

Tax Incentives

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The findings suggest that localities may achieve more success in economic development through infrastructure improvement than through tax abatement or other business subsidies. Yet increased infrastructure expenditure is likely only if externality problems can be controlled. A municipal taxing district must be allowed either to retain most of the financial benefit resulting from infrastructure improvements or to pass some of the costs along to other taxing bodies that

share the benefits. Tax-increment financing allows for more of the benefits to be retained by the municipal taxing district.

Conclusion

Under any of the circumstances considered in the above analysis, property tax abatements are shown to provide negative results to society. Society could benefit from federal laws restricting the use of property tax abatement programs. Tax increment financing holds more promise as a tool of economic development, though tax shifting problems can result. Shifting might be reduced through index

ing, which would permit the base year tax base to increase by the rate of inflation. Other possible improvements in the use of TIF might include permitting expenditures on infrastructure only, allowing affected taxing districts some control over expenditures, and establishing stricter guidelines for creating TIF districts.

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Foreign Ownership:

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In a society without laws, ownership is nothing more than the ability to use property until a more powerful party terminates that use by force. Fortunately, the U.S. is a land where law rather than force rules. The ultimate benefit of ownership, where law prevails, is the right to receive residual income and other residual values. There certainly may be other attendant benefits, such as the right to use, although owners routinely assign rights of use to other parties through leases.

Yet vocal critics in this country, from businesspeople to legislators, have attributed much greater importance to the concept of ownership in bemoaning the presence of foreign purchasers in the U.S. real estate market. They note that the British, Canadians, Dutch, and, particularly, the Japanese (with abundant capital but little available real estate) purchase income producing buildings at record prices in U.S. cities, and fear that America is being sold away. Are their concerns well-founded?

We suggest that they are not. There are two reasons why we should welcome foreign purchases of U.S. income producing real estate. The first is the nature of the ownership right, and the second is the economic benefit that accrues to both the real estate market and the nation's economy as a result of foreign purchases.

One of the first lessons in any introductory real estate course is that real estate ownership, because of the immobility of the asset, involves a bundle of rights. The rights are protected, but also limited, by federal and, more directly, local laws. Among the limitations are taxation, emi-

nent domain, and the police power.

Through the police power, local governmental units have instituted rent controls on income producing residential property in several cities. Notable examples have been New York City and Berkeley, California. The owners of affected buildings, who are in many cases vocal, visible, and voting local citizens, are unable to curb rent controls when the majority of the local population favors them. Certainly we can not expect that foreign owners would fare any better in limiting voters' control of their investment returns. (The recognition that rent control can be enacted by unhappy citizens should not be equated with an advocacy of its use.)

In other words, if parties without the ability to vote were to control a high percentage of an area's income producing real estate (residential or commercial), and were to attempt to use that control to the detriment of the local economy, the citizenry could simply legislate away the owners' residual returns by enacting rent control statutes (or perhaps levying added taxes on real estate ownership, or even taking property under eminent domain). Foreign purchasers' fortunes are clearly tied to those of local owners, who have greater ability to influence land use issues. Foreign interests, then, have no incentive to become the majority landowners in a jurisdiction. The problem, to the extent that a problem may exist, is self correcting. In buying U.S. real estate, knowledgeable foreign investors show confidence in a system in which the protection of property rights limits political risk.

Foreign purchasing power also benefits local real estate markets. Well-meaning parties who worry that property may become priced beyond the reach of American buyers would nevertheless likely state that an owner should be allowed to sell for the highest possible price. We would not strengthen our real estate markets by assuring buyers that their artificially low purchase prices would be matched by artificially low future resale prices resulting from restricted ownership.

Finally, the inflow of foreign purchasing power benefits our nation's economy. For example, Americans buy Japanese consumer products, and use them in the U.S. to enhance the quality of life. The Japanese, on the other hand, buy U.S. real estate, and have no choice but to leave the property here for the benefit of domestic users. In addition, the foreign owners' dollar-denominated residual returns may well be spent on more dollar-denominated American goods.