine is $500, increasing arithmetically to $5000 if the structure has been vacant for 10 years. This fine qualifies as a land value tax by punishing speculators and encouraging owners to generate income from their properties, or alternately, to sell their structures. This fine can achieve many of the same goals as the two-tier tax on land and buildings. The economic growth and efficiency benefits are predicted to be extremely high. In addition, these fines are expected to generate an additional $2 million revenue for the City in fiscal 2004.

As in most other older urban areas, the City of Wilmington is pursuing an aggressive campaign to rid the landscape of the 3500 vacant homes identified by the 2000 U.S. Census\textsuperscript{12}. A recent (2003) report by Kise Straw and Kolodner, a Philadelphia architectural firm, found that 50\% of Wilmington’s housing was owner occupied, and that with its fairly stable population base; there was an excess supply of housing.\textsuperscript{13} They recommended an extensive demolition plan for the vacant housing, and the City plans to tear down approximately 50 of the homes in the worst condition this year. To date, 700 have been identified as not viable for rehabilitation.
Fourteen percent of the vacant homes are owned by public entities, e.g., the City, the Wilmington Housing Authority, and the Wilmington Housing Partnership. These were mostly taken for non-payment of taxes and are gradually being auctioned to the highest responsible bidder with a reasonable plan for the dwelling. One hundred eight such properties will be sold this year.

**Conclusion**

Although many economists prefer a pure land value tax to the fines implemented recently in Wilmington, those fines should accomplish some of the same resource allocation and efficiency goals long thought desirable in a pure land value tax.

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1 University of Delaware, Newark, DE 19716, craige@lerner.udel.edu
4 Netzer, op. cit., p. 121
5 ibid, p. 125
6 McCain, Jensen and Meyer. Research on the Value of Land and Improvements in Philadelphia. prepared for the City Controller, 12 March 2003, p. 15
8 Anas, Alex. Commentary to Mills article, ibid
12 3500 is 8% of the total housing units in Wilmington.
13 Kise Straw & Kolodner. City of Wilmington Vacant Property Strategy and City of Wilmington Residential Improvement Zones, 14 March 2003