

Separate Land and Building Valuation Systems for Taxation?

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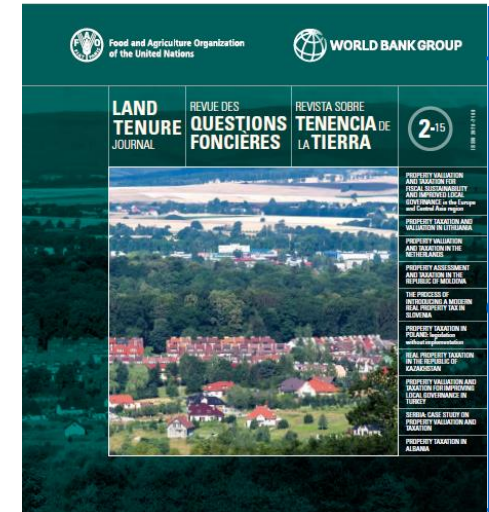


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Pre-conditions for value-based property taxes; FAO and WB Study 2015

- **Active and efficient** property market with **significant numbers** of properties traded each year
- Market is **transparent** in which the prices can be discovered.
- **Comprehensive register** of properties
- **Characteristics and attributes** of properties are recorded
- **Valuers exist** who are able to estimate the market value of properties in a consistent and accurate fashion



<http://www.fao.org/3/a-i5429t.pdf>

Finnish Property Tax Valuation Reform

- Aims to simple, understandable and transparent method and values
- Mass valuation hybrid
- Dualistic approach
 - National Land Survey provides tax values for land
 - Building reconstruction cost valuation outsourced (periodical, ad hoc)
- Land values analyzed from registered transactions and condominium price index
- 6000 value zones accessible via eGovernment portal.

Summing Built Property and Building Site Values

- Key problem: How to divide real property values to land and building values that originate from property transactions
- Standalone built properties doable - plenty of building site sales data available
- Condominium building site sales an issue, not enough sales
- Apartment sales plentiful, but their relation to land value is 'higher science'
- According to Peltola (2018) building site represents 20-30 % of an apartment value, but with a problematic level of fluctuation in high value locations 15-55 %
- Office building sales data negligible making 'land valuation' hard

Finnish Recurrent Property Tax Approach

- Land and building tax values separated in Finland, land valued from transaction prices and building values from reconstruction costs
- Most real properties have same tax rate for land and buildings, only housing properties have different rates for land and buildings
- What is the point for dividing land and building value for an office or retail property? 'Full' property values would be available from property sales.
- Housing land is taxed higher than buildings, but is it necessary? Unique tax rate would remove the need for separate values. It would be a simple and understandable tax.
- Re valuation, the low number of land sales is a real challenge in all other than housing properties.

The Real Deal are Apartments

- Apartments the center of property markets, but they are not subject to tax
- Instead the building and building sites are taxed leading to quite some science in valuation to project land and building prices from apartment sales
- Taxation values of apartments mostly divided per area of apartment in relation to the entire condominium floor area. Higher value apartments per building benefit with de facto lower tax rates.
 - Apartments in the same condominium can sell for example 4000 € or 6000 € per SQM. 1 % recurrent tax results to 1,25 % 'real' tax rate to the basement apartment and 0,83 % to the penthouse with skyline view
 - In comparison, an income of 4000 €/m results to 30 % income tax, and 6000 €/m to 40 %.
 - Income tax is progressive, but the recurrent property tax obviously regressive!

Mass Property Taxation Valuation

- Average land values analyzed from sales and quality parameters
 - Individual deviations ignored apart from area parameter
- Buildings broken to reconstruction parameters, which are multiplied with average cost norms. Age discounts applied according to building type specific formulas
 - Quite some building detail information is required, and collected from owners based on a request.

Approach Credibility?

- As system deviates from property market values to 'science' the result of is of no use to owner – it only benefits the tax man (i.e. Municipalities)
- Produced values are only valid for tax and do not help e.g. public leasing, land acquisitions or mortgaging
- Property tax is a pure wealth tax in Finland
 - Notably in comparison, the VAT acceptance rate is high, as purchasing is a 'choice', voluntary
 - Instead, the way property tax is applied has issues with equity and in clarity and the setup adds little value. It's quite unpopular tax.
 - History shows how people change behaviour to minimize property taxes (narrow houses of Amsterdam as a sample, or small windows in other jurisdictions)
 - What makes sense to the owner, may lead to unwanted consequences for the State
 - Our article in the main Finnish Newspaper led to comments on 'having to burn down non valuable buildings to avoid unfair building taxation'

Remove Issues and Produce Benefits

- Popular property tax requires
 - Visible benefits to the tax payer (schools in US)
 - Equal and just tax burden
 - Tax to match societal values
 - Transparent and understandable valuation methods and values
- Move away from
 - Higher science valuation that nobody understands or can defend
 - Tax man taking the tax payer for granted
 - High collection costs
- Credible property tax is transparent and market value based and up to date. It produces values that benefit multiple purposes and not only taxation, and it treats tax payers equally and fairly.
- If this can't be met, other taxes maybe more acceptable to public.

Many thanks for listening

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