

**State and Local Governments Cannot Afford To Allow Real Estate Prices to Collapse
(One Man's Opinion)
by Adrian Van Eck**

That would cut tax receipts. Following this article, I am including two charts on taxes. One chart is on sales taxes. The other is on property taxes. As you will see, property taxes raise almost as much local and state revenue as sales taxes, making such levies crucial to the success of local schools across America. Some cities and states collect income taxes and some do not. Most, but not all, collect sales taxes.

But, so far as I know, local or state governments all levy a tax on the value of real estate, including housing.

This year, as a result of some unusual bursts of housing price increases, there have been quick moves by governments all over the U.S. to send out appraisers to revalue their housing. As the results have come in, they are adjusting their tax levels on property. From what I hear, it is usually not quite an even swap of rates and taxes. When they raise valuations by 25 percent, the tax rate should fall by 20 percent.

Somehow it never works that way. Governments manage to raise more via property taxes than ever before.

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to 10 homes a year, clearing \$100,000.

And the extra money is quickly spent on raises for teachers and police and firefighters and on higher costs for health insurance for public employees. Note: Courts in a few states have ruled that real estate taxes must be collected on a statewide basis and then spent evenly on poor and rich communities alike.

When that happens, voters in rich communities have often voted for extra local taxes, which allows them to keep their quality schools at current levels.

Maybe most of the Wall Street "experts" predicting a collapse in real estate values have their sons and daughters enrolled in private schools and do not relate to the problems that would be caused in cities, towns and states by collapsing real estate prices. Public pressures would force the same appraisers who have been revaluing houses upward to get back into action and reverse their most recent adjustments ... maybe even going lower than before.

This would require drastic cuts of real estate taxes and spending on schools, police and fire protection. Unless Congress would be persuaded to kick-in with more federal money for local communities (which I find hard to picture) at a time when demands are rising to lower federal spending, not raise it, there would be bitter fights galore about taxes and spending in a crucial election year.

At any rate, I have to believe that state and local politicians will do everything then can to talk up real estate values in their community, and they will revamp public policies when necessary to attract and hold employers.

They will also resist depression –style moves to gut their school systems because that will, by itself, intensify and turned downward in home prices and, hence, tax valuations. But all such talk ignores the fact that the economy is growing at a strong rate and the forces of inflation – driven by swelling money supplies in America and many other nations – is a force to keep home prices at least even.

That brings me to the last piece of hard evidence that housing is on more solid ground than many analysts now suspect: The last two charts cover total, new privately owned U.S. housing units started, and houses not yet started, but sold. The latter may sound like a contradiction. Some may ask: "How can a house be sold when it has not even been started?" Believe me, in the past three years, there has been a lot that activity going on.

At a time when home prices were rising in some areas at a rate of 15 percent per year, speculators would make a down payment on a house not scheduled for completion until six months later. They would sign a binding contract. They might put down \$5,000 on a \$200,000 house. Then, when the house was almost finished, they would reach out for a buyer at \$207,500. That was not hard to do.

By then, the builder had likely raised his own asking price to \$210,000. And those were the days when bidding contests would break out, with the final price often topping the asking price by \$5,000. So, the speculator might sell out for a \$10,000 gain, tripling his \$5,000 outlay in six months. Plus, he recovered his \$5,000 down payment when he sold. Some speculators were doing this to 10 homes a year, clearing \$100,000.

Builders did not mind at first, since speculators helped to get developments off the ground. More recently, with sales coming harder, builders have come to hate speculators, for they have become price competitors, seeking to get out even. Now, it is not uncommon for builders to make a buyer sign a pledge to live in the house for a year.

This, plus the cooling down of starts, helped to reduce supply. I have said for months that this was goal of the Fed and mortgage lenders, as a way of protecting and preserving the value of existing homes.

Source: Adrian Van Eck, Adrian Van Eck's Real Estate and Bank Advisory, December 2005. www.vaneckillman.com. As printed in the Wall Street Digest, January 2006.