International Property Tax Institute

PRESIDENT'S MESSAGE

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An interesting recent article advocated the charging of "land rent" in South Africa as a means of introducing a fairer distribution of income within the country. The article referred to a submission to a government tax committee which stated, "The most equitable possible conditions under which citizens might gain access to land would be if the government collected the rent of land and shared it equally among all citizens, either through a 'citizens' dividend' or through spending for public services."

It stated that a "general equilibrium analysis" in the United States of the effect of shifting taxes to land concluded that, in the short run, the overall benefit from the combination of higher wages and higher returns to investment would be 15% of net domestic product and, in the long run, a consistently higher growth rate. It said that South Africa could expect similar benefits and estimated that a tax collected from all of the rental value of land in South Africa would yield a sum which was close to the 2017-18 budget for VAT and income taxes.

It went on to say that, with the economic growth that could be expected to result from removal of the taxes that impede the economy, it was possible that the proposed land rent taxes could fully replace VAT and income tax. It argued that, given that land prices reflect the present value of the expected after-tax benefits of simple land ownership, and hence uncollected land rent, collection of land rent has the potential to replace most taxes.

It went on to look at the meaning of "land rent" and quoted Adam Smith who said it was simply "payment for the use of land". Putting this into the historical context, the article looked at the United Kingdom and stated "Then, as now, most of the UK was owned by the descendants of William the Conqueror's Normans who lived off the rents paid by tenant farmers. Some of them, like the Duke of Westminster in London, were later to do even better with urban rents."

It contained a further quote from Adam Smith in "The Wealth of Nations", where he said, "Both ground rents and the ordinary rent of land are a species of revenue which the owner, in many cases, enjoys without any care or attention of his own …". While the French and British landowners of the late 18th century ensured that this advice was not implemented, the concept was carried to heights of popularity in the Anglo-Saxon world by the publication in 1879 of Henry George's "Progress and Poverty". George advocated the single tax on land to replace all other taxes and, after he died while running for mayor of New York in 1897, over 200,000 people attended his funeral showing how popular he was.

It went on to say that, in a somewhat more democratic Britain than in Smith's time, Lloyd George's Liberal Party proposed a land tax in the budget of 1909. Although it was ardently espoused by Winston Churchill in rousing speeches, the land-owning House of Lords vetoed it. Many cities in North America, Australia and South Africa nevertheless introduced site value (only) rating as a result of George's work.

In his "A History of Economics: the Past and the Present" (1987) John Kenneth Galbraith notes, "In his time and even into the 1920s and 1930s, Henry George was the most widely read of American economic writers.… Progress and Poverty in various editions and reprintings, had a circulation in the millions." Galbraith also notes, "His Progress and Poverty, despite its continuing social influence, receives only passing mention or none at all in the standard works on the history of economic thought."

The article asks why? The short answer, it suggests, is that vested interests mounted a highly successful campaign to expunge discussion of the single tax from economics. One of the weapons in the neo-classical economists' arsenal was the conflation of land with capital. So, land was airbrushed out of the debate.

In the 20th century, the even greater failings of Marxism (plus tarnishing Georgists with that brush) made neoclassical economics seem like the only way to go. After the fall of the Berlin Wall, neoclassical economics had a decade or two in the sunshine, but its shortcomings are now plain to see. Economics really needs to come down to earth. Ignoring rent and the concomitant need for taxation have led to major distortions in the financial system and growing inequality.

The article goes on to argue that, freed from historical hang-ups on rent, South Africans can begin to appreciate and examine to what extent economic activity will be stimulated once the community begins to collect rent on the value it creates and reduces taxes on production and consumption, that is, economic activity. And, it goes on to say, the further we go in this direction the faster we will grow. Even those states where land rental collection has been applied, albeit to a limited extent, such as Singapore and Hong Kong, are prospering.

Moreover, there are signs that recognition of this phenomenon is gaining traction elsewhere, with economists paying increasing attention, while in Britain an all-party parliamentary group has been set up to examine land value capture. An example of the latter is the mushrooming of buildings around stations such as the Jubilee and Crossrail underground lines in London, which testifies to heightened land values due to publicly paid for infrastructure.

Moreover, while the neo-colonialist taint is overworked, it is particularly apt with regard to our (South African) dysfunctional rent-free land tenure system and its flip side, the equally dysfunctional tax system. Both have their roots in Britain ignoring the advice of the classical economists to collect the land rents arising out of the agricultural and industrial revolutions, which it was able to do by allowing the victims of land enclosures to go to the colonies willingly, or unwillingly, to join the army or navy, work in the dark satanic mills or go to prison!

An entertaining, and interesting, line of argument which readers may or may not agree with. At least it gives a new perspective on some of the issues involved in either land tax and/or land value capture.

Moving on, we held a series of interesting meetings during July which included a meeting of IPTI's Board of Advisors. Among the many issues discussed by the Board was an update from our colleagues in China about the proposed introduction of property tax in that country. The current view is that the Chinese government will complete the necessary legislative procedures in 2019.

We also completed work on some IPTI projects during July and we have just received confirmation that IPTI has been appointed to carry out a revaluation audit which will be interesting.

Looking ahead, we will be delivering a series of webinars in partnership with the Royal Institution of Chartered Surveyors (RICS). The topics to be covered in this series will include the "Valuation of Contaminated Properties"; "Preparing Expert Reports for Valuation Disputes"; the "Valuation of Public-Private Partnerships"; and "Giving Expert Evidence in Valuation Disputes".

In August, I will be speaking at the Australasian Valuers-General Conference which is being held in Christchurch, New Zealand. I will also be speaking at the Council on State Taxation (COST) Property Tax Workshop in Dallas, Texas. This annual workshop is held in cooperation with IPTI and is of particular interest to corporate entities, especially those with a global property portfolio.

In September I have been invited to speak at the WAVO-ANEVAR conference in Bucharest, Romania which is focussed on "Ethics in the Valuation Profession" which should be an interesting topic to explore, particularly in the context of property tax valuations.

Our annual Caribbean conference, held in partnership with the RICS, will take place in Montego Bay, Jamaica on 25th and 26th October 2018. Details of the agenda are now available on our website and it promises to be a very interesting and enjoyable event.

Our 2019 MAVS will be held in Slovenia on 25th and 26th June 2019. A recent "Expression of Interest to Present" has been published with a closing date of 1st September so, if you would like to speak at this event, please send us a submission.

More information about all our forthcoming events, along with registration and other details, can be found on our website: www.ipti.org.

Now, it's time for a quick look at what is making headlines concerning property taxes in selected countries around the world.

There have been some very high temperatures in the UK recently, and that is not the only issue that is making UK property taxpayers hot under the collar. The government has been promising reform of the UK business rates system (property tax for non-residential properties) for some time but, so far, has failed to deliver. Although progress is being made in Scotland following a report recommending improvements, in England, the Chancellor of the Exchequer has ruled out any imminent changes. There is continuing pressure to address business rates issues, in particular in relation to the retail sector where there has been closure of many High Street shops and associated job losses due, in part, it is said to the high burden of property tax as well as the increase in competition from online retail activity, but no indication of any major review of the system which ratepayers and many Members of Parliament are requesting.

In Greece, it is reported that the state continues to use different “objective values” (property prices used for tax purposes) for the taxation of residential properties, with one used for the calculation of the Single Property Tax (ENFIA) and another when the property is sold. The result of this policy is that the construction sector contributes less than 1 percent toward gross domestic product, with investment in housing having dropped to 0.6 percent from 11 percent in 2007. An example of this is the age coefficient for the objective values, which is the exact opposite of the factors that apply in ENFIA calculation. For ENFIA there is in effect the application of a “freshness” coefficient, as there is a 25 percent tax hike on newly built properties, even though the zone rates have just been determined according to the values of new homes. For example, a 100 square-meter apartment that is three years old with a zone rate of 2,500 euros/sq.m. will not be taxed for a value of 250,000 euros but as if it had a 312,500-euro value due to the additional application of the 1.25 multiplier imposed on buildings less than four years old. Yet if that same property were to be transferred, the transaction tax would be calculated on a value of just 225,000 euros thanks to the 0.90 age coefficient! Similar problems arise with the coefficients on commerciality and floor level, as there are major differences between the values used for ENFIA calculation and for property transactions. Property market professionals are calling for a radical overhaul of the property taxation system, with values updated annually to reflect the going rates.

It is being said that Hong Kong’s plan to tax unsold new apartments may have little effect on the city’s red-hot housing market. The levy was announced as part of a broader effort aimed at boosting supply in the world’s least affordable property market. Yet some analysts say the latest impost won’t dent soaring prices. Dealing with Hong Kong’s property boom has been one of the biggest challenges for the city’s lawmakers who’ve unveiled a series of measures in recent years to cool the market. But those measures have fallen short as demand has surged ahead of a chronic under-supply of homes, helping propel a more than 50 percent increase in prices over the past five years. With the latest rules, apartments left unsold for more than six months will be taxed at twice the annual rental income, or about 5 percent of the unit’s value. That’s a level, analysts say, developers can easily absorb. The tax is less than Singapore’s, which starts at 4 percent if an apartment is empty two years after completion, but rises to 12 percent if it’s still vacant after four years. The new tax in Hong Kong has to be approved by lawmakers, giving developers six to nine months to sell empty apartments. In addition, of the 9,000 vacant units in the primary market as of March, about two-thirds were completed since 2017 which means that developers may not need to sell them as quickly as the government expects.

The IMF is calling on the Tax Working Group in New Zealand to introduce a land tax in a bid to help give the Government’s KiwiBuild project a leg up. The report says KiwiBuild can provide the certainty needed to redirect builders’ incentives toward lower-priced housing and adopt new, more cost-effective building technology. “[But] the direct market intervention by the Government also comes with risks to the budget and risks of crowding out private housing supply and market distortions more broadly.” Raising land taxes, the IMF says, will help the Government meet its KiwiBuild goal. Calls for New Zealand to adopt a land tax are not new and have come from the likes of the OECD and the Productivity Commission before. In fact, a Tax Working Group in 2010 said it would be one of the best ways to help improve housing affordability because it would reduce the value of land. The Finance Minister has already told the TWG a land tax on family land under the family home was off limits. But beyond that, there may be scope for such a tax.

In Thailand, the government is poised to get some cash back from developers who build near public transport systems. The Cabinet will soon forward to the National Legislative Assembly (NLA) a “windfall tax” bill on sales of properties whose owners gain financially from government investment in public transport. The proposed law targets both existing and new commercial developments such as condominiums that are located within five kilometres of public transport systems in which the government has invested. The aim is to redistribute the excess profits that private landowners and developers derive from multibillion-baht public-investment projects, such as elevated and underground railways. The market value of privately owned properties often jumps after the state invests taxpayers’ money in new mass transit systems such as elevated trains and subways. The private sector subsequently benefits from building high-rise condominiums and other commercial projects on adjacent land, projects that command a much higher market value due to their close proximity to the new infrastructure. Proponents of the bill believe it’s unfair to the general public when landowners and investors gain enormously from the so-called windfall profits after taxpayers’ money pays for the transport infrastructure. The ordinary citizen gets nothing in return. The proposed law aims to levy a maximum 5-per-cent tax rate on the extra profits earned by landlords, condo developers and condo sellers, as well as other beneficiaries, when they sell their properties following completion of public transport projects. These people also benefit from public investment in elevated tollways, dual railways, seaports and the like and would be taxed accordingly under the bill. The proposed windfall tax is not to be confused with the land and building tax bill currently awaiting its second and final readings at the NLA later this month. Both pieces of legislation are seen as necessary fiscal measures in boosting government coffers, including those of local governments and, in doing so, reducing their dependence on the central government for development funds.

In the US, the so-called “dark stores” issue was the subject of a recent decision by the Ohio Supreme Court. The court ruled that a property’s sales price in an arm’s length transaction is not necessarily the value of the property for tax assessment purposes. In this case, a school board sought to have real property valued according to a recent arm’s-length sales price. The county auditor assessed the property at $1,084,660 for tax year 2014. The School District Board of Education complained that the property should have been valued at $5,641,100, because that is what the owners paid for it in July 2014. The Board of Review agreed and increased the property’s valuation to $5,641,100. The owners appealed the Board of Review ruling and introduced testimony and the valuation of an appraiser who concluded that the sales price represented the value of the leased fee, not the unencumbered fee-simple real estate. The appraiser stated that, since the retailor was a high-quality tenant, the lease provides for a rental rate that is more than double the market rent. Also, the lease term exceeds what is generally available in the market. It was also stated that “the real property would not command this price if it were vacant, leased at market levels after exposure of the market, or occupied by a less creditworthy tenant, or a tenant with a shorter remaining lease term.” Using the cost, income, and sales-comparison approaches, the appraiser valued the fee-simple interest as if unencumbered at $1,660,000 as of January 1, 2014. The Board of Tax Appeals refused to address the merits of the appraisal, so the owners appealed to the state Supreme Court. As already indicated, the Supreme Court ruled that taxing authorities must consider more than just the sales price to correctly value business real property and referred the matter back to them for reconsideration in the light of their ruling.

In Afghanistan, the protracted conflict and migration in search for better economic opportunities have led to unprecedented population growth in cities. Improving living conditions for burgeoning city populations is critical for prosperous and inclusive cities and has an important bearing on the country's future stability. UN-Habitat's City for All Programme (CFA) provides the Kabul Municipality and the Deputy Ministry of Municipalities in Afghanistan with technical support to reform municipal finance systems through a multi-pronged approach which includes revising legislation, improving procedures for registration of properties, promoting better financial management systems and strengthening human resource capacity. Although tenure security is a catalyst for economic development and poverty reduction, millions of households in Afghan cities have no property ownership rights and live in constant fear of eviction with minimal access to basic services such as water, sewerage and electricity. Many municipalities do not generate adequate local funding to provide basic infrastructure relying instead on central government funds. As the country moves to reduce its reliance on foreign aid and towards the declared national goal of self-reliance by 2024, it has become increasingly important to improve outdated local authority revenue systems. Although there are over 50 recognized municipal revenue sources, a property tax known as safayi has proven to be a cost-effective and relatively straightforward intervention with multiple benefits. Besides increasing municipal revenues, it also improves land administration, increases tenure security, and stimulates local economic development, particularly in informal settlements. With UN-Habitat's support, a comprehensive review of laws and regulations under which safayi fees are collected has been undertaken to improve efficiency and fairness. New regulations governing the issuance of occupancy certificates will grant occupancy rights for 70 per cent of properties in informal settlements in cities across Afghanistan. This has led to a more transparent and comprehensive system which has improved tax collection and simplified the process of safayi payment. UN-Habitat has also supported development of a safayi database and an automatic invoicing and payment tracking system.

Back to the USA where the Illinois Policy Institute has issued a report entitled "Puzzled by property taxes: Improving transparency and fairness in Illinois' assessment system". Among its many interesting findings is that Cook County performed worst on measures of assessment accuracy and fairness, but each county studied fell outside accepted standards in some respects. It also found that Illinois can improve its assessment process by replacing fractional assessment with assessment at full market value and by requiring more frequent assessments - ideally every year - and using more recent sales data.

And finally, another "unreal" tale of action taken by a body collecting property tax. In England, a council taxpayer was recently sent a back-dated bill for 3 pence (i.e. 0.03% of a British pound) relating to the 2013-14 tax year. It was accompanied by a letter saying that if it was not paid, the matter would be referred to the court and bailiffs may be sent round to enforce collection. Not surprisingly, the taxpayer complained that it would have cost the council far more than 3 pence to prepare and send out the bill and it would cost him far more than 3 pence to send the payment to them. Nevertheless, the council insisted that this was their normal practice. I suppose it is commendable that "every penny counts" when it comes to property tax collection, but surely common sense must kick in at some point!

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