The Progress of Poverty

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AN ALL-OUT-ATTACK on poverty has been the slogan of progressive US politicians of both parties during the past few years. And many more heated words on the subject will be exchanged in the coming elections. A recent study completed here by Letitia Upton and Nancy Lyons of the Cambridge Institute shows that there is no room for complacency in the poverty war and that although millions of dollars in various forms of relief, subsidy and aid have been re-distributed by the Federal and State governments in the last few years, the relative position of the poor has worsened rather than improved.

Looking at the picture from the income side the researchers found that the 10.4 million families in the poorest fifth received less than six per cent of the total money income or about $3,054 a year. On the other hand the nation's richest fifth took over 40 per cent of income or an average of $23,100 a year. Between 1958 and 1968 the dollar earnings gap between the top and bottom fifths of US families increased by over $5,000 a year. And if little solace can be found in the income figures, the picture of relative wealth distribution is even darker. The top fifth of Americans owned 77 per cent of the personal wealth in 1962 and probably own more today. The top one per cent of wealthiest Americans receive nine per cent of total income but own between 20 and 30 per cent of all personal wealth and have done so for decades. Herbert Gans of Columbia University has argued, "such inequality is a major source of social instability and unrest and is even a cause of the rising rates of crime, delinquency and social pathology - alcoholism, drug addiction and mental illness."

The irony of this is that Henry George, writing in 1879, came to much the same conclusion. Unfortunately few contemporary politicians have as good a grasp of the causative factors of inequality as George had. Those who are concerned with the problem, like Senator McGovern and his supporters, show little understanding of how inequality arises. They, like most analysts, are preoccupied with looking at the income end in money terms rather than at the streams of income earning and their sources.

Towards the end of last year, speaking at the 64th Annual Conference of the National Tax Association, Professor M. Mason Gaffney tried to set the delegates on the right course. He pointed out that savings rise with income and that with savings one acquires property which in turn attracts a disproportionately high share of other income.

A 1948 study showed that the highest class of income earners receive not only 23 per cent of all income but 78 per cent of dividend income and 45 per cent of rental income. Looking at it another way, about 45 per cent of the people own no meaningful value of real property at all. And, as Professor Gaffney emphasized, the ownership of large property gives control of other assets. "Property," he said, "is borrowing power and credit rating: all studies show interest rates to be very regressive with size and quality of collateral, and terms easier. But simple borrowing is only the beginning. With great wealth one goes into banking and exerts multiple leverage. The story has been told many times . . . collateral, leverage, conglomerates, interlocking directorships, mergers, lender suasion, industrial leadership, pyramiding, market control. Control is power and status and control is a source of additional income as revealed by the premium prices of shares during battles of control."

Although Professor Gaffney's main purpose was to refute persistent argument that property taxes are regressive particularly for the poorer owner—a refutation which was masterly, scathing and scholarly—he also high-lighted the importance of land rental income in wealth accumulation. Pointing out that in most property-tax assessment land is under-assessed and under-taxed, he emphasized that recent studies showed that land (at least in California and Washington DC) is about 40-50 per cent of the total true property valuation. Moreover, that as the proportion of land in real estate tends to rise faster and as taxes on that value fall directly on the owners, the non-shiftability of property taxes rises as total values rise. In Professor Gaffney's view, income taxes fall far short of attacking the inequalities in wealth—property taxes, (especially land taxes) are far superior.

"Ability-to-pay," he points out, "derives from wealth as well as current income. Property taxes reduce the differential effect of inherited wealth on the current generation. They strike directly at concentration of economic and other power based on wealth, so promoting competition and better opportunity."

In comparing the effectiveness of the land element of the property tax with income tax as a re-adjustor of wealth, many analysts fail to take into account very large sums of "imputed wealth" which frequently only manifest themselves as income on rare occasions when declared as capital gains at the time of sale. An asset in land appreciating over say a nineteenyear period represents real income during the period but it becomes visible only on transfer. If the imputed income was taxed at source annually as an *ad valorem* charge on the land, not only would it encourage the wealthy to hold a greater percentage of their assets in liquid funds to meet the charges, but would also most probably act positively in encouraging a better use of land. In fact the tendency would be towards freeing the real estate market of its log jams caused by tax-haven seekers. The effects would rebound throughout the economy as the supply of land loosened. More people would use land rather than hoard it and its selling price would be decreased proportionate to the tax rate, thereby diffusing ownership and earning ability.

As a sidelight let us look at what is happening in Mexico, where the government has agreed under pressure to permit owners to grant thirty-year leases on choice location beach front property to aliens, mainly wealthy US citizens. Although there is no guarantee that a future government will allow the leases to be renewed on expiration, at least one banker believes that around the year 2000 there will not be enough wealthy Mexicans to purchase the expensive properties developed by Americans, even if the government restricts sales to native born residents.

With seaside lots in California costing $90,000 and the Mexican equivalent costing only $12-16,000, the attraction for Americans is easily seen. If, instead of yielding to the pressures of land owners seeking higher rents from rich foreigners, the Mexican government decided to tax the desirable properties at near rental value, the Americans' bidding advantages would still be retained but the lessening of the general taxation burden on the poorer Mexicans who have only their labour to offer, could help them to considerably improve their earning capacity in a thirty year period! At the end of which time more native born people would no doubt be in a stronger position to compete with the foreign invasion.

It would seem from this little story that not only are Americans on the wrong tack themselves in trying to achieve a more equitable distribution of wealth through the income tax within their own country, but that because of equally false policies pursued elsewhere they are exporting and compounding the problem for the "have nots" of their Latin neighbours. Let us hope that Professor Gaffney's light will burn brightly in the future and that, if his advice is not heeded at home perhaps it will be taken more seriously elsewhere on the American continent where the need for it is proportionately greater!