Barriers to the use of property taxation in municipal finance\textsuperscript{1}

Abstract

Purpose The paper presents the findings from a series of case studies that examine the problems faced by countries seeking to introduce value-based recurrent property taxes to replace ones levied on the basis of area or inventory value. It identifies that two of the most significant barriers are the absence of comprehensive list of taxable properties and inadequate data on transaction prices. Both of these can be overcome with sufficient resources but this raises the question as to why governments are reluctant to do so in spite of the advantages of such a change.

Design/ methodology/ approach The paper makes particular use of case studies of Moldova, Poland, Serbia, and Turkey, which have explored the potential of introducing value-based recurrent property taxes, and the issues they have faced. The case studies have been produced by participant observers who have had the opportunity to examine developments over long periods of time. The case studies are set against a wider statistical analysis of the role of recurrent property taxes in tax systems.

Findings Putting in place comprehensive systems for registering properties and recording their characteristics and systematically collecting data on transaction prices require significant investment over a long period of time. This requires commitment on behalf of governments. Governments may be reluctant to support this because of the opposition such reforms can face unless confronted with compelling fiscal or external pressures to act.

Research limitations/ application The issues identified are ones that many countries seeking to introduce value-based recurrent property taxes will face and puts forward how they can be tackled. The case study countries are middle income ones with relatively well developed infrastructure, which low income countries may lack.

Practical implications The solutions to overcoming the barriers to value-based recurrent property taxes encountered in the case study countries are ones that are applicable to many other countries, who can learn from their experience.

Originality/ value The paper provides a perspective on overcoming the issues encountered in introducing value-based property taxes from the viewpoint of those who have been involved in working out ways of overcoming them and so provides insight that is a useful addition to the literature.

Key words Recurrent property taxes, value-based/ ad valorem taxes, Moldova, Poland, Serbia, Turkey

\textsuperscript{1} The views expressed here are those of the authors and not necessarily those of the institutions who employ them.

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Recurrent Property Taxes – the ubiquitous tax

The two words that can best describe recurrent or annual property taxes are ubiquitous and light. Recurrent property taxes are very widely used. Almy (2014), for instance, identified 166 countries with such taxes. To put this into context, the United Nations has 193 countries as members, so approximately, nearly 9 out of 10 countries have such a tax. In his compendium of property tax systems produced for the Lincoln Institute, Almy found 190 countries and territories out of the 225 surveyed has a recurrent tax on immovables (Almy, 2013). The reasons why recurrent property taxes are in wide use are not difficult to find. They fall on immovable assets and so are difficult to avoid. The tax base is a relatively simple one compared with taxes such as value added tax or corporate profits taxes. Levying them involves drawing up a list of the properties in an area and they are taxes that can be collected in situations in which governance is not well developed. They are widely used as local taxes to finance municipalities because the assets being taxed are immobile and there is no doubt as to the jurisdiction in which they are located. The ownership or use of a fixed asset indicates ability to pay and those who own or use these assets benefit from the provision of local services. Tax revenue does not leak across jurisdiction boundaries as happens with sales, income, or profits taxes.

Although widely used, the revenue raised through recurrent property taxes tends to be relatively low so that they can be argued to be a light tax. Figure 1 shows recurrent taxes on immovable property as a proportion of the Gross Domestic Product (GDP) in the countries of the Organisation for Economic Cooperation and Development (OECD). Although Canada and the UK raised 3.1 per cent of their GDP in the form of recurrent taxes on immovable property, the OECD average was only 1.1 per cent and 19 of the 35 countries raised less than the average. To elaborate on what this means, the UK in 2014 raised 8.4 per cent of the Gross Value Added less employee compensation in recurrent taxes on immovable property whereas 11 European Union member states raised less than one per cent (Grover et. al., 2017). The Gross Value Added less employee compensation can be taken as a proxy for the share of national income received by owners of land and capital. The gap between the countries that raise the highest levels of recurrent taxes on immovable property and the average tax take from this source indicates the potential for raising revenue that most countries forgo.

Insert Figure 1 here

The countries which are not members of the OECD, which for the most part are lower income countries, tend to raise little revenue from recurrent property taxes. Figure 2 uses OECD data to show the percentage of GDP raised using recurrent property taxes on immovable property for selected non-member countries. Although some like Singapore have income levels comparable with those of OECD countries, most have much lower incomes per capita. Out of the 41 countries for which the OECD has collected data, only four reached the OECD average percentage of GDP raised from recurrent taxes on immovable property. An IMF study of 30 middle and low income countries similarly found that only one country raised a higher proportion of its GDP in recurrent taxes on immovable property than the OECD average (Norregaard, 2013). A survey of property taxes in Africa identified only three
countries which exceeded the OECD average of recurrent property tax revenue to GDP, with the average being 0.38 per cent and the tax being almost negligible in Francophone Africa. However, in metropolitan cities it was a major source of revenue and they accounted for a significant proportion of the revenue raised in this way in their countries (McCluskey et.al., 2017). These figures suggest that the untapped potential from raising additional revenue using recurrent property taxes is even greater amongst lower and middle income countries than amongst OECD members.

Insert Figure 2 here

An intellectual case can be made for greater use of recurrent property taxes. Their use reduces reliance on consumption taxes that bear particularly heavily on low income groups, and taxes on income, employment, and profits that can distort investment, reduce incentives for employment and enterprise, and alter the balance between work and leisure and savings and consumption (Grover and Walacik, 2018). They tax accumulated wealth rather than income and so have less of an impact on future behaviour (Norregaard, 2013). They encourage the productive use of land and discourage land hoarding (Malme and Youngman, 2001). By targeting immovable assets, they are amongst the taxes least affected by globalisation and the internationalisation of supply chains (Johansson, et.al, 2008).

The light use made of recurrent property taxes has fiscal consequences. Local governments can become more dependent on the use of inter-governmental fiscal transfers in the form of grants from central government or tax sharing arrangements for national taxes rather than fully exploiting their own tax resources. One can readily see how it may appeal to local politicians to have a greater share of the cost of local services met by central government rather than taxing their own citizens and to be able to blame central government for funding shortcomings. This becomes problematic if the central government itself is under pressure because of unsustainable levels of debt or current budget deficits, which could be reduced by greater use of recurrent property taxes. For instance, the Second Economic Adjustment Programme for Greece agreed with the European Union in 2012, involved increasing the property tax and simplifying its rate structure (EU, 2012).

If effective recurrent property taxes are not available, there is the danger that local governments will resort to other means of raising finance that may be damaging, particularly to business. For instance, in Serbia there were 15 communal fees, including ones on business signage until their abolition in 2012 (Rašković et. al, 2016). In Serbia (until its abolition in 2014) and Slovenia businesses have paid an urban land use charge for buildings on land retained in public ownership when the businesses themselves were privatised (Žibrik, 2016). In Serbia the annual property tax is only the third most important source of revenue for local governments after their share of income tax and fiscal transfers from central government. The annual property tax contributed 14.3 percent of current local government revenue in 2015. This masks considerable variations with the average proportion being 9.6 per cent but with a range from 0.4 per cent in Trgovište to 22.8 per cent in Svilajnac (Vasiljević, 2017).
Ways of raising local revenue can include pseudo property taxes in the form of developer exactions or value capture devices payable in return for development consent or access to infrastructure, for which the actual charges may bear little relationship to real costs. Poor performance in collecting taxes can result in these instruments being seen as a pragmatic substitute for other taxes. In Latin America developers commonly hand over 15 to 35 per cent of the land (Smolka, 2013). In Serbia there are different rates for development fees charged for access to infrastructure based on the cost of construction, the use of the property, and the zone in which it is located (Rašković et. al., 2016). These are often higher in city centres, where infrastructure is already in place, than greenfield sites, where the costs of connection can be expected to be greater. Local government bodies advocate their use as value capture devices (Žerjav, 2013), a suspicion that is strengthened by the fact that the development fee forms a significant part of the incomes of many municipalities, particularly in the larger urban areas. For low income countries the problem of low revenues from recurrent property taxes is likely to mean problems with actually providing local services, such as education, healthcare, clean water, roads, and sewage.

The light use of recurrent property taxes is reflected in the role that they play in the tax system. Figure 3 shows that on average for OECD countries, recurrent taxes on immovable property generated just 3.4 per cent of tax revenues, though for the leading countries this was 9.6 per cent. Similarly, in only six of the non-OECD countries shown in Figure 4 did the receipts from recurrent taxes on immovable property reach the OECD average contribution to tax revenues.

The central question is why are recurrent taxes on immovable property so lightly used in many countries and generate relatively little revenue in spite of the ubiquitous nature of the tax and the arguments in favour of levying it. This would suggest that there are impediments in the way of greater usage of this type of tax. The methodology employed in this article is to explore the impediments using case studies of Moldova, Poland, Serbia, and Turkey, countries that have in recent years sought to reform their systems of recurrent taxes on immovable property and the issues that have been encountered in doing so. The case studies have been produced by participant observers either working for the implementing agencies or funding bodies or as valuers, and draw on a variety of sources, including the analyses of laws and regulations, statistical analysis, and interviews with stakeholders.

Recurrent Property Taxes – the problem

Taxes can be levied using two main bases – by value (ad valorem taxes) or on a specific basis, such as by volume, weight, or size. Recurrent property taxes can be levied on the values of the properties, using evidence derived from market prices, or as specific taxes such
as according to the size of the property. In reality, the latter can be modified by applying coefficients to the rate per unit to reflect factors that influence the market price, such as the form of construction or the zone in which the property is located. However, such modifications mean that the assessment is not based on market prices even though the coefficients may reflect factors that can play a role in influencing value. These modifications are likely to mean that there can still be substantial variations in value even within a class of property that is subject to the same coefficients. The sizes of the classes used generally result in mixed collectives with each class containing properties that significantly diverge in value.

Moldova provides an interesting contrast between the two approaches. In 2000 the parliament approved a tax code which introduced value-based assessments (Buzu, 2016). Mass valuation was launched in 2004 with the intention that all properties would be valued between 2004 and 2008. The plan was for an additional class of property to be added to the system each year and that the new value-based assessment system would be implemented in stages. Between 2004 and 2011 assessments were undertaken for residential properties in urban areas, garages, commercial and industrial properties, and agricultural land with structures on it, the new tax system being implemented in stages over the period 2007 to 2012. However, only 12.5 per cent of properties were brought into the system as value-based assessments were not carried out on agricultural land, rural housing, or special purpose properties, such as power plants, railways stations, and airports. They continued to be assessed under the former system. Agricultural land is assessed at a flat rate per hectare with an adjustment for the fertility of cropland using a bonity system that places land into broad categories. Pastures and hayfields are assessed at a flat rate. Rural housing is assessed on its historic replacement cost adjusted for depreciation. The migration of the remaining properties to the mass valuation system has been delayed as funds were not made available by the government for completing property registrations and assessments. The result is a dual system with urban areas and industrial and commercial properties in rural areas having been assessed on their market values whilst agricultural land is assessed on its area and rural housing and special purpose properties on their inventory values. Moreover, the periodic revaluations of the properties in the mass valuation system have not been undertaken so that assessments no longer reflect current market values.

In Poland the way in which the recurrent property tax is assessed is determined by the type of object (Walacik, 2016). For land the assessment is based on the area recorded in the cadastre. In the case of agricultural land, it is adjusted for the type and class of land. For buildings, assessment is based on the usable area. Work on reforming the tax system has been going on since 1990, with large numbers of changes being made to the basic legislation, but without bringing about a fundamental change to a value-based system. In 1994 the Council of Ministers required the Ministry of Finance to determine the value of properties for tax purposes. In 1998 the Ministry of Finance created a Department of Local Taxes and Cadastre to prepare and implement property tax reform. A thorough reform of property taxation was also proposed in 2012. Although a system for mass valuation and the legislation for it are in place, the detailed guidelines have not been developed nor how the costs are to be met determined.
By contrast, in Serbia the recurrent property tax is, in principle, based on market values. Taxpayers are divided into two groups. For those that keep records (such as corporate bodies), assessment was based on the book value of properties, but since 2013 local governments have been expected to use fair values (Rašković et al., 2016). For other taxpayers, which include unincorporated business and households, the average sales price per square metre as at 31 December of the proceeding year for the zone in which they are located is taken and applied to the usable area. The principal problem is one of capacity. Responsibility for the annual property tax was transferred from central to local governments in 2007-09 though without the resources to support it. There are 168 local authorities serving a population of approximately seven million people, many of which are too small to reap the benefits from economies of scale. As is discussed below, the cadastre does not accurately record all properties, so that local governments cannot rely on a central source from which to derive comprehensive tax rolls and the zones can be of such a size that there may be significant variations in value within them.

The annual property tax in Turkey has two parts, a buildings tax and an urban and rural land tax. Although assessed by local governments, the valuation methods are determined by central government. Taxpayers provide municipalities with information about their properties. Building valuations are calculated using a depreciated replacement method. Although construction costs are determined each year by the Ministries of Finance and Urbanization and Environment, the depreciation rates were set in 1982. Land values are determined by valuation commissions that take into account factors that should influence the values of streets and main roads. Until recently, there was no requirement for licensed valuers to be on valuation commissions. Pilot studies in the Fatih district of Istanbul and the Mamak district of Ankara undertaken in 2013-14 indicated that the annual property tax assessments would need to be 2.94 and 1.88 times higher respectively for these to reflect market values (Güneş and Yildiz, 2016).

The problem with area-based property tax assessments or ones based on something like the inventory value, replacement cost, or an average value in a zone or use type that covers a wide group of properties is that governments do not know what the effective tax rate is on any individual property. For instance, large low-value properties can be taxed more highly than smaller but more valuable ones. The effective rate at which the tax is applied is likely to vary within the groups to which properties are assigned. Taxes levied on this basis can be argued to be inequitable and are unlikely to reflect ability to pay. Those taxpayers in possession of more valuable properties, who have the ability to pay more in tax, are not identified as properties are not classified by value. They are likely to be in the same tax group as properties whose unit value is much lower. In such circumstances, tax rates have to be set at levels that are affordable by all. Even though effective tax rates vary between taxpayers, those in possession of low value properties can still pay the tax. But the result is that tax revenues could be increased if recurrent property taxes were value-based are foregone and tax yields are depressed.
If recurrent property taxes are not to be lightly used but to make a more significant contribution to tax revenues, then governments need to levy them based on current values of properties so that they can reflect ability to pay. Such an approach is also more equitable since taxpayers can be charged the same effective tax rate as their peers. If governments are to levy recurrent property taxes on a value basis, there are some formidable obstacles that have to be overcome. It requires governments to move away from assessments based on mixed collectives containing properties of different values and to move either to individual valuations based on market value or the clustering of properties that are of similar value. This requires greater knowledge by governments about the market values of properties and how to apply them to the majority of properties for which there have been no recent transactions to derive tax assessments.

In each of the four countries examined, there is recognition that the current situation is unsatisfactory. Moldova has recently taken out a World Bank loan to improve its land registration and cadastre. This will also finance the extension of its mass valuation system to those properties not currently included and the revaluation of the properties currently within the mass valuation system (World Bank, 2018). Both Serbia and Turkey are engaged in land registration and cadastre improvement projects using World Bank loans that have components on property valuation and taxation. Evidence from these countries and others in the Europe and Central Asian Region of the World Bank that have engaged in property tax reforms indicate that there are a number of problems that have to be resolved as preconditions for successful programmes. First and foremost, there must be a political willingness to reform the current system and momentum to introduce value-based property taxation. There are also various technical issues that have to be resolved. The cost of overcoming them and the time this takes should not be underestimated, and these can be a test of political resolve. Governments are likely also to have to overcome opposition from taxpayers and within government before the resources and sustained commitment needed can be realised.

**Barriers to recurrent property tax reforms:** (1) The lack of comprehensive land records

Taxes on immovable assets ought to be difficult to avoid. Immovable assets are by their nature almost impossible to conceal. The problem is that such assets may not be recorded and recurrent property taxes require there to be a comprehensive and accurate list of properties. This implies that there is a cadastre, in which properties are listed, and a register of property ownership recording transactions so that taxpayers can be identified. As Slack and Bird (2014) have noted, the effectiveness of recurrent property taxes depends on the quality of land administration. Informal construction undermines the accuracy of the cadastre, which may not record what actually exists on the ground, and informal transactions mean that the land registry may not be an accurate record of land ownership.

Serbia has a history of informal land markets and construction. During the socialist period, approximately 75 percent of agricultural land was part of private family farms and land transactions were mainly conducted informally. During the 1970s there was rapid urbanisation resulting in unplanned and illegal developments. Violent conflicts in the former Yugoslavia during the 1990s resulted in almost half a million refugees and internally displaced persons...
having to be housed, often through informal development. Property rights were often not registered because of obsolete land books and a dual system in which land registration was the responsibility of the courts and the cadastre was maintained by the Republic Geodetic Authority (RGZ). Only since 2012 has there been a unified system operated by RGZ for the whole country (Rašković et al., 2016). Investigations by municipalities in 2015-16 into objects that were not legally constructed and/or registered as part of legalisation procedures uncovered over 2 million informal objects (Republic of Serbia, Ministry of Construction, Transport and Infrastructure, 2017). More recent estimates have suggested that the number of informal objects may be as high as 5 million (http://www.rgz.gov.rs/vesti/2865/vest/blic-o-broju-objekata-koji-nisu-upisani-u-katastar-nepokretnosti). These reinforce findings from earlier studies. In 2012 a study by GIZ reported that 37 per cent of municipalities estimated that the level of unregistered properties in their jurisdictions was between 20 and 40 per cent (Arsić et al., 2012) and comparisons between databases in Arandelovac and Indija found significant numbers of properties receiving utilities, such as electricity, but not paying the annual property tax (Rašković et al., 2016). As utilities are supplied by companies and not municipalities, they have separate billing systems from those used in property taxation. Properties which have not been formally registered or for which all the procedures for securing building approval have not been followed have in the past been able to obtain utility connections and obtain supplies of services like electricity and water for which they have been billed.

In response to this problem RGZ, over the period 2017-18, extracted buildings from satellite images to create a Buildings Register that includes all taxable objects, whether legally constructed or registered or not. The process of legalising informal developments is a complex and time-consuming one so that this was deemed to be a more efficient approach than updating the cadastre. In effect, a fiscal cadastre has been created. Statistics from satellite images indicate that there are about 5 per cent of registered buildings that need to be removed from the cadastral records as they do not exist. The number of unrecorded buildings varies according to the type of settlement and economic development of the area but pilot studies found that there were roughly an equal number of unrecorded buildings as those actually recorded in the cadastre (Republic Geodetic Authority, 2017-18). Work has also been underway to digitise paper documents containing information about buildings collected during field inspections by local governments as part of legalisation procedures and to create a Condominium Register following legislation in 2016 requiring these to be registered (Rašković et al., 2018). This work should result in a comprehensive record of taxable objects together with their addresses. As RGZ is responsible for maintaining the addresses register, each object will have a unique identifier which can be used in a wide range of databases. The Government of Serbia has decided to create central system for recurrent property tax. It is a task for the Office for IT and eGovernment.

Turkey, like Serbia, has undergone rapid urbanisation with the average compound rate of urbanisation over the three decades starting in the 1980s being over 4 per cent. A permissive tenure regime granted squatters on urban public land legal status. Many cities were unable to accommodate the growth in their populations, and it is estimated that between 30-60 per cent
of all urban housing stock was informal. Between 1949 and 1990 there were eight amnesties legalising informal housing (World Bank, 2014). The latest regulation in this field was made with the Temporary Article Number 16 being added to the Zoning Law on May 11, 2018. It is foreseen that at around 13 million immovable properties will be legalised with this amendment. The application deadline has been set as the end of October 2018. The Turkish Government is expecting to raise 40 billion Turkish Liras (6.5 billion USD) of income with this measure. Similarly, the response to incursions on to degraded forest lands has been to sell them to the occupiers, usually farmers from neighbouring villages, thereby legalising the trespass. It is not clear that the system for recording properties has kept pace with urbanisation and Turkey is known to have an issue with illegal densification in which buildings are replaced by larger ones and extra storeys added to permitted developments. There has, though, not been the same systematic study of the extent to which properties are accurately recorded in the land registry and cadastre that there has been in Serbia. There is though some anecdotal evidence. The Mayor of Altindag in Ankara has reported how he was able to boost tax revenues and increase municipal expenditure by targeting illegal constructions to the extent that his municipality has even had funds to spend on services that are not officially its responsibility, such as the construction of schools. Even if the information is recorded accurately, it may not be useable unless the data models are consistent. In Turkey, TKGM (the cadastre and land registry agency) is responsible for the Land Registry and Cadastre Information System (TAKBIS) and the Spatial Property System (MEGSIS). These official records have a lack of data standardisation so that reliable information is difficult to obtain. Some data fields have been structured in text format in which users are able to choose what to write and others cannot be classified systematically because of legislative issues. “Data is not hidden, but remains a mystery” (Yildiz and Güneş, 2018).

In Moldova the completion of the mass valuation system has been held up by initial first registration being incomplete or inaccurate. Approximately 85 per cent of private lands have been registered but the extension of the mass valuation to include rural properties requires the completion of the system of initial registrations, an aspect of which is the collection of data about each property. Past registrations were not always undertaken accurately resulting in errors in the form of registered titles with graphical parts that have not been defined spatially, overlapping registered parcels or buildings so that boundaries are ambiguous, and titles with no corresponding graphical part. Public lands in the ownership of the state and local governments account for 45 per cent of the land area but only 7 per cent of this is currently registered. Of the estimated 1.1 million unregistered parcels, 325,000 are in the public sector (World Bank, 2018). These parcels need to be delineated as they include lands, such as pastures, which abut on to private lands. The completion of the first registrations is budgeted to cost 15.3 million euro.

In Poland the issues with property information systems have been less to do with the completeness of the records and more to do with records not being unified or accessible electronically. The property right registers are kept by district courts. The cadastre is maintained by starosts (district councils) and provides entry into the land and mortgage
registers and, therefore, the physical characteristics of the property. It should not matter for property taxation purposes whether there are different bodies maintaining the various registers providing that the principle of the EU’s Inspire Directive are met so that users are able to access them electronically for their own purposes. Work on computerising court registers began in 1995. Since 2010 the land and mortgage registers have been accessible via the Ministry of Justice’s website. Entries into the paper books have been discontinued but the migration of the books into electronic databases has not been completed. Access to data in the cadastre is through paper systems and the information in it is not linked to the register. It is anticipated that by 2020 the Construction of an Integrated Real Estate System (ZSIN) will be operational so that there will be a central repository of cadastre data sets and exchanges of data between the cadastre and the property registers (Grover and Walacik, 2018).

**Barriers to recurrent property tax reforms: (2) Availability of transaction price data**

Value-based recurrent property taxes can only be implemented if there is evidence of transaction prices. Depending on the tax base – whether it is the annual or capital value – and how the market operates – whether access to property is by purchasing or renting it – information is needed about sales prices, rentals, and yields. Value-based property taxes take the transaction prices for those properties that have changed hands during a given time period and use them to estimate the market prices of comparable properties. This is typically done using mass valuation systems in which statistical models are derived which identify the principal characteristics that determine price and their influence on it. Where governments require purchase prices to be declared when transactions are registered, the registry is an obvious source of transaction price data. Similarly, if there is a property transfer tax, then declarations made by those buying and selling property should provide a database of property prices. If transactions have to be completed through notaries, then they should have knowledge of transaction prices since these determine their fees. Data from property title searches about properties should be shared.

One of the main factors to undermine transparency in property markets is the cost of transactions. The costs include financial ones such as registration fees and property transactions taxes, but also include the time and difficulty involved in registering transaction, particularly if multiple agencies are involved, there are complex data requirements that owners must satisfy, or there are a large number of stages to the process. Under the influence of the World Bank’s Doing Business league tables, one of the areas of which is registering a property transaction, there is pressure on governments to simplify and reduce the number of procedures and to lower costs, or else be “named and shamed” over their performance. However, for countries seeking to adopt value-based property taxes there can still be issues to overcome, particularly about the accuracy of the data collected.
In Turkey the mass valuation pilot studies undertaken in Fatih and Mumak identified that the transaction prices declared should be 2.5 and 2.1 times greater respectively than those actually declared (Güneş and Yildiz, 2016). Because it was suspected that transaction prices were under-reported, the mass valuation models made use of mortgage valuations rather than declared prices. Mortgage valuations can only be undertaken by licensed valuers, who are members of the Association of Appraisal Experts of Turkey (TDUB – Türkiye Değerleme Uzmanları Birliği), a professional organisation authorised by the Capital Markets Board (CMB). The CMB has adopted International Valuation Standards as the basis for the valuations it regulates and TDUB can discipline members who breach valuation standards. Property transactions in Turkey are subject to a land registration fee of four per cent of the transaction price. Some buyers and sellers appear to evade this by declaring lower values, often based on the tax value, which, as the pilot studies showed, is only a fraction of the market price. This is more difficult where the purchase is financed by a mortgage as the mortgage charge must also be registered. Approximately 22 per cent of sales are financed using mortgages, but this varies within the country from 45 per cent in metropolitan cities to 15 per cent in some smaller ones. When multiple sales of a property take place over a short period of time, the declared price can fluctuate markedly according to whether a mortgage has been taken out or not (Yildiz and Güneş, 2018). Reducing the rate at which land registration fees are levied could improve the quality of data by making their evasion less worthwhile, particularly if this was to be accompanied by stronger enforcement action in challenging declarations that look to be unrealistic. The pilot studies suggest that a lower rate applied to true transaction prices is capable of generating a similar level of income to the present fee structure. Policymakers are understandably reluctant to undertake such a radical move in case fee income declines if there is no Laffer curve effect in which lower rates boost activity and revenue. An alternative that has been proposed is to develop an on-line valuation databank for tax valuations using the valuations produced by TDUB members as a proxy for transaction prices.

Moldova has similarly experienced issues with obtaining accurate transaction price data. It has been estimated that as many as 90 per cent of the property sales contracts understate the true prices (Buzu, 2016). This is surprising given that notaries’ fees are calculated as a percentage of sales prices (0.1 per cent) but interviews with notaries indicate that they are reluctant to challenge the information they are given. The property transfer tax is only 0.5 per cent. The reason for the inaccuracy though would appear to be the way in which the capital gains tax functioned. This was levied at 12 per cent of the taxable difference between the declared price and the tax valuation, (which is 20 per cent of the entire difference between the declared price and appraised tax value), encouraging buyers and sellers to declare the purchase price to have been at the tax value. Tax values were mainly produced between 2004 and 2009. Proposals to change this so that residential properties are exempt from capital gains tax unless sold within five years should mitigate the problem for this class of property. Growth in the mortgage market should result in more accurate information, though this may be undermined by proposed changes in the regulation of valuers. Companies must employ valuers who have been licensed by the Agency for Land Relations and
Cadastre (ALRC). ALRC set standards, accredited university programmes that valuers must take as initial entry qualifications, required would-be valuers to gain appropriate supervised experience in practice, tested them on their competence, and disciplined those who breached standards. A new law will abolish the role of ALRC. Instead valuers will only be required to gain an initial qualification from an accredited certification body and renew this every five years. MOLDAC, the Moldovan accreditation body, will accredit these certification bodies. In the absence of more reliable information, the mass valuation system made use of proxies including asking prices, information from realtors and valuers, and prices achieved at auctions.

For Serbia the problems with obtaining reliable price information have been more procedural than about accuracy. There is a property transfer tax levied at a rate of 2.5 per cent of the market price or the contract price, whichever is the higher. The Tax Authority uses statistical techniques to identify what it considers to be declarations that are below the market price and has a robust attitude towards collecting what it considers to be the appropriate level of tax. Buyers are usually responsible for paying the transfer tax and there is a 15 per cent capital gains tax on the difference between the disposal and acquisition values, so buyers have no incentive to collude in under-declarations. Until a licensed valuer system was introduced in 2016 under pressure from the International Monetary Fund (IMF), mortgage valuations were undertaken by court experts appointed by the Ministry of Justice. They were experts in construction but did not necessarily have valuation qualifications. Unlike Turkey, mortgage valuations would not have been a useful proxy for market prices. The new system introduced valuation standards aligned with International and European Valuation Standards, accredited training bodies, and a rigorous examination system. The first examinations under this system were held in January 2018, in which a pass rate of 14 per cent was achieved, indicating that in the past, valuations may not always have been reliable proxies of market prices.

Buyers and sellers of property submit information about the transaction to three bodies: notaries who authorise the contract and register it with the Ministry of Justice, the Tax Authority, which collects the property transfer tax, and RGZ, which registers the transfer. Before the creation of notaries, contracts were registered with local courts. The problem has been that the various databases have not been able to communicate with each other. A National Spatial Data Infrastructure law is expected to be promulgated which will embody the EU Inspire Directive principles. Two approaches have been adopted to resolving the problem. RGZ developed a Sales Price Register in 2012, which extracted data from sales contracts and manually entered them into a database. Initially the contracts came from local courts but since 2014, have come from notaries. From 2014 market reports have been published. The public have access to certain data from the Sales Price Register - the approximate location of the sale, price, purchase date, real estate type, area, and transaction type (such as sale or transfer between relatives). Professionals (mainly banks, valuers, and realtors) have access to more detailed data, such as precise location (parcel number, street and street number), number of floors for buildings or floor of an apartment, number of rooms, and if encumbrances exist (Rašković et. al., 2018). Interviews indicate that professionals have welcomed the information that the Sales Price Register provides and it appears to have
improved market transparency. The manual entry system was not a sustainable approach in the long run and runs counter to the philosophy of having a “one-stop shop” in which those engaged in property transactions can supply the necessary information once with it being supplied electronically to the various agencies that require it. Work is underway to develop means of communications through databases with the relevant data about properties needed for mass valuation being collected at the property contract stage. Contracts are sent by the notary system to eFrontDesk developed by RGZ and thence to the Sales Price Register and the Real Estate Cadastre, and are available for the Tax Authority.

Securing comprehensive and accurate lists of properties and their characteristics and good quality information about transaction prices is an immense undertaking that requires significant upfront investment. This is before work is undertaken on modelling values, using the models to generate assessments, and billing taxpayers. It may be argued that once the system is established there are economies of scale so that administrative costs are low as a percentage of the tax yield and the costs of valuation per property are modest. In Moldova the costs per valuation were €0.36 per apartment in 2004 and €1.4 per residential block in 2005 (Buzu, 2016). This compares with €17 per assessment in 2014 in the Netherlands (Kuijper and Kathmann, 2016), the Dutch costs probably reflecting higher labour costs than in Moldova. Implicit in the development of value-based recurrent taxes is the assumption that the tax rate will be set at a level that makes the investment in the system worthwhile. Collection systems may also have to be improved so that rates of default and the costs of collection are minimised. All of which implies that there needs to be significant political support behind the move to value-based recurrent property taxes and the administrative effort needed to achieve a successful outcome, and to ensure that resources are made available for completion of the tasks.

Some countries have successfully made the transition to a value-based recurrent property tax from an area-based system of which Lithuania is a notable example (Almy, 2016). Others, though, have encountered problems. In Slovenia, a well-designed value-based property tax system has not been implemented as it was ruled in 2014 to be unconstitutional (Žibrik, 2016). In Moldova the move from area-based to value-based property taxation ran out of traction so that the reforms were not applied to most rural properties. The issue was that the costs of extending the system would fall primarily on central government, particularly that of completing initial registrations of rural properties, whereas the benefits from enhanced revenue would be reaped by local governments (Buzu, 2016). The government under financial pressure had limited resources available. Policymakers appeared at that time not to recognise the link between local government finances and those of the government as a whole and therefore the desirability of investing in enhancing revenue from recurrent property taxation. The decision in 2018 to enter into a World Bank loan to complete initial land registration and improve the cadastre and to extend the mass valuation system should bring about the completion of the transition from area-based to value-based property taxation.

Poland’s journey started in 1993 but there are no signs of a value-based recurrent property tax being implemented any time soon (Walacik, 2016). In 2008 Turkey borrowed 135 million euro from the World Bank for a land registry and cadastre modernisation project, which
included 4.96 million euro for a property valuation component (World Bank, 2008). This resulted in mass valuation pilot studies in two municipalities and the development of policy proposals (Güneş, and Yildiz, 2016). There has been limited progress towards value-based property taxation since the conclusion of this loan but in September 2018, the Ministry of Finance published a New Economic Program for the period 2019-21. The policies include reorganising the tax system “so as to introduce a real estate appraisal system….. and charge title deed fees and property taxes based on real values of properties” (Republic of Turkey, 2018). As was noted above, legislation in Serbia supports the use of value-based property taxation but the responsibility for implementation lies with local governments, which had received relatively little support from central government. However, In 2015 Serbia borrowed 32.6 million euro from the World Bank for a Real Estate Management Project of which 6.6 million euro is for a valuation and property taxation component primarily to develop a sales price register, undertake mass valuation pilot studies, and establish a buildings register (World Bank, 2015). Work to realise these objectives is now underway, including a proposed mass valuation law that will enable the Ministry of Finance to connect all the participants in the process.

These experiences raise the question as to why governments seem to be so reluctant to support the development of value-based recurrent property taxes in spite of the case in favour of doing so. It is true that there are significant costs, particularly for putting in place the initial infrastructure, but soft loans from bodies like the World Bank and bilateral donor aid is often available providing that it is possible to demonstrate that the financial benefits outweigh the costs. Several reasons can be put forward. The support of ministries of finance is needed as they are ultimately responsible for taxation policy and determine whether loans from bodies like the World Bank or commitments to bilateral donors can be entered into. Policymakers do not necessarily take a whole of government approach to public revenues and expenditure and so may not appreciate that what happens in one part of the public sector has repercussions on others. Thus, the impact on intergovernmental fiscal transfers from the inability of local governments to maximise their own revenues is not always appreciated. Ministries of finance can find themselves out of their comfort zones when dealing with property taxation. It involves what is for many policymakers an alien world of property valuations, land registers and cadastres. Exploiting the potential of value-based property taxes runs counter to the prevailing philosophy of “one-stop shops” in which taxpayers, particularly companies, can deal with a single point of contact for the range of taxes they have to pay rather than separate agencies (Grover et. al, 2017). The particular technical demands of recurrent property taxes mean that they are likely to require different institutions for their assessment and collection than other taxes.

Governments are likely to be wary of the political consequences of making changes to the ways in which recurrent property taxes are levied. Monkam and Moore (2015) have argued that they are neglected because they are highly visible and unavoidable. Their intrusive nature is not calculated to make them popular even though they raise much less revenue than many taxes, such as consumption taxes, that can be imposed more stealthily. The use of property values as the base will inevitably increase the tax burden on some taxpayers. They are likely
to be vocal and active in their opposition whereas the beneficiaries may well be inarticulate and disorganised. Cases where change has commanded support have tended to be where additional income has been generated in a relatively painless manner. This enables public support to be garnered through increased expenditure on popular items and by providing more generous relief to some taxpayers particularly adversely affected by the change. These include asset-rich cash-poor groups, such as pensioner households. In transition economies the privatisation of housing resulted in some households gaining ownership of properties they would never have been able to have bought. As owner occupied housing is not an income generating asset, this can present problems for those with low incomes residing in valuable properties bought in the past, when their incomes were higher, or the-acquired as a result of restitution, privatisation, or encroachment amnesties. If there are significant numbers of properties that had previously escaped taxation through not being registered, something that is likely if there has been rapid urbanisation, then the potential for raising greater revenue whilst at the same time reducing tax rates, increasing public expenditure, and applying more generous reliefs exists. Where this is not possible, consideration needs to be given to implementing change first for industrial and commercial property and, only when the benefits from increased tax revenue feed through into public expenditure, should the new approach to property taxation be applied to residential property occupied by voters. This raises technical issues since mass valuation can generally applied more readily to residential properties because of the higher numbers of transactions and availability of price data. For industrial and commercial properties, it may be necessary to use income-based valuation models rather than those using comparable sales prices. As shorter leases are generally not registered, securing rental and yield data is likely to be more of a challenge than for sales prices of residential properties.

External events can make feasible policies that previously seemed impossible to bring about. Although Serbia’s national debt has fallen from its peak of 74 per cent of GDP in 2016 and there was a budgetary surplus in 2017, previous debt levels were regarded as being unsustainable. As the World Bank noted, “The global financial crisis exposed the structural weaknesses in Serbia’s economic growth model and prompted the need for fiscal consolidation and an acceleration of the unfinished transition to a market economy” (https://www.worldbank.org/en/country/serbia/overview#). In 2014 $1 billion was siphoned out of three of Moldova’s largest banks, Unibank, Banca de Economii, and Banca Sociala, leading to a bail-out that absorbed half of the government’s annual budget (Monahov and Jobert, 2017). The Turkish economy has proved to be vulnerable to external events, particularly increases in US interest rates. The exchange rate for the lira fell by 38 percent in the first nine months of 2018 and the central bank increased its interest rate from 8 per cent to 24 per cent. These provide the backdrop to the New Economic Program published in September 2018. These examples all point to governments being willing to accept pain from tax reforms if the economic circumstances and related external pressures require it.

Conclusions
Recurrent property taxes are widely used with most countries in the world having them. However, they are lightly used raising relatively little revenue either as a percentage of GDP
or total tax revenue in each country. There is a significant gap between the revenues raised by
the countries that make most extensive use of them and that of typical countries. This
difference points to the untapped potential from recurrent property taxes. This matters
because of the role that such taxes play in a tax system. By falling on immovable assets, they
are appropriate for use as local taxes but it also makes them relatively immune from impact
globalisation has had in particular on company taxes. They are relatively neutral and by
falling in wealth, can help to reduce the impact of taxes on consumption, income, and
employment.

The relatively light use of recurrent property taxes seems to reflect the tax base used in many
countries. Rather than being levied on the market values of properties, they often tax by area
or inventory or cadastral value. The tax rates may be moderated according to factors such as
location or construction type but the overall result is that properties that differ widely in value
are placed in the same tax band. Governments respond to not knowing what the effective tax
rate is on any individual property by setting low rates that are affordable by all taxpayers,
thereby forgoing the tax revenue that some property owners could afford to pay. If recurrent
property taxes are to generate higher revenues then they must be levied on the basis of market
values.

There are some significant barriers that governments must overcome to do this. They need to
have comprehensive tax rolls that identify all the properties that should be taxed and their
characteristics. This is a particular challenge in countries where there has been rapid
urbanisation or significant levels of informal development or transactions. Governments need
to draw up fiscal cadastres and this often requires the creation comprehensive cadastres and
land registers. Fiscal cadastres usually contain more comprehensive information
about properties than general cadastres, which may be limited to data about parcel
boundaries and land uses. As has been shown in Serbia with the use of satellite imagery,
it is necessary to collect accurate data about buildings. Information also has to be
collected about the characteristics of the buildings. This may be possible through data
collected from buyers and sellers when property is transferred but may also require surveys to
be undertaken to establish the initial fiscal cadastre. Reporting structures so that the
property tax administrators can learn from spatial planning and building control
authorities what changes are made to buildings help to ensure the currency of the fiscal
cadastre.

Governments also need to access good information about transaction prices so that data about
those properties for which there have been recent transactions can be used to
value comparable properties. Significant investment may be required to establish systems
such as sales price registers which generate comprehensive information about transaction
prices. This may require governments to tackle under-reporting of transaction
prices during property transactions to evade fees or taxes and to prevent due to
informal transactions or tax or fee evasion. High levels of transfer taxes or fees
provide an incentive for under-reporting real transaction prices whereas carefully
structured capital gains taxes that buyers may be faced with when they in due course
sell the property can discourage collusion between buyers and sellers in declaring false
prices since it will not be in the interests of buyers to have recorded
an artificially low base price from which capital gains are calculated. The use of mortgages to finance purchases with mortgage valuations being carried out by licensed valuers diminishes the opportunity for under-declaration where charges like mortgages have to be registered.

The investment involved in tackling these technical issues is substantial and takes time to realise. Governments have to be willing to maintain momentum for reform for a significant period of time. There are governance obstacles that can stand in the way of this. Taxpayers may object to reform on the grounds that they fear (correctly in some cases) that the tax burden will increase. The potential beneficiaries, by contrast, are likely to remain silent or be disorganised. Governments need to address the reasonable fears of those households who lack liquidity to meet higher tax bills because they are cash poor but asset rich. It can be difficult to find champions of reform in government as property taxes require specialist skills and an approach that is very different from taxes on incomes, consumption, or employment. Many countries with low revenues from recurrent property taxes could raise the funds needed for investment in this area through World Bank loans. Their willingness to do so may require external stimulus. Economic crisis and the need to increase tax revenues can make possible what was previously thought to be unattainable.

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Figure 1 Recurrent Taxes on Immovable Property as a Percentage of the Gross Domestic Product of OECD countries, 2015

Figure 2 Recurrent Taxes on Immovable Property as a Percentage of the Gross Domestic Product in selected non-OECD countries, 2015


Figure 2 Recurrent Taxes on Immovable Property as a Percentage of the Gross Domestic Product in selected non-OECD countries, 2015
Figure 3 Recurrent Taxes on Immovable Property as a Percentage of Total Tax Revenues of OECD countries, 2015

Figure 4 Recurrent Taxes on Immovable Property as a Percentage of Total Tax Revenues in Selected non-OECD countries, 2015