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**TOPIC: REAL PROPERTY TAX  
AND INEQUALITY**

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# CONTENTS



1. **Background**
2. **Real Property Tax, its determination and Tax Units**
3. **Arguments in favor of Real Property Taxation**
4. **Horizontal and Vertical Equity in Real Property Taxation**
5. **Real Property Tax and Fairness**
6. **Property Tax and Local Government Revenue**
7. **Real Property Taxation – Tanzania Experience**
8. **Real Property Tax Revenue Use and Impact on Compliance**
9. **Conclusion**

# 1.0 BACKGROUND

- Very few countries, outside industrial Anglophone countries, raise significant tax revenue from real property taxes
- Property taxes may represent the best choice as source of steady revenue, in particular, at the local government level.

# Background.....Cont



The vivid advantages of property tax are:

- Most important autonomous revenue source of local governments.
- Can provide access to broad and expanding tax base.
- Compared to indirect taxes and grants it promotes broader efficiency aspects and is easy to administer.
- The property tax relevance as appropriate local tax includes the following:
  - Satisfies theoretical requirements of a local tax- which are; immobility, non-exploitation and non-redistributive.
  - Properties are primary source of storing accumulated wealth, hence a clear indicator of wealth.

# Background ....Cont

- Real property is visible and immobile, and therefore easy to administer.
- Space-specific and not subject to fluctuations.
- Most appropriate tax for generating local revenues.
- Provides realistic and stable revenue base/flows.

## 2.0 REAL PROPERTY TAX, ITS DETERMINATION AND TAX UNIT

- ❑ Real Property for the purposes of taxation is defined as land and permanent structures (developments) attached thereto. Real Property Tax is based on the value of real property.
- ❑ The kind of properties assessed to the Real Property Tax is the parcel of real property in an assessing unit.
- ❑ Some real properties, such as religious or government owned properties are completely exempt from paying property taxes.

## REAL PROPERTY TAX, ITS DETERMINATION AND TAX UNIT.....Cont.

- ❑ The amount of Real Property Tax is determined by two factors; the properties assessment (valuation) and the tax rates.
- ❑ Real Property Tax is usually focused on the tax paid by real properties owners.
- ❑ Real Property taxes also affect persons who rent, rather than own properties.



### 3.0 ARGUMENTS IN FAVOR OF REAL PROPERTY TAXATION



- ❑ Real Property tax fulfills the “ability to pay principle” by taxing those people with large quantities of wealth more heavily than those without such wealth.
- ❑ Property tax is rooted in the “benefit principle of taxation”.
- ❑ Real property tax based on the value of land and buildings (immovable assets), is stable and easily enforceable hence a legitimate target for taxation.
- ❑ Real property tax is considered among the best options available for providing additional source of revenue required to finance local governments.

## 4.0 HORIZONTAL AND VERTICAL EQUITY IN REAL PROPERTY TAXATION



- ❑ Equity is one of the fundamental criteria used to evaluate individual taxes and tax systems.
- ❑ Most taxpayers and policy makers consider equity or fairness to be extremely important.
- ❑ Most agree that higher income or wealthier persons should contribute more in taxes than those with lesser ability to pay - how much more, is often the subject of fierce public debate.
- ❑ Horizontal equity means that equals are treated equally under the tax system, or those with the same ability to pay, pay the same amount of taxes.

## 4.0 HORIZONTAL AND VERTICAL EQUITY IN REAL PROPERTY TAXATION.....Cont



- ❑ Theoretically, property tax is a wealth-based tax with the value of property (usually restricted to real estate property) serving as the tax base or measure of ability to pay.
- ❑ Under a horizontally equitable property tax, taxpayers with equally valued property pay the same amount of taxes.
- ❑ The implicit assumption is that real property market value is the appropriate measure of accumulation of wealth because it reflects the amount that the owner would receive if the property was liquidated or sold.

## 5.0 REAL PROPERTY TAX AND FAIRNESS



- ❑ Compared to other taxes, such as sales tax or value added tax and excise taxes which are most regressive taxes, are rarely maligned as the real property tax.
- ❑ The “sticker shock” effect of property tax is partly to blame on this.
- ❑ Property Tax is a large, very noticeable payment that is made once or twice a year, while sales tax or value added tax is spread throughout the year on hundreds of purchases.
- ❑ The property tax can seem more oppressive and more unfair than actually is, simply because it is more visible.

- ❑ Property tax is generally regressive being based on property value rather than income levels- and real property values do not always vary directly with income levels.
- ❑ Real property values represent a much larger share of income for middle and lower income families than for wealthy ones.
- ❑ Inequities in property taxation include such circumstances as the ones listed below:

- ❑ Property tax is payable once or twice a year hence largely noticeable payment, as opposed to taxes that are paid on monthly or quarterly basis.
- ❑ Property taxes are based on property values rather than on income levels and do not always vary directly with income levels.
- ❑ Property taxes are not responsive to variation in taxpayers income.

- ❑ Elderly taxpayers at the end of their working careers who find themselves “property rich but income poor “are not considered.
- ❑ Value of real property is not an excellent measure of one’s wealth, because wealth held in other forms, e.g. Stock bonds, Shares, are not taxed until when realized.
- ❑ Collectability; poses tax payment problem where one has no income, but has taxable properties.

## 6.0 REAL PROPERTY TAX AND LOCAL GOVERNMENT REVENUE

- ❑ Based on Tanzania Experience, Real Property has some attractions as a local revenue base since it is imposed on immobile assets and therefore difficult to avoid.
- ❑ It also has some obvious weaknesses which need to be taken into consideration before heavy reliance is placed on it. For instance, problems of valuation and tax enforcement.
- ❑ Harsh enforcement mechanisms may result in intervention from politicians hence, experience advocates cautiousness when extending real property tax to local governments.



- ❑ A fundamental requirement when designing a local tax system is to put greater emphasis on the cost-effectiveness of revenue collection.
- ❑ Taking into account not only the costs of tax administration, but the overall costs to the economy, including compliance costs to the taxpayers.

- ❑ As a result of limited revenue base, taxing property may provide a useful source of revenue to local governments.
- ❑ It is important that local governments are vested with the power to collect property tax in order to enhance their accountability to the local community.
- ❑ Decentralization by most governments that has seen transfer of certain powers and responsibilities to local governments, necessitates for the need to fiscally empower these governments cannot be overemphasized.

## **7.0 REAL PROPERTY TAXATION, TANZANIAN EXPERIENCE:**



### **7.1 History of Real Property Taxation in Tanzania**

- ❑ The imposition of property tax in the United Republic of Tanzania goes back to the colonial period when various forms of hut and house taxes were levied.
- ❑ Powers to levy property taxes are provided under the Local Government Finances Act of 1982 and the Urban Authorities (Rating) Act of 1983 which sets out the modalities for the rating exercise itself.

### **7.2 Legal frame work**

- ❑ Under the Local Government Finance Act, 1982, a local government may levy flat rate Real Property tax through issuing of local by-laws approved by the Minister responsible for the local government administration.
- ❑ In its simplest form, a flat rate property tax system would apply a single tax amount on each ratable building.
- ❑ The rating system although simple to administer would create inequity given the differences in size, location, and the value of properties within a jurisdiction.

- ❑ The flat rate system is used in Tanzania for buildings that are not yet valued.
- ❑ The flat rate system has evolved to introduce a number of adjustments which differentiate the flat rate by size, property use and location.
- ❑ In addition to flat rate, the local government, may levy a special rate (betterment tax) to cover the costs of special capital work schemes like new streets, upgraded side walls etc; which only benefit the owner of the property.

- ❑ The Urban Authority (Rating) Act of 1983 stipulates that all properties should be valued according to the open market value or the replacement cost adjusted for depreciation.
  
- ❑ In Tanzania Real Property tax is applied to buildings only, categorized into four basic groups:
  - Residential,
  - Commercial,
  - Industrial and
  - Hotels.

- ❑ Within each category there are three sub-categories of building types, each within an established range of costs per square meter.
- ❑ A separate category is established for site works with a percentage of adjustment applied to the basic cost figure depending on the quality of the site works.
- ❑ In addition, four depreciation adjustments are prescribed on:
  - the physical condition,
  - functional obsolescence, and remaining economic life of the property.
  - further provides allowable depreciation rate of 25 per cent.

- ❑ In Tanzania, land is not taxed under the property rating system because it belongs to the State.
  
- ❑ Exemption to tax is granted to:
  - property personally occupied by the President,
  - properties used for public utilities or public worship,
  - public libraries and museums,
  - cemeteries and crematoria,
  - civil and military airdromes,
  - sporting facilities,
  - railway properties and
  - any such properties as prescribed by the Minister responsible for Local Authorities to be tax exempt.

### **7.3 Problems affecting Real Property Tax Administration in Tanzania and its Impact on Equity:**

#### **□ Inconsistency in valuation/assessment of properties**

- Due to various factors the property tax system in Tanzania is affected by a number of problems particularly,
  - The inconsistency in valuation/assessment of properties,
  - Time lag between valuations,
  - Lack of effective statutory rates of property tax, and
  - Overall inadequate property tax administration.
- The combination of these factors becomes and creates inequities in the country's property taxation system.

- For the property tax to be effective it requires a proper valuation system. This is a key to both horizontal and vertical equity consideration.



- ❑ For lack of properly valued properties, people feel inequitable burden distribution.
- ❑ Under the current system, some properties are taxed based on valuation rolls, and others on flat rate.
- ❑ It is also common to find properties of different sizes and quality subjected to same rate, threshold.
- ❑ It is a challenge that all properties are properly and timely valued and assessed. This in turn creates equitable, fair and uniform assessment factors which are prerequisite of the tax equity cardinal.
- ❑ The system of valuation is a challenging area in Tanzania, notably, due to lack of sufficient financial resources and enough valuers to perform valuation.
- ❑ The result of this being failure to achieve horizontal equity where equals are treated equally.

### ❑ **Time lag in Valuation**

- ❑ The property tax law in Tanzania requires that revaluation of properties be undertaken after every five years to depict the correct market value as well as the additional value due to various improvement on those properties.
- ❑ This is not what is on the ground, as constructions and improvement are missing in the existing valuation rolls.
- ❑ Hence resulting into most of assessed properties paying tax below their realistic amounts relative to their market value leading to vertical inequities in our property tax system.
- ❑ Long time lag in valuation also not only causes inequity in property taxation, but is equally a big source of revenue leakage which negatively impacts the revenue collected from source.

## ❑ **Unrealistic Tax rates**

- ❑ Consideration of effective tax structure in property taxation is very essential.
- ❑ Most cases local authorities tend to set tax rates that are unrealistically low and have little regard to the actual cost of valuation and other areas of administration.
- ❑ In addition, minimum and maximum taxes for particular classes or sectors of property are inappropriately set.
- ❑ If nominal tax rates remain at low levels then any gains made in terms of new valuations, will be negated, as the improvements will have little revenue impact in real terms.

- ❑ In order to reflect the fact that such properties are intensive users of local government services and should therefore pay more.
- ❑ A further argument in taxing such sectors is the legal right for the owners of commercial/industrial enterprises to set property taxes off as a legitimate business expense for purposes of calculating income tax liability.
  
- ❑ **Untapped/not registered Properties**
  - ❑ Inequitable property taxation is also found in terms of taxing only the identified properties captured in the valuation roll and other local government registers.
  - ❑ Property owners whose properties have not been identified and registered safely escape the property taxation.
  - ❑ The growth of cities and towns does not match with the property valuation rolls nor is the pace for valuation of new properties match with the said urban growth.

- ❑ As a result of unregistered properties the property taxation coverage base is very low.
- ❑ This problem besides creating discrimination among payers is also a source of lost revenue.
- ❑ For example in Dar es Salaam region which has three Municipal Councils a property valuation Report made in March 2011 showed that out of 572,405 properties, 330,928 properties were valued equivalent to 58% as detailed below:-

## REAL PROPERTY TAXATION, TANZANIAN EXPERIENCE....Cont



Zone	Estimated No of Properties	Valued	Not Valued	Valued Total
Temeke A	116,301	48,108	68,193	41%
Temeke B	53,628	65,682	7,622	123%
Kinondoni A	160,096	104,531	68,868	65%
Kinondoni B	101,650	58,756	42,894	58%
Ilala	140,740	53,851	86,889	38%
<b>Total</b>	<b>572,405</b>	<b>330,928</b>	<b>241,477</b>	<b>58%</b>

**Source Prime Minister's Office Report**

### ❑ **Inadequate property tax administration system**

- ❑ An effective property tax system is considered necessary in addressing issues pertaining to a country's property tax policy.
- ❑ Administration of property tax should address issues like realistic tax rates, appropriate exemption and relief measures, assessment and revaluation frequencies.
- ❑ Because of inadequacies in property tax administration, it is common to find delinquent taxpayers left unpunished or least punished. Hence, compliant taxpayers feel unfairly treated.

- ❑ In an ideal situation real property tax administration should oversee a uniform, fair, transparent and rational taxation of real property. The principles of an adequate property tax administration system are:-
  - Regardless of ownership, all property shall be taxed.
  - In principle, taxable persons shall be the owners of real property.
  - The revenue from real property shall remain with the local government authorities.
  - The method for tax base (i.e. market value) determination shall be uniform.
  - Tax rates shall be realistic.
- ❑ In Tanzania the main problems are:
  - ❑ exemptions from payment of the property
  - ❑ different methods for determination of tax base between valued and flat rate (unvalued) properties, late service of tax bills and low compliance in general.
- ❑ The above problems significantly contribute to inequity in property taxation. In order to address the inequity in the property tax we intend to focus on the following:



### **Taxpayer Education:**

The eventual taxpayers must be kept well informed of their likely liability, rights and obligations.

### **Sustainability**

Must develop a property tax systems and administrative procedures that are sustainable overtime.

### **Capacity building and capability**

There is need to build capacity and capability of the tax administrators including the property valuers.

### **Realistic tax rates**

Consideration should be given to the tax rate structure such that the rates are realistic.

### **Valuation and collection**

These should be the two main driving forces within a property tax administrative system.

### **The need for IT technology**

Use of IT technology should be emphasized and encouraged.

### ❑ **Mismanagement of exemption and reliefs**

- ❑ Lack of transparency in terms of procedures and basis for property tax exemptions and reliefs to eligible persons cause dissatisfaction among the paying public.
  
- ❑ Some property owners apply for relief and exemption on pretence of inability to pay, are in fact well to do people and are not supposed to receive relief from payment of real property tax.

## 7.4 REAL PROPERTY TAX REVENUE USE AND IMPACT ON COMPLIANCE



### 7.4.1 PROPERTY TAX REVENUE USE

- ❑ Property taxes are an appropriate local government's revenue source owing to the connection between services funded at the local government level and property taxes.
- ❑ In real situation property tax is like a benefit tax because the taxes approximate the benefits received from local government services.

- ❑ The general duties and functions of local government authorities include the following:
  - Maintenance of law, order and good governance;
  - Promotion of social and economic welfare and well being of all persons in their areas.
  - Furtherance of economic and social development in their areas.
  - Effective collection and proper utilization of resources.
  - Implementation of national and local policies.
  - Consideration, regulation and coordination of development plans, projects and programs so as to ensure more beneficial development and mobilization of productive resources to combat poverty, diseases and ignorance and for the improvement of agriculture, trade and industry.

## **Water and Sanitation:**

- ❑ The Central Government agencies are responsible for the provision of water and sanitation in planned areas of towns while local governments are responsible for implementing water and sanitation programmes in peripheral urban areas.
- ❑ The services in almost all the local government authorities is not satisfactory due to inadequate resources.

## **Roads:**

- ❑ Local authorities are responsible for management of district urban and feeder roads from Road Fund collections made by the Central Government and their own resources to develop and maintain roads.
- ❑ However, resources available are too little compared with the enormous task. This leaves poor roads in many areas.

## **Education:**

- ❑ Provision of primary education is the responsibility of local governments with funds from the Central Government and for the provision of schools infrastructure and maintenance, books and stationary.
- ❑ General observations indicate that there is inadequate physical infrastructure, human resources, books and stationery. Local governments in Tanzania have little resources to invest in education.

## **Health:**

- ❑ Local governments are responsible for the provision of health services at the level of district hospitals, health centres and dispensaries, including construction and maintenance of infrastructure. There is noted lack of good and adequate infrastructure and drugs.

### **Waste Management:**

- ❑ Local governments are responsible for management of liquid and solid waste that originate from various sources such as households, industrial and business premises.
- ❑ Due to limited resources they cannot undertake all processes of proper waste management.

### **7.4.2 Services Provision Impact on Real Property Tax Compliance:**

- ❑ Voluntary compliance on Property Tax administered by local government authorities in Tanzania is low generally.
- ❑ Property tax compliance was high where services and infrastructure which had been rehabilitated under the Urban Sector Reform Programmes (USRP).
- ❑ However the current service levels are straining voluntary compliance because many people are not happy with infrastructure and services provided in their areas.



- ❑ Taxpayers also suspect that the local tax revenue is diverted to other activities that are not of benefit to them or misused.
- ❑ They claim that they receive little in return for what they pay. This in turn results to resistance to pay the taxes.

## 8.0 CONCLUSION

- ❑ Although Real Property tax is seen as the most important autonomous revenue source of most local governments across the world it is highly under-utilized in most local governments.
- ❑ Little emphasis is put in Real Property tax collection by most central governments besides the glaring fact that it is a good and stable source of revenue and vital in their resource mobilization strategy.
- ❑ As a mainstay of local finance source of revenue Real Property Taxes are besieged by a host of problems in developing countries; like low yield and stagnancy and inconsistently.
- ❑ Developing local governments have to address the problem of:
  - ❑ loss of property tax revenue due to low assessed values
  - ❑ non valuation of properties,
  - ❑ wide scope of discretion in assessments,
  - ❑ gross disparities in tax assessments and
  - ❑ realistic tax rates to compensate for narrow base which induce evasion and create inequity.

# Thank you



## For Your Attention