The children of Beverly Hills headed back to school last week. At just under $12,000 per child, the rest of Los Angeles County may be envious of Beverly Hills’ spending – while much of the country would laugh derisively. How is it that ultra-rich Beverly Hills spends less on its schoolchildren than the states of New York, New Jersey, Connecticut, Massachusetts, Rhode Island, Wyoming, Vermont, Maryland, Maine ... even Alaska?

In an iconic town whose cost of living is 65% above the national average, where the median sale price of a home is $2 million, one might ask, don't they care about their kids? (Yes, Alaska relies on oil revenue – but so does Beverly Hills Unified ... to the tune of $2,000+/year per student from the well on the high school campus.)

Of course Beverly Hills cares, but since Proposition 13 was passed in 1978, whether we Californians care about kids has been a tough question. Rolling back assessed property values of long-time owners to 1975 levels, raising assessed values only if a sale occurs, restricting existing assessments to no more than a 2% increase per year, and capping the basic tax levy at 1% – plus all the legislative actions to implement this – certainly has had an effect on school spending. But what effect? I took a look at Beverly Hills.

About two-thirds of Beverly Hills' total assessed property value lies in single-family houses and condos. Of those homes, 16% still enjoy a 1975 base year assessment – carrying a meager 3% of the total residential tax burden. Meanwhile, the 42% of local homes that have changed hands in the past 11 years shoulder 61% of the residential contribution towards schools, police, fire, roads, courts, city and county services. (The other 42% of homes showing a change of ownership between 1976 and 1999 get a some benefit – carrying about 35% of the total burden.)
One home in six definitely rides on the super-discounted senior fare. But does the buck really stop with widows and retirees? What's that we've been hearing about commercial property – the office buildings on Wilshire, the stores on Rodeo Drive?

An even larger percentage of those parcels – 21% – enjoy the same tax break as their elderly residential neighbors, also shouldering just 3% of the commercial contribution to local services. Their competitors – who've bought in the last 11 years and are more likely to actually operate the businesses on their properties – carry the lion’s share of the burden, like newer residential neighbors.

This uneven playing field doesn't stop there. When Beverly Hills transitioned to a locally funded school district last year (receiving only minimal “local aid” from the state), it cut down dramatically on transfer students from outside the district. With revenues flat, getting spending-per-student up is coming from getting the number of students down.

A quick look at other locally funded districts (Palo Alto, Carmel, and my own local Menlo Park-Atherton district) would suggest this is a short-term fix. Parents desperate for a good education for their children are willing to rent. Demand for family housing increases in the single-family housing detailed above, but often multi-unit residential is the only choice for people without the $20,000/child for a private high school. And Beverly Hills has 3000 units of 2BR+ multifamily residential.
In this segment, an even larger percentage of properties enjoys the 80% tax discount granted under Prop 13, leaving new property owners (irrespective of the age or tenancy of their renters) to pick up the tab. Unlike their entrenched competition – the 29% that are paying less than one-half, in real dollars, what they paid in 1975 – the new owners and their tenants are carrying, proportionately, the greatest load of all.

Looking at all these numbers, both commercial segments contain a sizeable group of property owners who are getting a longer, larger free ride than homeowners -- due to the longer-term nature of investment property ownership and to the ability of such owners to obscure changes in ownership. (Three-quarters of Beverly Hills commercial property and half of commercial residential is held in LLCs, partnerships, and corporate entities, which can easily mask or enable the transfer of control without triggering reassessment.) We can also see how the majority of commercial owners are suffering – not benefiting – from the tax subsidies enjoyed by their competition.

The Plot Thickens

But this isn’t, yet, the whole picture. Property owners who are getting an 80% discount on their taxes are only one of the entitled parties contributing to Beverly Hills’ unimpressive spending per pupil. How the collected taxes are distributed creates the second set of entitlements.
Before Prop 13 was passed, each underlying taxing entity – school districts, cities, counties, and special districts (fire, flood, mosquito, etc.) – levied separate taxes on homeowners. Different tax areas had different rates, all of which had to be shoehorned into Prop 13's mandatory 1% cap. The Legislature decided this would be proportional to the original underlying distribution. Thus, if one entity happened to have levied a large short-term tax, it benefited disproportionately. Similarly, an entity that raised funds in a different way might be cut out all together. (I have been told, but not been able to verify, that it was decided to cut back the schools' portion – with the understanding that the State would backfill accordingly.)

In the decade after Prop 13 passed, the proportion of taxes in Beverly Hills going to each entity finally settled, by 1991, into:

![Pie chart showing tax distribution](Image)

If something looks a little lopsided to you about this, take a look at my San Mateo County (Northern California) tax allocation:
Somehow, proportionately, ours may look a little more like you'd imagine – more to the schools, less to the county. Throughout California proportions differ substantially.

A new wrinkle was added in 1991, when the state of California was still backfilling both our school district and Beverly Hills’ – and, not surprisingly, struggling with its own budget crisis. Gov. Deukmajian instituted the first of the meat-cleaver take-backs designed to backfill the schools from county, city and special district budgets (“ERAF”).

After these take-backs, Beverly Hills looked like this:
While my area looked like this:

(One wrinkle is a Redevelopment Area in one part of our school district that siphons about 2% off the top here - mostly, when pass-thrus are netted back, from the schools. Beverly Hills has none, while many exist elsewhere in Los Angeles County and San Mateo County - pulling 10-15% of tax increment revenues to themselves, varying amounts of which flow back to the underlying entities via pass-thrus.)

Incidentally, Compton spends 18% on its local schools and contributes 20% to ERAF\textsuperscript{vii}, which, until 2004, it got back to it one way or the other. LA County as a whole spends 24% on local schools, county education and community colleges - with 24% going to ERAF.

In 2004, ERAF was re-purposed to cover losses to counties and cities from Governor Schwarzenegger's Vehicle License Fee Cut Initiative, and the Triple Flip that funded Economic Recovery Bonds. This left all of LA County's public schools dependent once again on the Sacramento spigot.

What do these fixed, meat-cleavered apportionments mean? Essentially that every local agency has had a fixed entitlement since 1978, with one great shift in 1991. Whatever amount of tax revenue comes in each year automatically flows to predestined uses. Voters who might have wished more to go to schools - or cities - or special districts (open space, lighting, etc.) - have had no say - unless, of course, they were willing to pass additional parcel taxes.
Special interests, meanwhile, have kept a very sharp eye on the California real estate market – knowing how it feeds a gush and sputter cycle of property taxes.

So what might we do?

What about fixing both imbalances at once? Putting allocation back in the hands of the voters, while limiting the ability of commercial landlords to extend their tax subsidies in perpetuity?

Some options:

(A) Granting commercial property owners no more than twenty years’ tax cap after a sale would rebalance the commercial and residential benefits from Prop 13. If a commercial or commercial residential property hadn’t gone through an arm’s-length transaction within two decades, it would be reassessed – then enjoy another 20 years of increasing tax subsidy. In addition to leveling the playing field for new and emerging businesses, the increased tax base would cushion the blow to those underlying tax agencies that voters choose to downsize. Imagine, every few years, being presented with the opportunity to rebalance allocation percentages, taking effect two years out.

(B) Reassigning all properties that still enjoy 35+-year-old bases to a Unitary Tax-like pool calculated by the BOE would be another alternative. It was recognized in 1978 that certain companies (primarily utilities) would have a perpetual life under Prop 13 – and that that was economically undesirable. It was also recognized that 35 years marked a turning point (long-term leases). Thus, at 35, it seems reasonable to bring long-term ownership of commercial properties back up to par, and to arrange a measured, but certain way of ensuring that they are contributing to the common weal.

Or maybe you can think of a better way of doing it – putting the power back in the hands of the citizenry to define a productive, well-balanced state? There is a multi-billion dollar pot of unproductive tax subsidies out there that can be used to lubricate a shift back towards local control.

TANGENTIAL THOUGHTS AND RESEARCH

Death and Taxes: Who’s Actually Benefiting From 1975 Bases on Commercial Property?

In Beverly Hills 143 commercial parcels enjoy a 1975 assessment year basis. Their assessments, climbing at 2% or less per year since then, are now 67% higher than they were in 1975 – while inflation has climbed 320%. Compared with nearby commercial properties that have sold in recent years, they are getting approximately an 80% tax
subsidy – i.e., the same civic services (fire, police, courts, roads, city, county, etc.) for about a fifth of the annual tax burden.

Who owns these parcels?

➢ Fifteen appear to be owned by corporations (Budget Rent a Car, Ford Motor Company, City National Bank, Phil Gersh Agency, etc.) of which about half are no longer actively registered in California.

➢ 21 are held by real-estate holding companies and 32 by limited liability companies and partnerships. (Who owns these is not apparent).

➢ 10 are held by individuals, estates or trusts – though a number of these people seem to have passed away a decades ago. It seems odd to see the names of Hugh Darling (the late mayor of Beverly Hills, d.1986) and his business partner William Ehni (d. 1974) laboring away as trustees of the 30,000 sf building at 9356 Santa Monica (Civic Center at Alpine)vi. And that Academy Award-winning screenwriter Sonya Levien Hovey’s ownership of 362 N. Camden hasn’t been wrapped up, 51 years after her deathvi. (The former bill goes to the trust department at Bank of America, the latter to Security Pacific. Who says death and taxes are inevitable?)

➢ 59 are held by family trusts of which at least ten, and probably the large majority, have been passed under Prop 58 (1986) to the heirs of the original property owners with no increase in basis.

➢ And six are held by miscellaneous owners ranging from the City (the Crate & Barrel/parking garage building on North Beverly) to the USPS to the Women’s Club.

But What About Prices Going Up and Jobs Being Lost?

A core tenet of economics is that the price is “what the market will bear.” When it isn’t, underpriced goods sell out immediately and overpriced goods languish on the shelf. Think about it: if costs determined price, a gallon of gas (including tax) would cost less than a dollar ... if any were left.

Favoring a fortunate minority of commercial property owners with an 80% tax subsidy has no benefit in lowering prices – it simply gives those owners more flexibility in picking and choosing tenants. Meanwhile, more recent entrants not only find themselves subsidizing their competition, but also shouldering the debt burden to acquire their property – and the dealing with faltering local court, police, school, city, and county services in improving and managing it.

The key effect of costs on business, according to economists, is determining whether that institution remains in business. Favoring that handful of entrenched businesses (and legion of entrenched landlords) that have the earliest tax bases discriminates against new or expanding businesses. (If this were a winning tax strategy, states would structure their corporate taxes accordingly. Think, for a moment, where Google, Facebook, eBay, Netflix, Genentech, Apple would have located if they were told that in California they’d
pay a 400% corporate tax premium for 10+ years over the companies that were already here. They’d locate elsewhere.

And, if we think that low property taxes somehow compensate for a weak business model, then it’s time to go test our theories around Beverly Hills. West Olympic Boulevard offers one set of immediate comparisons:

- The 8955 block between LaPeer and Almont has been owned by Ford Motor Company since 1954, entitling it to 1975 base assessments (the buildings all date to that era). Altogether, Ford’s general property tax bill is just under $14,000 for about 2/3 acre ($0.44 per sf).
- Immediately west of the Ford property, at 9001 West Olympic, is an identical parcel, purchased in 1997 by a real estate fund. Their tax bill, for a near-identical property, is just under $35,000 ($1.13 per sf).
- On the other side of the Ford property, at 8925 West Olympic, the .28 acre Ariaki parcel sold for land value in 2010, and pays just over $27,000 annually ($2.23 per sf) towards Beverly Hills’ police, fire, courts, roads, schools and other local services.

As you look at the three parcels, you might ask yourself whether forcing the new buyer to subsidize Ford’s ownership helps or hurts business in Beverly Hills. (Ford has not been located at that site for years.)

The only economic attempt to justify California’s wildly uneven property tax playing field for business (“The Economic Effects of Adopting a Split-Roll Property Tax,” Albero, Hamm – 2008) was predicated on three bizarre assumptions. First, it assumed that, if commercial property is valued on average at 60% of market, then every commercial property is valued at 60% of market. (By that argument, if the average person in the US is 30 years old, we are all 30 years old and the looming Medicare and Social Security crises are moot.) Second, it assumed that any tax savings were either passed on to the tenant (or through to the consumer) or reinvested in California property. Somehow, the authors seem unaware that landlords can easily just walk away – plowing tax savings into private schools for their kids or into vacations overseas. After all, why become a tax-disadvantaged newbie here, where other states play fair? Finally, the authors conclude that shortfalls in revenue create no loss in government or school employment – that California can just borrow to cover any shortfall.

I suggest a careful review of the actual beneficiaries of Prop 13 for commercial property would yield a radically different conclusion.

But Aren’t All The Kids Who Matter in Private Schools?

As a white, upper-middle-class native Californian, I’ve often been asked why, if I love my child, he isn’t in a private school. (Surely that would be a better use of my time and treasure than analyzing property tax!)
As a parent, the argument’s painful ... as a Californian, it’s worrisome.

Steve Jobs, Larry Ellison, Mark Zuckerberg, Sergei Brin, Jerry Yang – and a phenomenal proportion of California’s job-creating entrepreneurs – spent all or the majority of their time in public schools. Public schools develop an intuitive grasp of what business people will face in both the marketplace and workforce. A state whose graduates only know the handpicked upper-middle-class is a state that is hoping to import its success.

**But This is Beverly Hills! Is It Representative?**

Little hard data is available to the public on the distribution of Prop 13 benefits. However, the Los Angeles Assessors Office, in its Annual Report, shows 14.1% of Single-Family Residential property with a 1975 basis, a slightly larger amount of Residential Income (14.4%), and a larger proportion of Commercial-Industrial (17.1%)iii. While not as dramatic as Beverly Hills, a larger percentage of income-producing property owners still enjoy the highest property tax subsidies.

This is consistent with the only other county that annually publishes such data – Santa Clara’s 2011 Report shows 16% of single-family homes (paying 4% of their total), and 20% of commercial/industrial properties (paying 9% of their total) with a pre-1979 basisxiv.

These footnotes are all to help me quickly support references that I’ve made – but you may find them useful.

---

i June 28 Adopted Budget Report $50.3M revenue, $50.8M expend, 4257 estimated enrollment per Feb 22 budget meeting

ii [http://www.census.gov/govs/school/0933pub.pdf](http://www.census.gov/govs/school/0933pub.pdf), page 15


iv June 28 Adopted Budget Report; Mar 7 “Annual Establishment of Interdistrict Permit Cap”

v Average from spreadsheet of 2010 assessment to 1975 base value = 1.67; 1975 dollar in 2010 = $4.20, ratio of .398, even rounded up 11% for 02410 TRA tax rate of 1.109648, still well under 50%.


vii Modified ATI Ration Report from the Auditor-Controller LA County, 2010-11, page 3474, TRAs 9740 and 9741, averaged.

viii APN 4342-014-003

ix APN 4343-019-002

x APNs 4333-004-019 (acq 1947), -018 and -017 (acq 1954).

xi APN 4331-026-036

xii APN 4333-005-020
