



**British Columbia
Assessment Authority**

Real Property Taxation

A Summary of Three Alternative Systems

- **Poll Tax (Community Charge)**
 - **Proposition 13**
 - **Land Value Taxation**
-

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Preamble

In British Columbia our real property assessment/taxation system meets most of the criteria of an ideal taxation system.

In this paper, we describe how alternative taxation systems that have been implemented compare against criteria for an ideal system.



Poll Tax (Community Charge)



Introduction

The United Kingdom is a parliamentary democracy which includes four countries: England, Scotland, Wales and Northern Ireland. Although the structure of local government in each country is unique and independent of one other, their principal source of revenue (until 1989 in Scotland, and 1990 in England and Wales) had been generated from rates or property taxes. Such rates, in general, were based on annual rental values payable by the occupier of the property rather than the property owner.

Following years of turmoil and debate, the rating system for residential properties was abolished in favour of the Poll Tax. Non-residential (business/commercial/industrial) properties continued to be taxed, but instead of being taxed at a locally-determined rate, they would now be taxed by way of a national rate.

The Poll Tax Defined

In its original form, the Community Charge System was a simple concept which would create a direct link between the local authority services and the electorate. In reality, it turned out to be one of the most administratively cumbersome and complex tax-collection systems ever devised.

It focused primarily on three areas:

- The Grant System — Transferring money from central to local governments was to be completely revamped. In addition, the proportion of grant would be cut or reduced.
- The Non-residential Property Tax — This tax was to be retained, but would be transformed into a national tax. Non-residential properties would be revalued between 1988 - 1990, and a uniform national tax rate would be applied across the country. The proceeds from this "collection fund" were then to be distributed to local jurisdictions on a per capita basis.

- The Residential Property Tax — This tax would be abolished and a "community charge" or "poll tax" would be introduced in its place.

This paper deals primarily with the replacement of the residential property tax (domestic rates) by the "community charge" or "poll tax" as it was dubbed by opponents.

Introduced in 1987, it was originally intended that every person 18 years of age and older pay a levy to the local authorities.

Was the Community Charge System a Viable Alternative?

We now know that the Community Charge System was a failure (reasons for its failure will be outlined further in this paper). Still the question which remains to be answered is: Why the Community Charge System was even considered.

In Great Britain the development of the Community Charge System was driven mainly by the following key factors:

- Rapidly rising property values which created inequities due to infrequent revaluations.
- When revaluation did occur (Scotland, 1985) residential property values increased much more rapidly than commercial/industrial values.
- No variable tax rates were introduced to cushion the tax burden shift to residential properties.
- Rental values were difficult to determine due to a lack of rental comparisons (the incidence of owner-occupied residences in Great Britain was 75 per cent — the highest in Europe).
- The central government wanted to reduce local government autonomy and increase their accountability to the local electorate.
- The prime minister steadfastly vowed to abolish domestic rates and sought ways to wrest control from local government. (In many cases, the origins and authorities exercised by local governments pre-dated British Parliament.)



- While the ratio of property taxes to gross domestic product is typically 2.5 to 3 per cent, in Great Britain it grew to 4.3 per cent by 1986.

Why the Poll Tax Failed

First and foremost, the United Kingdom was unsuited to a Poll Tax System. While some nations have regulatory and data collection agencies to track their populations, the United Kingdom did not. For example, there exist no national population registers, nor personal identity cards, nor any local list from which a credible population base could be set and tracked.

Use of the electoral roll had been considered. Unfortunately, not everybody in Great Britain over the age of 18 is listed on the roll, nor does the registry track residents in a given area. The voters' list did not include people such as aliens, and failed to record residents moving in and out of an area; instead it provided only a snapshot of voters at a given period of time. In addition, the accuracy of the electoral roll was questionable. Finally, in terms of political strategy, the government wanted to avoid using the voters' list because it did not want to be seen as imposing a tax on the right to vote.

It appeared from the outset, the Poll Tax would fail. So much of its success was dependent on developing and maintaining accurate and reliable population recording and tracking databases. One might argue that if a sound database had been in place, the Poll Tax might have worked.

Comparison with an Ideal Tax System

It is important to evaluate the criteria which makes for an ideal tax system. This paper reviews five key points which should be addressed and satisfied before a tax system is implemented. They are:

Ease of Administration

In theory the Poll Tax was to reduce the previous system's typical levy charges from 400 to 160 pounds sterling per annum. It was proposed that decreases would be achieved in two ways:

- by spreading the tax burden over 36 million people vs. 15 million property owners/occupiers. (Remember the Poll Tax was a tax levied on all persons over the age of 18, not just the property owner.)
- by saving administrative costs incurred in the reassessment process.

It was immediately apparent that the Poll Tax would prove to be an administrative nightmare. As noted earlier, the lack of accurate, up-to-date registries and data collection systems was a difficult hurdle to overcome. In several counties, 30 to 60 per cent of the population had either failed to register, or had not been billed for the Poll Tax.

Accountability

Increased accountability was presented by the proponents of the Poll Tax as a positive feature. They argued that the new Poll Tax would make local governments more accountable to the local electorate. Proponents of the new scheme also argued that there would be an immediate reduction in local government spending. They felt administrative charges would be significantly reduced. In practice, the exact opposite occurred.

It is important to note that under the Community Charge System, to gain a stake in local government activities, even the poor (including vagrants, street people, the homeless) would be required to pay the poll tax. The system was to be seen as equitable. Therefore, in order to work around this problem, the government opted to provide money to the poor so that they could pay their share of the tax. Welfare rates were immediately increased.

Not unexpectedly, this "flow-through" tax assistance scheme introduced some interesting administrative and collection problems. Immediately on the heels of its implementation, the alleged advantages of the Poll Tax were quickly debunked.



For example:

- in its first year of inception, local authority tax bills jumped 30 per cent. This was a phenomenal increase which burdened both taxpayers and government.
- spending during 1990 immediately increased. It rose 6 to 7 per cent over the national rate of inflation.
- during 1991, the central government moved to reduce the Poll Tax by approximately 1/3.
- to finance local grants, central government increased the value added tax from 15 to 17.5 per cent. Citizens were burdened with Poll Tax levies in addition to increases to the value added tax.

With the implementation of the new system, local governments now relied on the central government for 86 per cent of their financing.

Local governments did become more accountable, but not to the electorate. Instead they became increasingly accountable to the central government. In addition, local governments became relatively ineffective. They had little opportunity to provide input into developing policy and procedures; still they incurred large administrative costs to implement the Poll Tax.

Neutrality (or Economic Efficiency)

The Central Charge System also created its share of problems for the central government. It was burdened not only with accountability and procedural concerns, but also with huge increases to its administrative budget. There were no winners in the new scheme. Both local and central governments experienced difficulty implementing the program and meeting the financial costs the new system placed on them.

Since every person over the age of 18 was to pay the Poll Tax, it was argued by proponents of the new system that there would be no incentive for taxpayers to behave differently — after all, public media campaigns presented it as a neutral tax.

Unfortunately, the people did not agree. Opinion polls showed that only 25 per cent of the population approved of the Poll Tax scheme. In general, they felt the program was unbalanced, inequitable, and unfair. People did not like the charge; not only the poor, the agitators, or the left-wing, but also the middle class and wealthy citizens with a conscience.

The United Kingdom exploded. Its people protested vigorously and rioted in the streets. People simply refused to pay the tax. At one stage, there were over three million actions before the British Courts for non-payment of the Poll Tax. Clearly the Poll Tax was not a neutral tax.

Equity or Fairness

The Poll Tax proved time and time again to be an inequitable tax. For example, it did not make allowances for:

- wealth or the taxpayers' ability to pay. Huge subsidies had to be provided to the poor to pay their share of the tax. This resulted in increased administrative costs to increase the welfare benefits, but of course, the poor did not benefit from the increases.
- the level of benefits received was unbalanced. (In short, the Poll Tax became a day-tax. This meant that persons residing in a local area — for as short as one day — would be liable to pay that locale's poll.)

The Poll Tax resulted in reduced levies on the wealthy (eg., couples living in mansions) and raised levies placed on the middle and lower class (eg., large families living in rental accommodation.)

Clearly the Poll Tax was neither fair, nor equitable.

Can it be Understood

In its basic form, the Poll Tax could be understood. But once varying levels of grants from the central government were applied (in addition to the host of rebates, exemptions, and multipliers), the understandability quickly deteriorated. It



turned into an overburdened and complex system; difficult to understand, open to interpretation, and impossible to administer.

The speed with which the Community Charge System was developed and then implemented resulted in not only inaccurate policy interpretations, but also inequitable levies. Further, critics charged that the distribution of grants from the central government to certain local areas unfairly reduced the Poll Tax in communities that strongly supported the central government.

The Canadian Experience

As late as 1962, the Poll Tax was used in seven Canadian provinces. It was abolished in British Columbia in 1957, in Alberta in 1958, in New Brunswick in 1967, and with the exception of Newfoundland and Saskatchewan, the remaining provinces abolished the tax in the 70's.

By most provincial governments, the Poll Tax was seen as being out-of-place; an unworkable alternative in today's economic and political climate.

Ontario expressed, "It is an anachronism in modern society. We believe that the province should abolish the poll tax as a local revenue source."

New Brunswick commented that, "This is the first tax which should be rejected by all levels of government ... the poll, as a form of taxation, has been almost completely rejected by much of the western world."

Only Newfoundland continues to use some form of Poll Tax to supplement provincial grants to schools. Saskatchewan, although it carries legislation granting government powers to impose the Poll Tax, has not implemented the tax.

Summary

For many taxation jurisdictions, the immediate rise and fall of the Community Charge System

in the United Kingdom has reinforced the importance of scrutinizing new taxation and revenue collection systems. Before a system can be presented as a viable option and replace existing taxation systems, government must:

- be confident that a better system has been developed.
- anticipate whether public response will be neutral (or at least not undesirable).
- be seen by the public to be a fair and equitable system.
- be clearly understood, easy to put into practice, and not open to interpretation nor political influence.
- be administratively sound and cost-effective. Ideally, administrative costs should decrease or remain the same.
- be accountable to the local electorate. The implementation of an alternative scheme and the administrative powers should remain with local governments.

What is in the Future for the United Kingdom?

The British government is proceeding to reimpose residential property taxes, but based on market values, rather than rental values.

Called the "Council Tax", it is hoped that this taxation system will replace the unpopular and unworkable Poll Tax.

Still in the development stage, it has been proposed that the appraiser will determine the approximate value based only on exterior inspection. Each building would then be placed within a prescribed "band of value". The upper part of the band would have a cut-off of 160,000 pounds sterling. Discounts would be available to single-person households.

Proposition 13



Introduction

In the late 1970's, a large majority of American states adopted property tax reform measures. In 1978 and 1979 alone, 37 states reduced their property taxes. Although the property tax is a seasoned veteran that has survived many direct and indirect assaults, in the last decade it has been maligned by both political and social groups.

The most recent and significant round of attacks in the United States have been forerun by Proposition 13, a constitutional amendment that both sharply limits property tax rates and radically changes the tax structure in the State of California. Proposition 13 has been described as a tax that "resembles a structure designed by a mad architect, erected on a shaky foundation by an incompetent builder, and made worse by the well-intentioned repair work of hordes of amateur tinkerers."

Still the impetus for similar property tax reforms continue in the United States. In the fall of 1991, 15 states had initiatives on the ballot which would reduce property taxes.

Background Information

It is important to note that property tax reform in the United States has been affected to a great extent through state referendums and initiatives.

In a referendum, the state legislature refers a proposed piece of legislation to the electorate, whose decision may or may not be binding. Under the initiative system, a measure must be included on the ballot if a specified number of voters petition for its inclusion. If the electorate endorses the initiative, it automatically becomes law.

The move to implement Proposition 13 in the State of California was driven by the following factors:

- rapidly rising real estate values in the 1970's and an efficient assessment system which kept assessments up to date.

- no significant reduction in tax rates to compensate for increased assessments. The combination of dramatic property value increases and fixed tax rates resulted in whopping increases in property taxes.
- a large state surplus, which made it possible to replace property tax revenues with increased transfers to local government.
- voter resistance to a shift in property taxes from non-residential to residential properties (residential values increased more rapidly.)
- legislative processes that encouraged local initiatives.
- public dissatisfaction with government inefficiencies and overspending, particularly in the areas of welfare and social benefits.

Proposition 13 Defined

With the introduction of Proposition 13, California abandoned the concept of current market value assessment in favour of a dual assessment system.

The new system provided for assessments based either on a property's value as of March 1, 1975, or its market value at the time an ownership change occurred. Aside from this dual assessment concept, Proposition 13 contained several other important features.

Proposition 13 ruled that:

- a maximum tax rate on real property was not to exceed one per cent of full cash value. (The previous tax rate state-wide had been about 2.65 per cent.)
- taxes imposed by both state and local government authorities would be limited (i.e., it required a two-thirds approval vote at each house of the legislature to increase or to impose new state taxes; two-thirds of the voters in the qualifying electorate area had to approve any increase to taxes, or the addition of a new local or special taxes; and it



forbade any new ad valorem taxes on real property, or sales taxes on the sales of real property.)

- real property would be reassessed at its full cash value when an effective ownership change occurred. (Since initial inception of Proposition 13, many exemptions, exclusions, and base value transfer rights have been introduced.)
- properties that were not sold during the year would have their base assessments' inflation indexed to a maximum of two per cent per annum. There is no limit on decreases. (Inflation in California has exceeded two per cent every year since 1978 with the one single exception — 1986.)
- recently built properties would be valued at market value; once construction was completed they would be subject to the two per cent rule (see the above point.)
- new bonds, or other debts, could not be retired through the property tax even if they were approved by voters.

Shortly after Proposition 13 became law, growing opposition was reduced and averted. Interest groups were appeased through granting a number of exemptions, exclusions and base-value transfer rates.

Exemptions

Exemptions to the program covered circumstances such as:

- new construction following a governor-declared disaster.
- certain active solar energy systems with a sunset clause of January 1, 1991.
- new improvements for seismic safety.
- new fire-safety improvements.

Exclusions

Exclusions to the program covered circumstances such as:

- the acquisition of replacement property

(where the owner had been displaced by various expropriation proceedings.)

- various inter-spousal transfers.
- transfers of the principal residence between parents and their children (preferential property tax rights can now be inherited!)
- transfers of the first million dollars of full cash value of real property (other than the principal residence) between parents and their children.

Transfers

Under certain circumstances, property owners can transfer existing low assessed values to a new property.

Transfers of a base-year value from one property to another were permitted under the following circumstances:

- when a property is damaged or destroyed in a disaster and replaced by another property in the same county.
- when a person 55 years of age or older transfers his or her principal residence and, within two years, acquires a residence of equal or lesser value in the same county.

Other Changes

Other changes to the newly introduced proposition included the removal of the value-restricting feature on certain classes of property (e.g., state assessed utilities, open-space farmland, timberlands, and taxable municipally-owned properties), and the introduction of new laws which provided that property tax revenues be allocated among competing local governments.

Essentially the allocation was to be based on each local government's share of the prior year's allocation. A complicated process when one considers:

- different growth rates in various areas.
- varying levels of market transactions resulting in varying incidents of revaluation.



- various levels of service provided in different areas.
- the phenomenal growth in the number of tax-rate areas — from 27,207 as of March 1, 1978 to 49,008 as of March 1, 1988. (Many of the tax-rate areas resemble security-walled subdivision cities which are insulated from the general population and the environment.)

Comparison with an Ideal Tax System

It is important to evaluate the criteria which make for an ideal tax system. This paper reviews five key points which should be addressed and satisfied before a tax system is implemented. They are:

Ease of Administration

The proponents of Proposition 13 apparently believed that Proposition 13 would streamline the assessment function. The assessor would simply identify property transfers from recorded documents, obtain the sales price of sold properties, identify new construction from building permits, and obtain construction costs from contractors. At first glance, this administrative process appeared to be quite sound.

Taxpayers on the other hand are an innovative group, and California assessors quickly found that the information they needed to identify an ownership change could be extremely difficult to secure. Loop holes began to surface. Properties began to be transferred without effecting an ownership change.

The Appraisal Journal wrote "clever and resourceful real estate practitioners devise many ways to transfer property without affecting a change of ownership that would set off the reassessment machinery of Proposition 13." Several examples of this were: sale-lease-back transactions, innovative financing, under the table payments, and interesting marriages, divorces, and adoptions.

Another interesting problem for assessors was, how to distinguish between new construction requiring reassessment and minor repairs or maintenance activities that did not. A survey of 44 counties revealed that only 50 to 60 per cent of building-permitted construction triggered reassessment.

Ronald Welch, Assistant Executive Secretary of the California State Board of Equalization announced that, "county appraisers have been swept into a non-professional backwater that affords little opportunity to make professional judgements. Proposition 13 has diverted untold thousands of hours of efforts ... from productive service to a legally necessary but futile effort to cope with an inequitable tax system."

One of the results of changing the structure of the system from one based on value to one based on legality was frustration and stress for the professional appraiser. The number of appraisers employed in assessment work throughout the state dwindled from 2100 to 1550 while at the same time, the need for lawyers grew astronomically. The administrative problems grew. California's *Property Taxes Law Guide* now devotes twenty-three pages to changes in ownership, while only four pages are dedicated to a definition of new construction.

Accountability

It was found that the allocation formula developed to distribute property tax revenues among the multitude of tax-areas violated California's constitutional principle of *tax situs*. This principle mandates that property tax revenues remain in the jurisdiction in which they originate.

The new system failed to inform the taxpayer where his or her property tax dollars went, and limited the ability of local authorities to service the needs of property owners in their jurisdiction through increased property taxes.

In addition, the substantial reduction in property tax revenues increased local governments' dependence on state subsidies which led to a substantial loss of local autonomy and depleted the state treasury.

Further, tax areas bearing low assessments



could receive or demand a larger quantity or quality of local services than they would have enjoyed had they borne the full cost of the incremental services.

Scenarios like this made local government focus on getting a bigger share of the pie rather than on the efficient provision of service. As a result, local governments were forced to introduce a host of alternate taxes and fees to offset property tax revenue losses (e.g., hotel and motel occupancy taxes, utility user's fees, construction fees and taxes, payroll taxes, franchise fees, and parking taxes.)

Proposition 13 has been described as a tax that "resembles a structure designed by a mad architect, erected on a shaky foundation by an incompetent builder, and made worse by the well-intentioned repair work of hordes of amateur tinkerers."

Neutrality (or Economic Efficiency)

Proposition 13's dual assessment concept (i.e., assessments based either on a property's value as of March 1, 1975, or its market value at the time an ownership change occurred) created two types of incentives for property owners.

First, homeowners were discouraged from selling their property because:

- higher property taxes realized by the purchaser, were capitalized into a lower selling price.
- the vendor (unless he or she was 55 years of age or older) faced higher tax levies on his or her next property purchase.

In effect, Proposition 13 continues to deter people from changing residence. Statistics indicate that approximately 44 per cent of owner-occupied residences did not change ownership between 1978 and 1991.

Likewise, businesses (particularly property-intensive firms) experienced this type of "lock-in" effect. In many cases, this continues to immo-

bilize existing business enterprises and has created a property acquisition barrier for new businesses entering the market.

Further, reduced property taxes did not have a neutral impact on the housing market. On the supply side, local governments imposed various fees, charges, and regulations on home builders and developers. Such charges significantly increased housing costs. Coupled with lower turnovers in existing housing, the supply of both new and used housing declined.

On the demand side, lower taxes and a permanent restraint on future taxes increased the demand for housing in an already tight housing market. One need not be an economics graduate to know that decreased supply and increased demand results in higher prices to the consumer.

Second, property owners found non-conventional and innovative ways to dispose of property without setting off reassessment mechanisms. For example, in California, it is legal for one adult to adopt another. Therefore, if a vendor adopts a purchaser and then sells to him or her property valued at one million dollars, the purchaser will realize a tax savings of ten thousand dollars per year.

Equity or Fairness

At least one attempt has been made to measure equity levels in the Proposition 13 System. A 1987 disparity ratio study (i.e., a sales-assessment ratio) in the state county of Contra Costa found a value-weighted average disparity ratio of 3.08 for commercial properties and 3.20 for residential properties. This means that properties which were sold and reassessed in 1987 bore assessments and taxes at a rate three times higher than inflation indexed properties.

It soon became apparent that inequities in the system, when they occurred, could be extreme. The Times Colonist reported that a 980 square foot home in Los Angeles was levied a higher tax than a 7,800 square foot mansion in Beverly Hills.

To re-emphasize, Proposition 13 basically shifted property tax from a current-value assess-

ment basis to an acquisition-based assessment system. Essentially voters traded off tax equity for a greater certainty about future property tax burdens. Inequities in the scheme began to result from the length of time property had been held (or conversely reassessment avoided), and the rate at which property values rose in relation to the two per cent limit.

Can it be Understood

Given what we already know, it would be difficult to argue that California's real property taxation system can be *easily* understood. Local finances in California have been described as being "an incredible maze."

Unfortunately, the system fails as a financing instrument. Revenues generated by Proposition 13 are insufficient — the State of California finds that it is unable to maintain the functions of local government.

The many services enjoyed and expected by Californians have been placed in jeopardy. As late as August, 1992 reports confirm that California's 1978 initiative (Proposition 13) has halved local taxes, but in the process has also hobbled government.

Summary

Two objectives: to decrease property taxes and to forecast with greater certainty what the future property tax burden would be, have been met. Proposition 13 is therefore, a success.

On the other hand, when evaluated against the principles of "what is a good local tax scheme", Proposition 13 is an utter failure.

However, Proposition 13 is firmly entrenched. It has been suggested that "there are now so many vested interests in the system that it may be expected to survive almost anything except a raging inflation that exacerbates the inequities beyond sufferance."

The final report of the Tax Reform Advisory Commission, issued in 1985, stated that: "Although Proposition 13 creates certain inequi-

ties and harm to the California economy, and Proposition 13's key limits on property taxes can be achieved in better ways, the existing system is presently not perceived by the public to be unfair."

This perception was sharpened in a homeowner's appeal to the United States Supreme Court. In *Nordlinger v. Lynch*, Stephanie Nordlinger challenged that taxes on her house (purchased in 1988) were five times greater than those paid by her neighbours.

While recognizing that the Proposition 13 tax system "frustrates the American dream of home ownership for many younger and poorer Californian families", Justice Harry Blackmun dismissed Nordlinger's appeal in June 1992 because nothing in the Constitution made it illegal.

Property tax reform measures continue unabated.



Land Value Taxation

*(Site Value or Graded Value
Taxation)*



Introduction

Land Value Taxation (also referred to as the Site Value or the Graded Value Taxation) is a taxation scheme which in principle values only land; all capital improvements are exempt.

Early forms of the land value concept suggested that the land component of property would be taxed as though it were in its original or natural state. The early system did not recognize the addition of improvements. This concept may be ideal for a new country, but as nations begin to develop, the sales of "original" lands and the availability of unimproved sales evidence diminish.

Background Information

Proponents of Land Value Taxation extol its theoretical virtues, but in practice the scheme has experienced some downfalls. As a consequence, advocates have generally abandoned pure land value taxation in favour of Graded Value Taxation. The graded system taxes improvements to property, but does so at a lower rate than land.

Today, there continue to be situations where advocates argue that Land Value Taxation is feasible. For example, the system may be effective in:

- developing countries (to break up large holdings of vacant land held by private land owners or state agencies.)
- decaying city centres (to encourage redevelopment to the highest and best use — e.g., the rebuilding of slums, and under-utilized commercial areas.)

Land Value Taxation has been applied in Canada, New Zealand, Australia, South Africa, Jamaica and some cities in the United States of America. Its disadvantages and relative merits continue to be argued. It is interesting to note, that after 135 years of use, New Zealand's central

government moved to abolish Land Value Taxation in 1992.

Comparison with an Ideal Tax System

It is important to evaluate the criteria which make for an ideal tax system. This paper reviews five key points which should be addressed and satisfied before a tax system is put into practice. They are:

Ease of Administration

Land Value Taxation maintains some of the advantages of total property assessment. The system's taxation levies cannot be easily avoided, and it contributes to local government autonomy. However, beyond these two advantages, several administrative problems have been encountered. For example:

- In many areas there is a scarcity of vacant land sales. It can therefore be difficult for appraisers to produce accurate and defensible land values.
- A greater number of appeals have been generated on the question: What constitutes land versus improvements? The higher incidence of tax on land value almost certainly attracts an added appeal burden as property owners seek to have the improvements they make to their land assessed as "improvements."
- Subject to statutory requirement, land is valued either on the basis of its existing use, or its highest and best use.

If valued on existing use, speculators could under-utilize the land and avoid incremental taxes. If valued on the subjective criterion of highest and best use, a large number of appeals could be generated because invariably the assessor's view would be at variance with the views of the property owner.

In built-up areas, where value often deter-



mines land use, appraisers receive some guidance to help them determine highest and best use. But again, it can be difficult to find vacant land sales for valuation purposes. Conversely, in largely undeveloped areas, existing use normally determines value. This results in disjointed land values, endless appeals, and complaints from property owners.

Accountability

Generally, a land value system will favour all properties with a lower than average ratio of land value to building value. For example, if the average land-to-building ratio is 50 per cent, properties with a less than 50 per cent ratio will enjoy a tax advantage.

This can lead to accountability problems because sites which are equally valued, but which accommodate different building structures could pay a disproportionate share of the tax burden (i.e., mansions would pay proportionately less than cabins.) Therefore, those receiving the larg-

est proportion of services may in fact not be paying their fair tax share.

It is interesting to note that in New Zealand, where three rating systems exist (i.e., land value, full market value, and rental value), a survey indicated that Land Value Taxation was favoured by property owners who had:

- larger residences.
- apartments.
- industrial land on which large expensive buildings had been erected.
- improved commercial land that housed buildings which had five or more stories.

Not surprising, the survey confirmed that taxpayers, in general, favour a system that shifts the tax burden from themselves to someone else.

Neutrality (or Economic Efficiency)

A positive argument for Land Value Taxation is that it may increase the incentive to improve property. As noted earlier, improvements are taxed at a lower rate than land, as opposed to full value assessments where owners would be assessed similarly on improvements.

Still, if Full Market Value Assessment was a disincentive to improve property, one would expect developers and homeowners to build smaller and less expensive homes. Instead, the opposite is true. Statistical data (i.e., information on 30 years of housing starts) confirm that single family dwellings have grown in size, complexity, expense, and feature more custom design work.

This phenomenon would therefore suggest that the impact of the tax on improvements is not significant when weighed against pride of ownership and social pressures (e.g., the trendy "needs" and "wants" of the yuppie generation.)

A host of incentives are introduced by either not taxing, or only partially taxing improvements. Proponents argue that Graded Taxation (an offshoot of Land Value Taxation) encourages both new development and efficient land use, especially in urban areas. If the tax is significant (i.e., if it outweighs other market considerations) this would be true, but today's socially minded generation places greater value on parks, heritage buildings, and low density developments.

If the tax is significant enough to encourage high density improvements, clearly it would be non-neutral because it would be encouraging the development of projects which realize the highest rate of return in the shortest period of time. The downfall of this is that short-term land use would lead to serious long-run problems (e.g., less open space; and fewer parks, heritage buildings and single-family dwellings.)

Therefore, the allocative efficiency of land value tax schemes may provide short-term advantages in periods of normal economic growth, when it has been applied in a consistent manner by all taxing jurisdictions. Conversely, because land value tax bases could prove unstable in

The impact of the tax on improvements is not significant when weighed against pride of ownership and social pressures.



recessionary or boom periods, long term growth in land tax areas might occur at the expense of stagnation in adjoining areas with different tax bases.

Equity or Fairness

The concept of Land Value Taxation is inequitable. It creates winners and losers. As noted earlier, in situations where the ratio of land to improvement value is lower, those owners would win.

Further, a New Zealand study found that a rating system based on Land Value Taxation failed to make a correlation to income or the ability-to-pay.

Consider two properties. Improvements to one property include a shopping centre. There are no vacancies; the shopping centre is full. Next door, we find a similar site which has not been developed. Under Land Value Taxation, both properties would be valued at the same rate and be assessed the same tax burden, even though the shopping centre property enjoyed a substantially higher income. Given that wealth is a component of ability-to-pay, in this situation, employing the Full Market Value System would appear to be more appropriate.

Changing business cycles also show that land is a considerably more volatile component of value than buildings or improvements. Often tax fluctuations, caused by land value volatility, are perceived by taxpayers to be a poor reflection of changes to their ability-to-pay, or to the benefits they receive.

Ironically, if Land Value Taxation did achieve higher levels of new construction, the tax base generated would be insufficient to offset the service demands of the user. This is because the new construction would be partially or fully exempt.

Can it be Understood

Pure Land Value Taxation is relatively easy to understand. Because the system does not recognize the addition of capital or labour improvements, assessors also found that it was relatively

easy to implement.

Unfortunately, the system was unable to address increased costs in services. It failed to make provision for changes to property (improvements) which placed a greater burden on available government services. Revenues generated by the system could not keep pace with economic influences.

Although Land Value Taxation can be understood, it does not satisfy all the criteria which make for an ideal tax system.

Canadian Experience

In Canada, Land Value Taxation (also called Site Value Taxation) was widely used from 1903 to 1918 in the western provinces. Site Value Taxation was introduced because it was purported to meet the following objectives.

- It broke up large tracts of unimproved land held by absentee owners.
- It prevented land speculation.
- It encouraged the construction of buildings.

In Canada, New Zealand and Australia, it was generally agreed that Site Value Taxation was a workable system, basically because it met objective #1 — it broke up large tracts of land holdings. New Zealand took the system one step further. The tax was made progressive relative to land area (i.e., as the amount of land held by one owner increased, so did the tax rate.)

If it met the first objective, it failed on the second. Site Value Taxation was in place during one of the greatest land speculation periods in Canadian history. Whether the system met Canada's third objective — encouraged the construction of new buildings — that is arguable.

Other interesting historical points to note are:

- In Edmonton, during 1918 to 1920, a local income tax was introduced to make up a shortfall resulting from a 50 per cent drop in revenues from a land only tax levy. Effective 1918, Edmonton added improvements to the property tax base to stabilize tax revenues.



- Graded Value Taxation still exists in many municipalities in the prairie provinces. Buildings are assessed at varying percentages of assessed value and land is assessed at 100 per cent.
- In British Columbia, Graded Value Taxation continued until 1978. Prior to 1978, improvements were assessed at 75 per cent value; land was assessed at 100 per cent value.
- Also in British Columbia, legislation providing for separate valuations of residential land and buildings was introduced in 1989. It is interesting to note that this legislation was repealed in 1992.

which have contributed many years of sustained growth, the appropriate long-term use of land, and the development of high-quality construction.

Therefore, for British Columbians, neither Land Value Taxation nor its surrogates (Site and Grade Value) offer significant benefits.

Summary

Land Value Taxation offers no advantages over the Full Value Taxation System.

The best argument for valuing land at a higher level than improvements has been to encourage rapid development. On the other hand, it has also been argued that a lower tax rate on land and a higher tax rate on improvements could slow down development and thereby preserve heritage buildings and park space. Unfortunately, there is no conclusive evidence to support either argument.

The tax rate imposed under Land Value Taxation is insignificant. It cannot overcome market factors such as availability of financing, provincial or federal grants, labour market conditions, and levels of foreign investment. If government opted to impose a suitable levy — substantial enough to overcome the market factors that have been identified — it would be regarded as confiscatory and would unquestionably be rejected by property owners.

British Columbia is neither in the early stages of development (there exist no large holdings of land which need to be broken up), nor are cities beset with slum areas (which could benefit from redevelopment.) The province continues to experience healthy market conditions. Conditions