

2 Strengthening property taxation in Asia

Recurrent taxes on property can be an important source of revenues, especially for local government. This chapter shows the level of revenues these taxes generate across Asia and it examines the base of these taxes as well as how they are administered. It then identifies constraints on recurrent property taxation in the region and options for how these limitations might be overcome.

Domestic revenue mobilisation is essential for achieving the United Nations' Sustainable Development Goals. If properly administered, property tax can be a significant revenue source, especially for local government services (Bahl and Bird, 2018^[1]; Bahl, 2009^[2]). However, the revenue potential of the property tax in lower-income countries in Asia can only be captured if the tax is well designed and properly implemented. Poor valuation practices and weak enforcement can compromise their potential. This chapter¹ focuses primarily on recurrent property taxes in the 24 member states of the Asian Development Bank (ADB) with a population of more than 2 million. Most of the remaining member states are micro or small island states and many of them do not, as yet, levy a recurrent property tax.

Property tax systems in Asia

This section examines property tax systems in Asian economies with specific reference to recurrent taxes on property. It considers these systems from three angles: the revenues these taxes generate; the base of these taxes and the valuation methods employed; and administrative arrangements for these taxes.

Revenues from property taxes in Asia

A regional comparison of property taxes (broadly-defined²) shown in Table 2.1 demonstrates that property tax revenues are less important in the Asian region than in the European Union (EU) and the OECD. At the same time, however, country comparison within the region shows there is significant heterogeneity among economies when looking specifically at recurrent property taxes (Table 2.2).

Table 2.1. Property taxes as a percentage of GDP in different regions, 2014-20

| Region | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|--------------------|------|------|------|------|------|------|------|
| EU (27) | 1.0 | 1.0 | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 |
| OECD (38) | 1.3 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 |
| Africa (23) | 0.1 | 0.1 | 0.1 | 0.1 | 0.2 | 0.2 | 0.2 |
| Asia-Pacific (19) | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 |
| Latin America (25) | 0.5 | 0.5 | 0.5 | 0.5 | 0.4 | 0.5 | 0.5 |

Source: (OECD, 2022^[3]), OECD Global Revenue Statistics Database (accessed 26 December 2022); for EU (27): Data from the Government Finance Statistics (IMF^[4]) supplement the missing data for EU countries of Croatia, Cyprus and Romania.

For many of the region's low- and middle-income economies, the ratio of recurrent property taxes to GDP is quite low: the average ratio for the 20 economies remained close to 0.3% of GDP from 2014 to 2019 before increasing to 0.37% in 2020. Considering tax revenues in Asian economies average about 15% of GDP, revenues from recurrent property taxes are not a major contributor to overall revenue mobilisation. For high-income countries in the region, the ratio of recurrent property taxes to GDP was about three times higher: the average for Japan, Korea and Singapore was 1.23% in 2020.³

Remarkable exceptions are Central Asian economies. Economies such as Georgia, Kyrgyz Republic and Kazakhstan have a higher ratio of recurrent property tax to GDP than other low- and middle-income economies in Asia. This is partly because of their centralised administration system. In those economies, valuation is a centralised function whilst the other administrative functions are handled through a system of decentralised tax offices (McCluskey, 2016^[5]). In addition, many of these countries have invested heavily in developing their land and property cadastres, ensuring more comprehensive coverage of properties.

Table 2.2. Recurrent property taxes as a percentage of GDP in selected Asian countries, 2014-20

| Country | Income Level | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|------------------|---------------------|------|------|------|------|------|------|------|
| Afghanistan | Low income | 0.10 | 0.10 | 0.00 | 0.00 | .. | .. | .. |
| Armenia | Upper middle income | 0.39 | 0.46 | 0.47 | 0.47 | 0.42 | 0.39 | 0.40 |
| Azerbaijan | Upper middle income | 0.32 | 0.39 | 0.39 | 0.35 | 0.31 | 0.34 | .. |
| China | Upper middle income | 0.68 | 0.69 | 0.69 | 0.69 | 0.67 | 0.61 | 0.57 |
| Georgia | Upper middle income | 0.79 | 0.85 | 1.01 | 0.97 | 0.99 | 0.96 | 0.88 |
| India | Lower middle income | 0.01 | 0.01 | .. | .. | .. | .. | .. |
| Indonesia | Lower middle income | 0.22 | 0.25 | 0.38 | 0.42 | 0.35 | 0.34 | 0.45 |
| Kazakhstan | Upper middle income | 0.47 | 0.55 | 0.45 | 0.47 | 0.48 | 0.46 | 0.44 |
| Kyrgyz Republic | Lower middle income | 0.55 | 0.53 | 0.52 | 0.49 | 0.49 | 0.48 | 0.47 |
| Lao PDR | Lower middle income | 0.11 | 0.11 | 0.08 | 0.08 | 0.12 | 0.12 | 0.11 |
| Mongolia | Lower middle income | 0.23 | 0.38 | 0.44 | 0.47 | 0.43 | 0.41 | 0.41 |
| Myanmar | Lower middle income | 0.02 | 0.02 | 0.05 | 0.05 | 0.01 | 0.03 | .. |
| Nepal | Lower middle income | .. | .. | .. | .. | .. | 0.00 | 0.99 |
| Pakistan | Lower middle income | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Papua New Guinea | Lower middle income | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Philippines | Lower middle income | 0.34 | 0.35 | 0.33 | 0.37 | 0.36 | 0.36 | 0.39 |
| Thailand | Upper middle income | 0.24 | 0.24 | 0.23 | 0.25 | 0.23 | 0.22 | 0.04 |
| Timor-Leste | Lower middle income | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | .. |
| Uzbekistan | Lower middle income | 1.03 | 0.97 | 1.03 | 1.01 | 0.97 | 0.88 | 0.72 |
| Viet Nam | Lower middle income | 0.04 | 0.04 | 0.03 | 0.03 | 0.03 | 0.03 | 0.03 |
| Average | | 0.31 | 0.32 | 0.32 | 0.32 | 0.32 | 0.30 | 0.37 |
| Japan | High income | 1.91 | 1.85 | 1.87 | 1.86 | 1.87 | 1.91 | 2.00 |
| Korea, Rep. | High income | 0.75 | 0.75 | 0.75 | 0.78 | 0.82 | 0.92 | 1.03 |
| Singapore | High income | 1.07 | 1.04 | 0.97 | 0.93 | 0.91 | 0.93 | 0.65 |
| Average | | 1.24 | 1.22 | 1.20 | 1.19 | 1.20 | 1.25 | 1.23 |

Source: (IMF, 2022^[4]), IMF Government Finance Statistics (GFS), 2022; (OECD, 2022^[3])OECD Global Revenue Statistics Database; (World Bank, 2021^[6]).

These findings raise important questions. Is there extra revenue space for recurrent property tax, especially in low- and middle-income economies in the region? If so, what are the policy and administrative challenges preventing them from exploiting this potential and what can policy makers do to address these challenges?⁴

Tax base and valuation method for recurrent property taxes in Asia

As with other taxes, the tax base, rate, and exemptions mostly determine the expected revenue from recurrent property taxes. Concerning the tax base, a significant difference observed among Asian economies is whether or not they tax buildings⁵ as well as land⁶. Most economies tax both land and buildings (Bahl et al., 2010^[7]; Almy, 2014^[8]; Radvan et al., 2021^[9]; McCluskey, Bahl and Franzen, 2022^[10]) because doing so expands the tax base and may be perceived as fairer. Some countries have implemented more complex bases by using more than one recurrent tax base (China, Philippines and Viet Nam).

The valuation of taxable items is important for property taxation because the fair value of real estate is not always directly observable. Also, the usage of the property may be considered, as residential use is usually less profitable than commercial use. Table 2.3 categorises property tax systems in developing Asia with reference to different valuation methods.

Taxable value may depend on various considerations. Some prefer to base it on cadastral value or book value, not on market price. Cadastral values are normally more closely related to area-based approaches given that the method of assessment is prescriptive and formulaic. An adjusted area basis is widely used

in Caucasus and Central Asian economies. Underdevelopment of the real estate market, which limits the references for market price, is often the justification for non-value-based approaches.

While fair valuation is important in property taxation, it is often too costly to assess taxable property individually. Individual valuation of taxable property increases the administrative costs required and, as a result, makes it difficult to conduct reassessments on a sufficiently regular and frequent basis (Slack and Bird, 2014^[11]). In part responding to the criticism, some countries have adopted a banding system for evaluation (Plimmer, McCluskey and Connellan, 2002^[12]). A banding system assigns properties to broad categories rather than evaluating each property. It is based on a robust estimation of property prices rather than a precise individual valuation which reflects limited administrative capacity. However, as all properties within the same band pay the same tax, it is likely to exhibit some regressivity.

A non-market-price-based approach is typically preferred when property markets are not liquid enough to provide sufficient information about the market price of individual properties. Other reasons to opt for this approach are: (1) insufficient valuation capacity within government; (2) incomplete registration of title transfers of properties; and (3) low reliability of the transfer price due to under-declaration (UN-Habitat, 2011^[13]). The most common non-market price methodology is to base valuations on size (McCluskey et al., 2012^[14]). Countries that use area-based approaches, such as India and Tajikistan, often adjust the assessment for specific characteristics, such as population of the municipality, building condition, property use and depreciation, to proxy market prices and enhance the fairness of the tax (Rao, 2008^[15]).

Table 2.3. Recurrent property taxes in Asia: Bases and assessment approaches

| | | |
|---|---|---|
| Capital value of land and buildings (improvements) collectively | Land and buildings are valued as one distinct indivisible property. Functions effectively where there are ample open market sales data. | Cambodia, Georgia, India (Mumbai), Mongolia, Nepal |
| Separate values for land and buildings | Common in former socialist countries, and low- and middle-income countries. | Afghanistan, Armenia, China, Indonesia, Kyrgyz Republic, Philippines, Thailand |
| Land only: capital value-based | This approach only taxes the land and ignores the value of the buildings and other improvements on the land. Adequate vacant land sales data are essential to fairly reflect the capital value especially in urban areas. | Fiji, Papua New Guinea, Solomon Islands, Vanuatu, Viet Nam |
| Land only: area-based | A simple, pragmatic approach in the absence of a land market or assessed values. | China (land use tax); Lao PDR |
| Buildings only | Where land is excluded for ideological, historic or social reasons. | China (real estate tax) |
| Cadastral, normative and balance sheet valuation approaches to land and/or buildings | Formulaic non-market value approaches that apply prescribed methods to determine the assessment. | Armenia, Kazakhstan (non-residential), Mongolia, Turkmenistan (non-residential), Uzbekistan (non-residential) |

| | | |
|--|--|---|
| Rental value of land and buildings (improvements) | This valuation approach is applied when property leasing is the principal form of tenure and there is ample rental data for all types of property. | Bangladesh, India, Pakistan, Myanmar (urban) |
| Area-based with adjustment factors | Typically applied where no formalised real property market exists and market transactions are thin across urban and rural settings. | Azerbaijan, India (Bangalore, Delhi), Kazakhstan (residential), Myanmar (agricultural land), Tajikistan, Turkmenistan (residential), Uzbekistan (residential) |
| No recurrent property tax | Some of these countries have property transfer taxes. | Cook Islands, Maldives, Marshall Islands, Micronesia, Nauru, Niue, Palau, Samoa, Tonga, Tuvalu |

Notes: Some cities in India use capital value, some rental value and others adjusted area as tax base.

Source: Authors' elaboration with reference to (Franzsen, 2009^[16]) and (Almy, 2014^[8]).

Administration of recurrent property taxes

Although revenue from recurrent property tax is mostly attributed to subnational government⁷, administrative structures vary across the region. The arrangements for administering the property tax in the countries of developing Asia differ greatly. For example, in the Philippines, local governments have wide responsibilities for administering the property tax, but in Viet Nam administration involves a multi-agency cooperative arrangement, and in other countries there are other approaches. These varying approaches are surveyed in the 13 country studies in (McCluskey, Bahl and Franzen, 2022^[10]).

In some economies, subnational government is responsible (Afghanistan, Bangladesh, India, Indonesia, Myanmar, Philippines), while in others central government is solely (Armenia, Azerbaijan, Cambodia, Georgia, Kazakhstan, Kyrgyz Republic, Mongolia, Uzbekistan) or partly (Nepal, Papua New Guinea, Thailand and Viet Nam) in charge of administration with responsibility for tax policy and design located within higher levels of government.

Various administration issues are observed for recurrent property taxation (Bahl, Franzsen and McCluskey, 2017^[17]; Norregaard, 2013^[18]; Bahl, Martinez-Vazquez and Youngman, 2008^[19]) even in high income economies. High administrative costs such as ownership identification and periodic valuation are significant challenges to the tax authority, as capacity is often more limited in subnational governments. Emerging technology can provide solutions. Examples include (1) property identification using aerial imagery; (2) billing through e-demand notices or email; (3) payments via online platforms; (4) automated valuation (model-driven valuations using statistical methodologies such as multiple regression); and (5) monitoring by geographic information systems (McCluskey et al., 2018^[20]).

Why are property tax revenues in developing Asia so low?

Uneven development of property taxation is commonly observed in the majority of Asian economies. Taxation has often been constrained by management problems and always influenced by the political economy (ADB, 2020^[21]). Various estimates place collection rates⁸ in the range of 30% to 60%, which is primarily due to weak tax administration, inefficient billing systems, poor record keeping and lack of follow-up on overdue accounts and arrears (Bird and Slack, 2004^[22]; NIUA, 2010^[23]). The weak revenue performance of recurrent property tax in developing Asia is likely due to the interaction of multiple factors.

First, tax bases have been narrowed by exemptions and preferential tax treatments. Thailand, for example, has an initial exemption of 50 million baht (USD 1.4 million) for residential property, meaning that few residential properties are within the tax net. These tax relief packages are rarely reviewed and their revenue costs are rarely monitored but they are widely believed to have eroded the tax base by a substantial amount.

Second, property valuations are often outdated due to non-compliance with legally prescribed revaluation cycles. (Kelly, R.; White, R.; Anand, A., 2020^[24]) reckon that the ratio of assessed value to market value is in the range of 30%-50% in low-income countries, largely as a result of infrequent revaluations. Also, some countries do not rely on the estimation of market values.

Third, central (and state) governments have not provided adequate incentives for local governments to utilise the property tax. In many economies, central governments have been reluctant to shift revenue-raising autonomy to local governments. In other economies, large-scale intergovernmental transfers have disincentivised the use of local property taxation. Centralised fiscal arrangements mean that local politicians are not responsible for unpopular taxing decisions.⁹

Fourth, strengthening property taxation failed to acquire political support against opposing interest groups, voter apathy and rent seeking. Political leaders are required to strengthen their compact with local voters to gain support for enhanced property taxation (van den Boogaard et al., 2020^[25]; Moore, 2015^[26]).

Fifth, improvements have caused a significant backlash in many countries. Examples include effective rate roll backs in the aftermath of revaluations in Kuala Lumpur, Malaysia and the adoption of fractional assessment practices in the Philippines. Fractional assessments, otherwise known as assessment levels, are used as a policy to reduce the tax liability. They are widely used in the Philippines but also in Cambodia and Korea. For example, in the Philippines, the assessment level for residential property ranges from 10%-60% of the market value of the property.

Exemptions and preferable tax treatments may reduce taxpayer opposition. However, it is noteworthy that successful revaluation practices in Hong Kong, China and Singapore have avoided such compromises but kept effective tax rates low.

How can developing Asia improve property taxation?

A holistic review of administrative efficiency is essential for regional developing economies to raise more revenue from recurrent property taxation. Raising rates without fixing the issue of narrow tax bases would likely worsen the distortions and compromise support for the property tax. To increase efficiency, the government can expand the tax base by ensuring all liable properties are registered in a cadastre. Second, simplifying tax payment processes and incentives for taxpayers can optimise tax collection. Third, the introduction of market value-based assessment will likely expand the tax base in many economies. In addition, it can increase the size of the tax base and its elasticity in many countries. For economies with non-value-based property tax, adoption of value-based property tax is a common basis for those potential enhancements even though the transition may require extra administrative capacity. The tax can be more revenue productive even though additional investments in valuation will be required.

Pakistan's experience provides a good example of a comprehensive property tax reform. The modernisation of the urban immovable property tax involved improving administrative capacity, which suffered from outdated manual processes, paper-based records, poor collection, and a small tax base. The project began in 2014 with the development of a GIS-based administration platform utilising satellite imagery along with a mass property data collection. Digitisation of records, automation of systems and field surveys to validate records added over half a million new taxable units to the tax base.

Market value-based valuation and periodic revaluation are essential to achieve an efficient property tax regime in countries with strong tax administrative capacity where abundant price data is available for property valuation. For lower-income countries with limited capacity, a simplified value-based banded system, objective assessment adjustments, or value zones can be an alternative, although they leave a significant space for further improvement. Property tax reforms recently undertaken in Sierra Leone demonstrate that moving from a value-based system (rental value) to one based on the size, location, condition, use, etc. resulted in improved revenue performance (Grieco et al., 2019^[27]).

All exemptions and other preferential tax treatments should be regularly reviewed. International norms suggest that the revenue from property tax should at least keep pace with inflation and rising expenditure by local government. Low revenue buoyancy, despite periodic reevaluation, indicates the existence of disproportional tax exemptions and preferential assessments. One way to ensure periodic review of the arrangements is to require re-voting for any extensions.

A simpler taxation would be beneficial to both the government and tax payers. A complex taxation system increases enforcement costs and, when capacity is limited, collection rates decline. Governments can promote tax payments by being transparent with taxpayers as to how the associated revenues are used and by penalising the delinquents.

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Notes

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² ‘Broadly-defined’ property taxes also include property transfer taxes, stamp duty, as well as estate and gift taxes.

³ Similarly, the high-income jurisdiction of Hong Kong SAR (China) also raises close to 1% of GDP from recurrent property taxes.

⁴ These questions are addressed in (McCluskey, Bahl and Franzen, 2022^[10]).

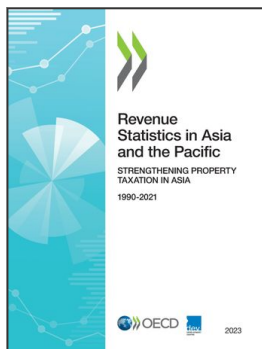
⁵ The tax base sometimes includes plant and machinery or personal property (e.g. boats).

⁶ In Fiji, Papua New Guinea, Solomon Islands and Vanuatu, land is the only tax base (Franzsen, 2009^[16]) as is the case in Viet Nam. In China, separate taxes on land and buildings exist (McCluskey, Bahl and Franzen, 2022^[10]).

⁷ There is large variation in the extent to which local government expenditures are financed by property taxation in developing Asian countries. This variation is surveyed in the 13 country chapters in (McCluskey, Bahl and Franzen, 2022^[10]).

⁸ Collection rates are calculated as the amount of revenues from recurrent property taxes collected by the government as a proportion of the amount the government billed households and businesses in a given year.

⁹ The diversity of these experiences is reviewed in (Bahl and Bird, 2018^[1]).



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