PRESIDENT'S MESSAGE

November 2018

Just when I thought we might be able to focus on something other than land value taxation, yet another interesting article on the topic pops up in "Tax Notes International" under the heading "The Perfect Tax That Nobody Likes". An interesting and perhaps appropriate title.

In part, this article is a critique of the recent article on land value taxation in "The Economist" for which I was interviewed. The authors of the latest article state, "In a nutshell, the editors of The Economist have concluded that most countries are chronically underutilizing land value taxes, which they describe as the 'most efficient of all property taxes.' Support for that proposition is drawn from sources as diverse as John Locke, Winston Churchill, and the inventors of the board game Monopoly. As it turns out, an early precursor to the modern version of Monopoly featured a type of land value tax that eventually had to be eliminated because it prevented the accrual of monopoly status, which is the whole point of the game. Three cheers for game theory."

The Tax Notes article, still referring to The Economist article, goes on to say, "This article examines the case for increased use of land value taxes and draws a few lessons from different countries' experiences with them. The conclusion is that while such taxes make theoretical sense, they lack popular support and are best suited for subnational governments. They're also unlikely to have a strong distributional effect. Those seeking a fiscal solution to income inequality would do better to look elsewhere."

It continues, "A perfectly efficient tax probably doesn't exist, but proponents argue land value taxes come darn close. A 2010 policy paper commissioned by the Scottish Green Party goes so far as to suggest that land value taxes should be called something other than a "tax" because they merely recover economic rents from private hands and transfer them to the public purse."

It goes on to say, "Land value tax is based on the idea that land in its unimproved state is a gift of nature and, unlike capital or labour, has no cost of production. Furthermore, since land is fixed in supply (again unlike capital and labour), its value is purely a scarcity value reflecting the competing needs of the community for work, leisure and housing. Thus, land value (excluding the value of investments in the improvements) owes nothing to the owner or to individual effort, and everything to the community at large. Thus, the value of land properly belongs to the community."

On the face of it, this article may be confusing land value capture with land value taxation - a common occurrence - but it may also be conflating the two concepts in a helpful manner.

It continues, "The argument resonates better when fleshed out by real-world examples. Consider tube stations in London. The UK government spent £3.5 billion on the Jubilee Line extension, running from Green Park to Stratford Station. One study determined the project's completion resulted in a whopping £13 billion increase in private land values along the affected areas. A different study estimated the private gains to be somewhat smaller, at £9.75 billion. Either way, the gains accruing to private land owners was a significant multiple of the government's expenditures. That's the equivalent of an unintended wealth transfer from taxpayers to landowners."

I noted with interest that the article refers to two practical problems which I referenced in connection with my comments on land value capture - firstly, the problem that the increase in asset value does not mean a matching ability to pay as the owner may be asset-rich but income-poor and, secondly, the challenges associated with providing accurate and reliable valuations with little or no direct evidence.

As the article states, "Most voters do not appreciate being taxed on somebody's hunch or estimation. In a litigious society such as ours, one imagines a land value taxation regime would give rise to endless lawsuits claiming erroneous valuation."

The article observes that "Nations with land value tax systems tend to be smaller places with modest populations. Denmark, Estonia, New Zealand, and Singapore come to mind. The tax is often administered locally, with municipal officials determining the details of the rates and tax base. In some countries, the tax does not apply to residential property. Public spaces such as parks and schools are normally zero-rated."

It continues, "None of these countries relies too heavily on the tax as a revenue tool. Denmark, for instance, is widely regarded as a high-tax jurisdiction, but it purposefully keeps land value tax rates low, ranging between 1.6 and 3.4 percent. By contrast, the country has no problem imposing a 25 percent VAT, the highest rate permitted under EU rules. It's an interesting observation that such a socially-minded nation chooses to max out the rate of its regressive consumption tax, but displays remarkable temperance when taxing land rents."

The author goes on to say, "New Zealand has a split-rate property tax system, with varying rates being applied to raw land and improvements. That's the equivalent of combining a land value tax with a secondary tax on real estate development (a neutral tax coupled with a less optimal partner). In recent years, the tax rates applicable to improvements have increased, while the rate applied to raw land has decreased. Arguably, the country is getting that backwards, unless factors other than neutrality and efficiency are at play. I suspect the impulse to tax improvements more heavily is due to a desire to extract higher taxes from the better off."

The conclusion in the article is, "The strongest argument for land value taxation is rooted in neutrality and efficiency - not a burning desire to redistribute wealth. These are causes that matter to the purists among us, which may help explain why land value taxes continues to have little traction worldwide."

Sadly, but perhaps predictably, the article does not therefore provide any solutions to the issues associated with land value taxes, but it does review the issue in a helpful and informative manner.

Moving on, I have just returned from the annual RICS-IPTI conference in Montego Bay, Jamaica. I am pleased to say that the conference was well attended and contained a wide-ranging series of interesting presentations from local, regional and international speakers. The conference was officially opened by the Mayor of Montego Bay and we had very good support from the Jamaican National Land Agency. There were many interesting and informative sessions, but I would just like to highlight two of them. The first was a discussion around "Ethics and Professional Standards" which provoked some lively debate. The other, for which I was a co-presenter along with a colleague from the RICS, was on the topic of "Land Value Capture" which looked at the situation in the UK and selected countries around the world and drew upon the latest research and articles on the subject, many of which have been referred to in these newsletters. In addition to the "formal" parts of this two-day event, we held a very enjoyable networking reception. Some photographs from the event can be found on the IPTI website.

Another interesting event that took place during October was a workshop IPTI delivered in Ontario on the subject of "Understanding Assessment and Property Tax Policy". Dr Enid Slack from the Munk School of Global and Public Affairs at the University of Toronto joined me for this one-day event which was well attended by a lively audience who fully participated in the interactive workshop. IPTI also delivered similar workshops in other parts of Canada recently and it is clear that there is a demand for this type of event which takes a high-level look at the policy and practice of property tax systems.

On 15th October, we held a meeting of IPTI's Board of Advisors which, among other issues, discussed the position with regard to the treatment for property tax purposes of churches and similar properties used for religious worship in countries around the world. The Board also had an interesting discussion on land value capture and land value taxation sharing the experience of Board Members.

Also, on 16th October, we held a meeting of IPTI's Corporate Advisory Committee. This meeting was held in Boston, USA and covered a number of topical issues along with the future events calendar.

During October, I attended the annual conference of the Institute of Revenues, Rating and Valuation (IRRV) which was held at Telford in the UK. The conference included a number of interesting and topical papers covering a wide variety of local government and property tax issues. The IRRV kindly invited me to present an Award at their Gala Dinner which was a very enjoyable occasion.

On 18th October, in partnership with the Institute of Municipal Assessors (IMA), we delivered a webinar on the "Derivation of Capitalization Rates". Our two experts covered the challenges assessors and valuers face in deriving capitalization rates in the application of the direct capitalization methodology. Emphasis was placed on the derivation of the rates from comparable sales and discussion of the data requirements and practical application of the methodology.

Looking ahead, on 1st November, we have a one-day IMA-IPTI workshop on the topic of "Conducting Appropriate Sales Investigation". This workshop will cover challenges with data collection from the buyers' and sellers' perspective; sales verification concepts; questionnaires and processes; sales adjustment grids and sale analysis; stratification of sales, use and location. General concepts and applications for investigation in appraisal value modeling and some components of statistical analysis will also be covered, along with practical applications.

On 6th November, we have an RICS-IPTI web class, this time on the topic of "The Valuation of Contaminated Land". Valuing property that is subject to some form of contamination is particularly difficult. Much depends on the nature of the contamination/impairment and the type, and cost, of necessary remediation works. The web class will be presented by a lawyer and an appraiser, both having considerable experience in dealing with this type of valuation work.

On 15th November, we have another IMA-IPTI webinar, this time on the very topical subject of the "Valuation of Big Box Retail Properties". The correct method of property assessment valuation of big box stores has proved challenging and controversial. There is a lot of discussion taking place regarding the appropriate valuation methodology. The presenters in this webinar will share their experiences on landmark changes in the assessments without the use of the typical adversarial process. A valuation methodology - including practical examples - will be discussed.

On 28th November, we are holding a one-day workshop in partnership with the RICS. This is concerned with "Property Assessment and Taxation in Canada". The aim of the workshop is to satisfy the need for a greater depth of understanding of the real strengths and benefits that distinguish property tax from other forms of taxation. It will provide knowledge about *ad valorem* fundamentals in three modules - evolution; tax policy (principles, challenges and issues); and assessment valuation and taxation challenges.

On 6th December, we are holding a one-day workshop in partnership with the IMA on the subject of "Separating Business Enterprise Value from Real Estate Assessment Value". This workshop will include a panel of experts who will discuss the important principles and guidelines in this challenging area.

More information about all IPTI's forthcoming events, including our 2019 MAVS in Slovenia, 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.

In Slovenia, the Finance Ministry has announced that the launch of a real estate tax, which has been in the making for years, is scheduled for 2020. It suggested that the tax would not exceed the levy imposed on real estate owners so far. The ministry said it continued working on the tax during the change of government and that next year could bring a repeat of the mass real estate appraisal. A draft version of the tax bill could be submitted for public debate at the end of November, while the act could be adopted before next year's summer recess. The launch of the tax is scheduled for 2020. Serving as the basis for the tax will be the value of the real estate, determined via a mass appraisal system based on the real estate valuation bill passed last December. The current plan is to let municipalities keep the entire revenue from the tax. Total revenue, estimated at EUR 230m for this year, is expected to increase by 20%-30%, since additional real estate will be subjected to the tax, possible also property owned by the church and the state. While it is too early to discuss tax rates, the ministry said municipalities could get the power to adjust the rates by 50% in either direction. A 2013 attempt to introduce the tax collapsed as the Constitutional Court ruled the act on the valuation of real estate unconstitutional. The Mapping and Surveying Authority (GURS) says that data on real estate has been improved substantially in the last four years and that appraisal models have already been drawn up on the basis of the new appraisal act.

Moving on to Africa, in Namibia it is reported that the government collected about N$350 million in land tax over the past 14 years, which is N$178 million less than the state wanted to collect during that period. The state introduced this tax to fund its resettlement programme, discourage multiple farm ownership, and to encourage the efficient use of agricultural land. Statistics show that the government did not collect the N$528 million in land tax as planned. A spokesman said the N$350 million was collected over 14 years, despite legal challenges by farmers who questioned the constitutionality of the tax. The land tax was collected between 2005 and 2018 at an average of N$25 million per year, he added. In February 2018, the High Court halted the land tax collections until objections lodged in the courts had been clarified. The court, however, lifted the ban three months later, and gave farmers an option to pay the tax, especially those who wanted to transfer the land to new owners. A farm owner needs a tax clearance certificate before selling or transferring land ownership. The spokesman stated that, should the objections before the court lead to an approval of the 2012 valuation roll, the tax collections not yet recovered will be backdated, and any penalties on any late payment will depend on the “court's directive in the matter”.

In the USA, Proposition 13 in California has strictly limited property tax increases since 1978. Voters could get a chance to change that soon as an initiative qualified for the November 2020 ballot that could lead to a $145-million campaign and dismantle Proposition 13’s protections for businesses. The initiative would end the state’s restrictions on taxing commercial and industrial properties and increase tax receipts for cities, counties and school districts by an estimated $6 billion to $10 billion a year. Proponents say that public services have been starved of resources since Proposition 13’s passage in 1978. By contrast, business groups and taxpayer advocates are already digging in to defend their interests from a tax increase they contend would worsen a business climate consistently ranked among the worst of any state in the country because of California’s high corporate, income and sales taxes. Proposition 13 limits property taxes for both homes and businesses to 1% of a property’s taxable value. The initiative also restricts a property’s taxable value from increasing more than 2% each year, no matter how much its value rises on the market. The longer a person or a company owns a property, the less they pay in taxes compared to its market value. Under the proposed initiative, protections for residential properties would not change, but local governments would be able to levy taxes on commercial and industrial land based on a property’s market value, a process known as “split roll.” No doubt the debate on “Prop 13” will continue.

In Canada, the City of Calgary in Alberta faces problems as the shrinking value of downtown office towers leaves a large property tax gap. Part of the solution could mean imposing higher property taxes on homeowners across Calgary, but that carries political problems. The downturn in oil prices in 2015 and 2016 led to thousands of employee layoffs and a dramatic increase in vacant office space in the central core. Under the city’s annual revenue-neutral reassessment process, empty offices and buildings with falling property values pay lower municipal taxes if their assessments decline. The city, however, still needs a certain amount of money each year to fund services. For the past two years, the council has utilised its reserves to soften the blow, capping property tax increases on businesses at five per cent. A recent study found the office vacancy rate in the city’s downtown dipped to 27.3 per cent during the third quarter. Even with moderate growth, it could take 10 to 12 years to get back to a normal rate of office vacancies in the downtown towers. Last year, all of the buildings in the downtown lost $1.6 billion, or more than nine per cent, of their assessed value. In 2016, they shed $3.8 billion.

Australia needs a national plan to encourage denser, better connected and more sustainable cities, argues a recent parliamentary committee report. Among its many recommendations are two new ministers, a statutory office and high-speed rail. With Melbourne and Sydney each zooming past 5 million people, expensive housing, an ageing population, an increasingly service-oriented economy and looming climate change, cities are shaping up as a major issue in Australia's policy landscape. Among its many recommendations, the report advocates the use of value capture "where government recoups part of the increase in private land values when it builds new infrastructure" which could help fund much needed projects. "The development of value capture as an organising principle of infrastructure planning and procurement, and the reform of the taxation system to match its requirements, are fundamental to the significant investment in infrastructure required to ensure the efficient growth and functioning of Australia's cities and regions," says the report.

In Luxembourg, it is recommended that property tax reform should be tackled by the next government. The Interior Minister says "sensitive" reform is one of the major issues that must be dealt with. "The next government will have to deal with two major topics - property tax reform, consistent with a comprehensive reform of taxes, and the unification of text on communes and communes' unions," he said. He went on to say that property tax - due to it being a reform that will "not satisfy everyone" - is an issue the current government has failed to tackle. The tax is implemented by communes, and all homeowners receive a property-tax assessment indicating an amount to be paid. The tax is levied on all properties, and multiple owners are jointly liable to pay. The tax generates €40 million for the State.

In France, it seems that even the incredibly wealthy don't like paying property tax. A well-known Russian billionaire, who owns a large property on the exclusive Cap d'Antibes peninsula in the south of France, is fighting his property tax bill. French authorities said they had undervalued the "holiday home" resulting in a €1.2 million additional tax bill. Built in the late 1920s for a newspaper magnate, the property spans more than 75,000 sq m (807,000 sq ft) with a living area of more than 2,400 sq m in the chateau and a guest pavilion. The chateau is known for having been the residence of several crowned heads. King Edward VIII moved in just after he controversially abdicated in 1937 to marry American socialite Wallis Simpson. King Leopold III of Belgium, the last Queen of Italy, and Farouk I of Egypt, also lived there. It was purchased by the billionaire for over €73million in 2004. Since then, a total of €150 million has been spent on improvements which the authorities are now seeking to reflect in their revised valuation. So far, the French courts have upheld their revised valuation, but the battle continues!

And finally, I don't know whether the UK Chancellor of the Exchequer reads my monthly newsletter and the occasional reference it contains to the treatment of public toilets for business rates (non-residential property tax) but, in his Budget speech on 29th October, he announced that owners of such toilets would no longer be liable to pay rates. He even took over my role as a provider of toilet puns when he mentioned that local authorities could at last "relieve themselves" of this liability and added "This is virtually the only announcement in this Budget that hasn't leaked." Is nothing sacred?

Paul Sanderson

President, International Property Tax Institute