

Is Land Tax a Real Option for Reform in Northern Ireland?

David Magor OBE IRRV (Hons)

Chief Executive

Institute of Revenues Rating and Valuation



Maintaining Municipal Fiscal Health in Northern Ireland

- Not just an issue for Northern Ireland
- Public expenditure is under immense pressure
- Stable and practical sources of income are the essential foundation
- Taking risks can have serious consequences
- It's too important to be an academic theory

Economic Principles Versus Political Realities

- “Tax policy is the product of political decision making, with economic analysis playing only a minor supporting role” (Randall Holcombe 1998).
- Political pressure to maintain the tax burden at or near its current level (e.g. capping increases) or to favour one group of taxpayers over another (e.g. over-taxation of business) often overrides economics principles.

Inter-Governmental Fiscal Relations

- Fixing local tax rates
- Fixing fees and charges
- Central control or interference
- Fiscal independence
 - Decentralisation
 - Imbalances
 - Equalisation
- Grants
- Assigning revenues

The Financing of Local Services

➤ Types of Expenditure

- Revenue expenditure
- Capital expenditure

➤ Sources of income

- Taxes and levies
- Fees and charges
- Grants and borrowing

Principles of Local Taxation

- Should be related to the ability to pay
- Should be easily understood
- Should be administratively efficient
- Should be difficult to evade and avoid
- Should be impartial
- Should be economically efficient
- Should benefit those who pay

Criteria for Local Taxes

- The choice of taxable subject
- Tax yield should be certain and adequate
- Fit local circumstances
- Local taxes should be a mix of stable and predictable sources such as property tax, possibly land tax, and alternative buoyant sources of income
- Local authorities should be accountable
- Administration and compliance costs should not be excessive

Does Land Tax Satisfy the test of Revenue Adequacy

- Is the tax base too small to generate sufficient revenue?
- Should it be part of the basket of taxes?
- Revenue adequacy depends on:
 - Revenue needs
 - Ratio of land value to total property value
 - How high tax rate can go without subsuming all of the annual land rents

Bringing a Land Tax into the Basket of Available Income Sources

- Linked with the quality of land registration
- Could be part of a larger and more dynamic tax base
- Market value based tax more likely to grow in relation with GDP but the supply of land is fixed
- Is it part of a consistent measure of municipal credit worthiness

Types of Land Value Taxes

- **Site value:** land alone without consideration of privately financed improvements (e.g. drainage)
- **Land value:** land value including improvements (drainage) rather than land and buildings
- **Graded property tax (two-rate; split-rate):** higher rates on land than on buildings
- **Single tax:** site value tax serving as sole source of government tax revenue (Henry George, 1879)

Efficiency of Land Value Tax

- Neutral tax: collects revenue without discouraging investment in new buildings
- Fixed supply of land means land owner cannot reduce the supply of land even if price changes
- Lowering tax on structures will encourage more structures on a given land area thus creating greater density
- Potential problem: greater density would necessitate more infrastructure (e.g. transportation, schools)

Fairness of the Land Value Tax

- As the quantity of land is fixed, the burden falls on the landowner with no opportunity to shift it others
- The owner can't avoid the tax by reducing the supply of land or using it less productively
- Tax falls on landowner – progressive burden

Assessment Methods and Requirements

➤ Methods

- Residual method: assess market value of property and subtract cost of replacing building and improvements
- Allocation method: assumes land values are same % of total value for every property
- Contribution method: Break down sales prices into values contributed by location, plot size, age, etc.; define neighbourhoods with roughly the same land values per acre

➤ Requirements

- Uniform assessments with respect to market value of land
- Frequent revaluation
- Public understanding of assessment methodology

Advantages of Land Value Tax

- Equity - Because the value of land is, for the large part, a result of society efforts rather than efforts on the part of the owner, society should reap the benefit of increased land values through taxing this enhanced value
- Efficiency - In that it removes a market disincentive, which discourages people from building or making improvements to their property because of the fear of increased taxes.
- Under a land value system improvements are essentially exempt.

Advantages of Land Value Tax

- From an environmental perspective land value taxation encourages compact city centre development.
- Administrative simplicity is an important advantage of land taxation.
- By excluding improvements the valuation process is less constrained and demanding
- Land values are easily determined as the valuation process requires less variables to be reflected.

Disadvantages of Land Value Tax

- It provides the taxing authority with a restricted tax base, excluding a substantial degree of wealth, especially in well-developed areas
- It can only produce sufficient revenue with high tax rates.
- Valuing land in a built-up environment with no or few land only transactions, necessitating the extraction of land values from improved value sales, and
- Defending such derived before a valuation appeal tribunal.

Disadvantages of Land Value Tax

- Explaining the system to ratepayers who are generally intuitively aware of the improved values of their properties.
- It does not reflect ability to pay as well as a capital value system
- It can create undesirable development particularly where the planning system is not operating efficiently.

Implementation Challenges

- Less easily understood by taxpayers – they know the value of their property but do they know the value of their land?
- Transition from property tax to land value tax: existing taxes are built into expectations and decisions – where to live, how much to spend on a house, where to place your business
- Smaller number of taxpayers, higher burden problems with distribution of that burden

Implementation Challenges

- Will need primary enabling legislation
- Shifts within and between property classes
- Need considerable political support
- May need to be phased in
- May need to offer tax credits to protect owners of modest properties with high land intensity

Implementation Challenges

- Winners and losers – those whose ratio of land to total property value equal to the average of the jurisdiction will face no change; parcels with above average land % will face increases
- Car dealerships and parking facilities will pay higher taxes; owners of high-rise office buildings will pay lower taxes
- Land values more volatile than improvement values

In Conclusion

- Local taxes must meet local needs
- The yield from taxes must be adequate
- Where possible taxes should be policy linked
- Should be easy to collect, but
- Difficult to evade and avoid, and
- Be fair in every respect
- **In Northern Ireland would a land tax satisfy these criteria?**

In my Opinion

- Introducing a system of land value taxation to replace the current domestic and non-domestic systems would fail
- Introducing a land value tax on vacant land (and agricultural land?) alongside the existing system is worthy of consideration, if only to spread the burden