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Overview of property taxation systems

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TITLE: “Overview of property taxation systems”

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1. Introduction

Property taxes are one of the traditional revenue sources for most governments of the world, and have existed for a very long time. The tax is collected at different administration levels, ranging from the national to the federal to the state/county/region to the municipality.

According to a United Nations Human Settlements Program report, property tax is widely implied and generally accepted to be a combined assessed value of land, buildings that it contains and any improvements made thereto (UN-HABITAT 2011a). Excluding the notion of land value taxation, property tax attempts to generate revenues from structures and land improvements, although the latter part has given rise to debates on its fairness. In the developed countries property tax is usually ad valorem, or market value based, since this is considered to be fairer than other methods. This paper categorises various types of property types as they are applied in different nations, with special emphasis on the EU region.

2. Classification of Property Taxes

The Organization for Economic Co-operation and Development (OECD) classifies property taxes into six basic types: recurrent taxes on immovable property; recurrent taxes on net wealth; estate, inheritance and gift taxes; taxes on financial and capital transactions; other non-recurrent taxes on property and other recurrent taxes on property (Eurostat 2014). Some of the above six types are subdivided into further categories – for example recurrent net wealth taxes are divided into individual and corporate taxes. Other competent bodies such as the System of National Accounts (2008 SNA) and the European System of Accounts (ESA95) apply their own code schemes to this classification. The property tax types and their codes are shown in Table 1 below:

Table 1: Property tax types and code schemes used by various authorities. **Source:** Eurostat 2014, p. 280.

| OECD classification | 2008 SNA | 1995 ESA | ESA 95 classification |
|--|-----------------|-----------------|--|
| 4000 Taxes on property | | | |
| 4100 Recurrent taxes on immovable property | | | |
| 4110 Households | D.59-8.63(a) | D.59A | Current taxes on capital |
| 4120 Other | D.29-7.97(b) | D.29A | Taxes on land, buildings or other structures |
| ----- | | | |
| 4200 Recurrent net wealth taxes | | | |
| 4210 Individual | D.59-8.63b | D.59A | Current taxes on capital |
| 4220 Corporations | D.59-8.63b | D.59A | Current taxes on capital |
| 4300 Estate, inheritance and gift taxes | | | |
| 4310 Estate and inheritance taxes | D.91-10.207b | D.91A | Taxes on capital transfers |
| 4320 Gift taxes | D.91-10.207b | D.91A | Taxes on capital transfers |
| 4400 Taxes on financial and capital transactions | | | |
| | D.59-7.95d | | Stamp taxes |
| | D.29-7.96e | D.214B, C | Taxes on financial and capital transactions |
| 4500 Other non-recurrent taxes on property | | | |
| | D.91-10.207a | D.91B | Capital levies |
| 4600 Other recurrent taxes on property | | | |
| | D.59-8.63c | D.59A | Current taxes on capital |

Property taxes might be area based or value based – the latter type is subdivided into annual rental value, market value and land value. Area based valuation makes use of the square meters of land occupied and may not, therefore be fair; the latter method on the other hand is based on a fair price as may be agreed between a willing buyer and a willing seller. The annual rental value method is used often because a tax on rental value is in effect a tax on the market value.

3. Property Taxes in EU

Property tax in the European zone is concerned mainly with collection of annual taxes on immovable property – the latter comprising both real property and real estate. Approximately 66% of property taxes in EU are of a recurring nature, contributing to 1.5% of the GDP and collected annually on an ad valorem basis. There are significant variations in recurrent property tax rates – the rates are highest in the UK (3.4% of GDP), Denmark (2.4% of GDP) and France (2.1% of GDP), while they are not applied at all in Croatia, Luxembourg and Malta. Rates of taxes on property and recurrent taxes on immovable property levied by different EU countries, arranged in descending order by recurrent taxes, are shown in Figure 1 below. For the group European Union 28 (EU28), property taxes accounted for 2.3% of GDP in 2012, with recurrent taxes on immovable property accounting for 1.5% and other property taxes accounting for the balance 0.8%. These taxes together generated € 293.5 billion in 2012.

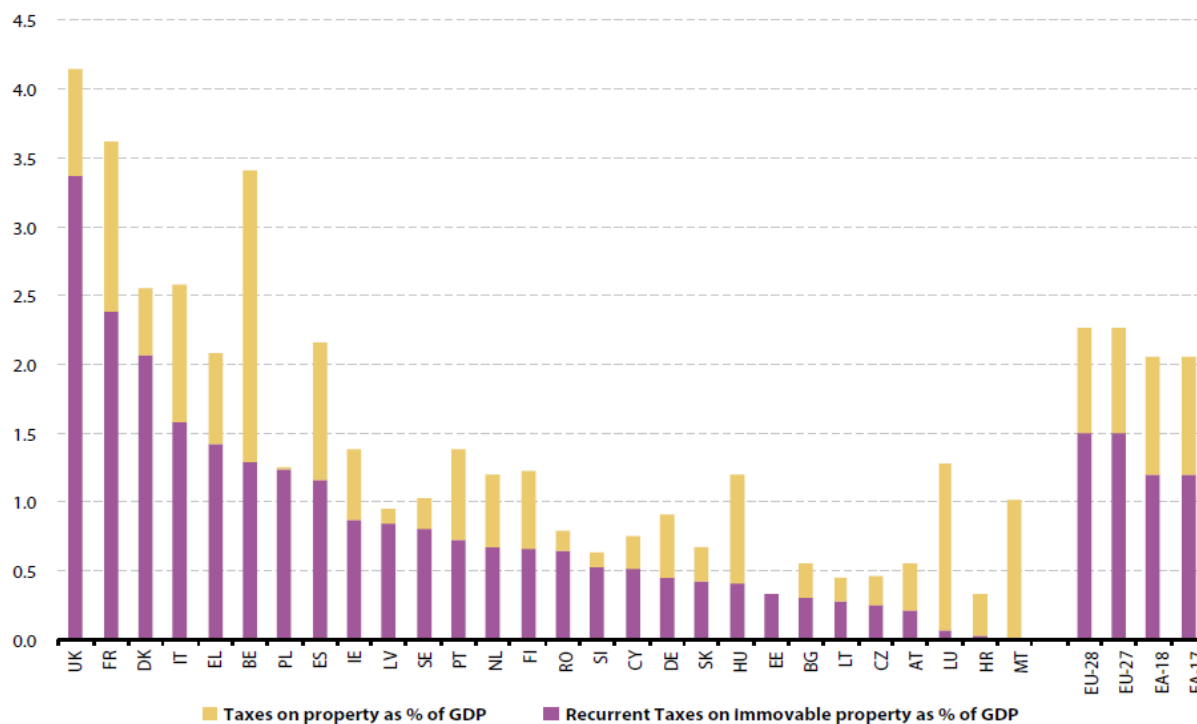


Figure 1: Property Tax rates in countries belonging to EU. **Source:** Eurostat 2014, p. 44.

Many European countries impose one or more taxes on property, including the following: recurrent, immovable; recurrent, net wealth; estates, inheritances, gifts; financial and capital transfers; other non-recurrent taxes; and other recurrent property taxes. Some of the countries have been characterized as high reliant on some of these taxes, if the ratio of revenues accruing from a particular tax to all tax revenues exceeds the 75th percentile of countries levying this type of tax. Other characterizations are mid, low (ratio not exceeding the 25th percentile) and none (IMF 2010). To cite two examples, Germany is characterized as mid reliant on recurrent, immovable; not reliant on recurrent, net wealth; mid reliant on estates, inheritances, gifts; not reliant on financial and capital transfers; highly reliant on other non-recurrent taxes; and low reliant on other recurrent property taxes. State or regional authorities in the countries received 52.3% of property tax revenues, while 47.7% of revenues accrued to local authorities; none accrued to central authorities. The U.K., on the other hand, follows a different model – with 68.7% accruing to central authorities and 31.3% to local authorities. The U.K. is characterized as highly reliant on recurrent, immovable; not reliant on recurrent, net wealth; mid reliant on estates, inheritances, gifts; mid reliant on financial and capital transfers; highly reliant on other non-recurrent taxes; and not reliant on other recurrent property taxes. Albania is an EU country in which 100% of revenues from property taxes are

collected by local authorities. Data on property tax type and percentage accruing to different authorities for fifteen countries in the EU are shown in Table 2 below:

Table 2: Property tax type, reliance and percentage accruing to different authorities for selected countries in the EU. **Source:** UN-HABITAT 2011b, p. 7.

| Country | Property Tax Type and Reliance on each type | | | | | | Accruing to Authority | | |
|-------------|---|-----------------------|------------------------------|-------------------------------|---------------------|--------------------------|-----------------------|-------|-------|
| | Recurrent, immovable | Recurrent, net wealth | Estates, inheritances, gifts | Financial & capital transfers | Other non-recurrent | Other recurrent property | Central | State | Local |
| Austria | Low | No | Mid | Mid | No | No | 14.4 | 4.4 | 81.2 |
| Belgium | High | Mid | High | High | Mid | No | 11.3 | 51.6 | 37.1 |
| Cyprus | Mid | Mid | Mid | Low | No | No | 91.7 | 0.0 | 8.3 |
| Denmark | Mid | Mid | Mid | Low | Low | No | 50.7 | 0.0 | 49.3 |
| Estonia | Mid | No | No | No | No | No | 0.0 | 0.0 | 100.0 |
| France | High | High | High | Mid | No | Mid | 19.3 | 0.0 | 80.7 |
| Germany | Mid | No | Mid | No | High | Low | 0.0 | 52.3 | 47.7 |
| Greece | Low | Mid | Mid | High | Mid | High | 87.8 | 0.0 | 12.2 |
| Ireland | High | No | Mid | No | No | No | 19.4 | 0.0 | 80.6 |
| Italy | Mid | Mid | Mid | No | No | Mid | 4.5 | 0.0 | 95.5 |
| Russia | High | No | Low | No | No | Mid | 0.0 | 79.1 | 21.0 |
| Spain | High | Mid | High | High | Mid | No | 0.7 | 58.9 | 40.4 |
| Sweden | Mid | No | Low | Mid | No | No | 60.8 | 0.0 | 39.2 |
| Switzerland | Low | High | Mid | Mid | No | No | 19.1 | 50.0 | 31.0 |
| U K | High | No | Mid | Mid | High | No | 68.7 | 0.0 | 31.3 |

Some EU countries impose more than one type of recurrent tax on immovable properties – these include tax on land alone, tax on buildings and other structures alone, and taxes on land and building clubbed together. Movable property is also taxed in most EU countries, and this category includes business machinery and equipment, certain vehicles, aircraft and watercraft (UN-HABITAT 2011b). Most of these countries use capital value-based, annual rental value-based and area based taxes; in addition the assessment for the first two tax types may either be closely tied to current market prices, or they might be completely dissociated from current prices. To cite a few examples, France collects land tax as per *Taxe Foncière (sur les*

propriétés non bâties), collects housing tax as per *Taxe d'Habitation*, and collects real property (land & buildings) tax as per *Taxe Foncière (sur les propriétés bâties)* and *Contribution Économique Territoriale, 2010*. It does not have movables tax and collects all taxes on annual rental value-based basis. Greece, on the other hand, imposes building tax as per *Special Duty on Buildings Powered by Electricity (2011)* – this is an area based tax – and imposes real property tax as per *State (Large) Real Estate Tax (2010)* and *Local Real Estate Duty (1997)* – both are capital value-based taxes. Denmark uses capital value based assessment for collecting all three types of taxes – land, building and real property. The capital value-based rates are usually cadastral value based (UN-HABITAT 2011b).

One of the features of the EU property taxation system is that recurrent taxes on net wealth is apparently going out of favor – on the other hand, countries such as France, Luxembourg, Norway and Switzerland impose these taxes for generating substantial revenues. While Iceland has recently reintroduced the tax for corporations only, countries such as Denmark, Finland, Netherlands, Spain, and Sweden have abolished the tax. On the other hand taxation of transfer of real property, are used by at least 33 countries within the EU (UN-HABITAT 2011b).

4. Property Taxes in the US

In the United States property taxes are collected by authorities whose jurisdictions fall at or below state levels. These taxes are collected on land, buildings and improvements thereof; but jurisdictions, and therefore tax rules, vary significantly across the fifty states in the country. Another peculiar feature is that some jurisdictions overlap – for example parishes or towns – resulting in multiple taxes being imposed on a common property.

Property tax payable by an entity in the US is determined by the tax rate and the tax base, and the latter is a function of both the assessed value and the assessment ratio (the part of the value on which tax is to be assessed). The tax burden is generally accepted to be substantial, and this has prompted most state level authorities to implement mechanisms that limit the burden (Harris 2013). Restrictions on tax rate and assessment ratio have been imposed, the overall tax liability has been reduced or even eliminated, and circuit-breakers have been introduced so that homeowners from specific demographic segments (such as the elderly or low-income groups) have a lower tax rate. This multitude of tax collection authorities, laws and restrictions has also given rise to a debate in the US as to the nature of the property tax. Some economists argue that it should be classified as a “benefit tax”, allowing local

administrative bodies to improve services from the property tax revenues, while others classify it as “tax on capital” that actually distorts the market for property investment. Progressiveness and efficiency of the property tax regime are also viewed accordingly (Harris and Moore 2013). Some economists have argued that the fiscal zoning practices are in fact close to an ideal situation where property development costs to the community and benefits accrued therefrom nearly balance each other (Fischel 2013).

If a state-wise picture of property taxes across the US is to be obtained, it should be noted that revenues from this source constituted 24-27% of total revenues in the period 1981-2008 (the proportion was even higher earlier, but tax rates were rationalized in the face of public discontent). Northeastern states typically generate 30% of their total revenues through these taxes, while states on the west coast and some southern states generate only 20% of their total revenues. Per capita property taxes imposed on households, businesses and industry are higher in the former group of states than in the latter. As an example, the state of New Jersey has the highest property tax rate in the country, with a median value of 1.89% aggregated from all its counties. Each county has its own assessment mechanism, but Essex County has the highest tax rate (it is also the County with the highest rate across the US). It imposes an annual average of 2.05% on the assessed fair market value of a property; its neighbor Hunterdon County imposes an annual average rate of 1.91% (Tax-Rates.org 2014). New Jersey taxes various categories of land (vacant, residential, commercial, industrial, apartment, etc.) and homesteads, but does not impose taxes on personal property, motor vehicles, inventory, machinery and equipment (with some exceptions). In contrast, the west coast state of California has a median rate of only 0.74% and Utah, has a rate of 0.6%. Texas is an exception – despite being the southernmost state of the US, it also has one of the highest annual median rates of 1.81%.

The annual ACS survey conducted by the Census Bureau on three million households across the US provides data estimates on five year averages of property tax revenues per household across 3143 counties. These estimates show that property tax payable by each individual house owner was \$1000 annually during the period 2007-2011, with the amount being between \$500-\$1500 for 60% of the counties. Residents in 13% of the counties paid less than \$1000 annually, while those in 27% of the counties paid more; a very few counties (less than 3%) had property tax amounts as high as \$4000 or more, while nine counties reported amounts over \$8000. This county wise classification is shown in Figure 2 below:

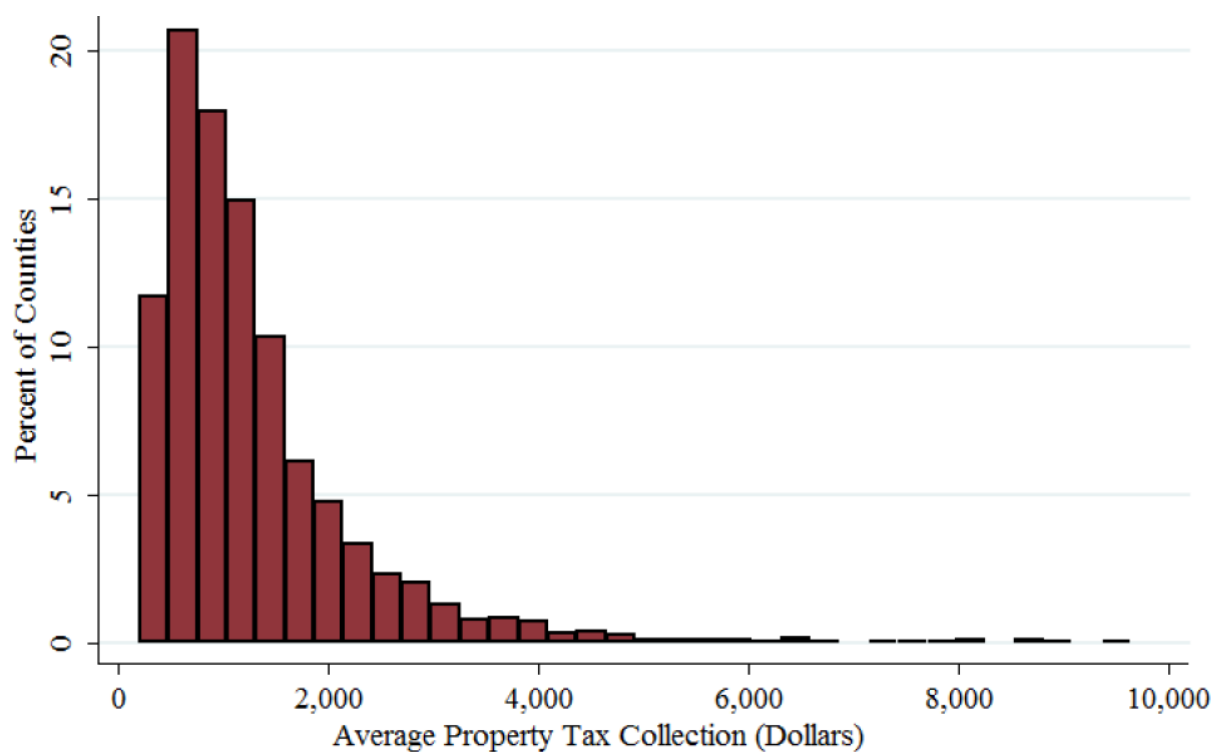


Figure 2: Classification of counties across the US in terms of property tax revenues collected per household during the period 2007-2011. Median collection amount is \$1000, with 13% counties collecting less and 27% counties collecting more. **Source:** Harris and Moore 2013, p. 5.

One of the distinguishing features of the property tax regime in the US is variations in rates and assessment frameworks from one state to another. There is much less intra-state (or county wide) variation, but even this observation has exceptions. For example the states of New York, Illinois, New Jersey, and Virginia exhibit significant differences in payable taxes from one county to another, while some states such as Pennsylvania and Texas exhibit county wide differences in property tax payable as a proportion of assessed value of the property (Harris and Moore 2013).

5. Property Taxes in Asia and Australia

The tax classification system developed by OECD and referred to earlier in this report is followed by many countries across the world, including most of the former Soviet Union countries now located in Asia, many developing countries in Africa, major countries in southeast Asia, and the Latin American countries. However, variations in tax collection mechanisms, assessment methods, property valuation methods and tax rates also exist in most of these regions. Practices in some of the major countries are discussed in this section.

India, located in Southeast Asia and one of the countries with the oldest tax systems in the world, exhibits variations similar to the US. Many parts of the country use the annual rental value or reasonable rent therefrom method of assessment; recently, however, major cities and some states have started using an area based valuation system similar to that in EU countries. Vacant land owners and building owners are taxed, at rates varying from 6-10% of the assessed annual value depending on the category of the property. Israel, also in Asia, taxes developed residential and non-residential property, occupied undeveloped land and agricultural land. It does not use an *ad valorem* system, instead relying on a non-value area-based property tax dating back to 1970. Taxes are collected mostly at municipal levels and rates are imposed on the basis of a complicated system with multiple consideration factors (Yuan, Connolly and Bell, 2009).

Australia imposes a recurrent, immovable tax, other non-recurrent taxes and taxes on financial and capital transfers. Although land tax is imposed at an annual rate of 1.6%, there is a threshold value below which it is not imposed. The principal place of residence of an individual is not taxed, but other types of buildings are taxed. Land tax in Australia is capital value based, while real property tax is assessed on the basis of capital value as well as annual rental value (Almy 2013).

6. Conclusion

Property taxes are imposed in most countries across the world and they are an important part of fiscal policies followed at national as well as local levels. Revenues from these taxes are used by many municipalities in order to provide community developments and other benefits. Recently there is a debate in many countries in order to make this particular tax type more progressive, equitable and efficient. Recognizing the need for a common framework, the OECD has classified property taxes into six categories that are recognized by many tax bodies in the developed as well as developing countries. It is expected that property tax practices will be further rationalized and reasonable rates will be imposed in the future.

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