



**MINISTRY OF FINANCE OF THE REPUBLIC OF INDONESIA
DIRECTORATE GENERAL OF FISCAL BALANCE**

Property Taxes in Selected Asian Countries

Seminar Proceeding

2013



**MINISTRY OF FINANCE OF THE REPUBLIC OF INDONESIA
DIRECTORATE GENERAL OF FISCAL BALANCE**

International Seminar

Challenges to collect Property Taxes

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Seminar Proceeding

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Foreword

Property Tax is considered to be an ideal revenue source for local governments due to its nature and characteristics. The tax object can't quickly move away and is easily visible. With enough discretion, local governments may attract investors for private and corporate objectives. Many developing countries have made significant efforts to design a tax system which is appropriate and suitable for their specific conditions and objectives. Some countries opted for a completely decentralised tax, others for a centralised tax with a revenue sharing scheme. In between, there are several options to assign functions like: valuation, collection or tax rate setting to different levels of government. Indonesia is currently reforming the tax fundamentally by devolving it from a central to a completely local tax by 2014.

Taxing property is a complicated and demanding affair, nonetheless with potentially important leverage for development. Taxing property requires a database of properties, their respective values, owners and geographical data which is constantly updated. Valuation and appraisal of properties is a science in itself and, if not managed correctly, a door-opener for corrupt practices. Not only appropriate equipment is necessary, but also the capacity to manage and update the data. As a result, many developing and emerging nations have not been able to explore property tax revenue optimally. As Prof Govinda Rao highlights in his contribution to this publication, India's share of property tax revenue is estimated at about 0.2% of GDP, compared to an average of 1.9 % among OECD member states. Under the given circumstance, Indonesia's average of 0.5% demonstrates quite a potential.

The Ministry of Finance, Republic of Indonesia, organised an international seminar on challenges to collect property tax, November 27 – 28, 2012 in Jakarta, with the participation of experts from several Asian countries. The purpose of the seminar was to exchange experience and mutually learn on how to deal with challenges faced to collect property tax. This was a great occasion for Indonesia to benefit and to share its experiences and get inspirations from other countries on how to successfully devolve property tax.

The Deutsche Gesellschaft für Internationale Zusammenarbeit, GIZ, supported the Ministry of Finance in defining the objectives, designing the programme and mobilising speakers, panellists and participants from selected Asian countries. The International Tax Compact (ITC) and the Australia-Indonesia Partnership for Economic Governance (AIPEG) financially contributed for this seminar. Experts, academia and practitioners from governments of: Bangladesh, Cambodia, India, Indonesia, Nepal, Pakistan and the Philippines as well as representatives of international development partners, attended the seminar.

This document aims to provide the participants and related institutions with references for further analysis and policy formulation in the area of property taxation.

The active participation, vivid debates, and positive feed-back from the participants are promising indicators for the continuation of this exchange and networking among tax experts and practitioners from the region.

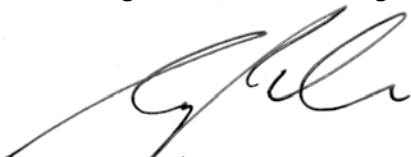
Sincere appreciation to all parties who contributed in finalizing this proceeding, as well as special thanks addressed to the International Tax Compact (ITC) and the Australia-Indonesia Partnership for Economic Governance (AIPEG) for financially supporting this seminar.

Last but not least, thank you to the organizing committee for the commitment and hard work to successfully organize the seminar.

Jakarta, January 2013

Deutsche Gesellschaft für
Internationale Zusammenarbeit
(GIZ) GmbH,
Acting Head of DeCGG Program

Ministry of Finance of the
Republic of Indonesia,
Director General of Fiscal Balance,
Director of Subnational Taxes and Charges,



Tim Auracher



Adjianto



1. SEMINAR PROCEEDING

1.1 Introduction

The international seminar on “Challenges to Collect Property Taxes” was organized by the Ministry of Finance of the Republic of Indonesia with the support of International Tax Compact (ITC), Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH, and Australia Indonesia Partnership for Economic Governance (AIPEG). The seminar was jointly opened by the Minister of Finance of the Republic of Indonesia, Mr Agus D.W. Martowardoyo and Deputy Head of Mission, Embassy of the Federal Republic of Germany, Ms Heidrun Tempel.

Participants from seven Asian countries: Bangladesh, Cambodia, India, Indonesia, Nepal, Pakistan, and the Philippines, attended the seminar. The country paper presentations and discussions were followed by breakout sessions and cross-group sessions to further discuss and elaborate certain important aspects of property tax collections.

The Secretary of Directorate General of Fiscal Balance, Ministry of Finance, Mr Heru Subiyantoro and the Country Director of GIZ for Indonesia and Timor Leste, Mr Ulrich Mohr, jointly closed the seminar.

1.2 Background

Property is taxed in one way or the other in almost every country in the world. It might lead to important fiscal and non-fiscal benefits. The revenue that such a tax produces is often of critical importance to government sub-national levels. Nevertheless, it is also a tax which requires effort, investment and skilled staff to administer and maintain it appropriately. So what needs to be done to make sure property tax can be collected and administered in an effective, efficient and rational manner in order to give maximum benefits to the societies?

Taxing property is a complicated and demanding affair, but with potentially important leverage for development. It requires a database of properties, their respective values, owners and geographical data which should be constantly updated. Valuation and appraisal of properties is a science in itself and, if not managed correctly, a door-opener for corrupt practices. Not only appropriate apparatus is necessary, but also the capacity to manage and update the data.

On the other hand, property taxes can lead to fiscal and enormous non-fiscal benefits. Thanks to the incentive in keeping the properties' data up to date, clarifying the property rights, ownership and property values, much of the necessary investments for land use and urban planning is already provided. Consequently, the professional administration of property tax paves the way for urban and rural development and reduces the risk of speculation on land.

According to the textbook wisdom, property tax should be a local tax – but what do experiences from South-East Asia, East-Asia, and South-Asia tell us? Property tax ideally should be measured as a local tax, considering that the tax base can't quickly move away and is easily visible. With enough discretion, local governments may attract investors for private and corporate objectives. However, local governments normally do not have the same level of skilled staff and performing equipment as the national level administration has. This is especially true in rural areas, where economies of scale may play a role in administering such taxes. So practice may challenge textbook wisdom on whether property tax really should always be a local tax.

Indonesia is one of the countries that follow the textbook wisdom. Since 2011, property taxes (*'rural and urban land and building tax'* and *'land and building transfer tax'*) were devolved from central to local governments (districts and municipalities). Some challenges were encountered during the devolution process, which are being resolved hand in hand by central government and local governments. The success of the devolution lies upon the capability of choosing the right methodology and strategies, while making use of other countries experiences.

To further discuss the issues of property taxation, a two day seminar on "Challenges to collect Property Tax" was conducted in Jakarta, Indonesia on 27th – 28th November 2012. The objective of the seminar was providing opportunities for representatives of public administration from national and sub-national levels, as well as academia from participating countries to mutually learn about good practices and lessons learned regarding property tax. Addressing the issues and exchanging the countries' experiences, could lead the participants to feed-back the conclusions into policy decisions of their respective countries.

Dr Hefrizal Handra, from Faculty of Economics, Andalas University, Padang, Indonesia, moderated the seminar. 99 participants from 7 countries in South-East Asia, East Asia and South Asia, respectively: Bangladesh (4 participants), Cambodia (3 participants), Nepal (6 participants), India (5 participants), Indonesia (52 participants), Pakistan (1 participant), Philippines (3 participants), and development partners: German Embassy, ITC, GIZ, AusAID, ADB, World Bank (25 Participants).

1.3 Opening Session

The seminar was jointly opened by Ms Heidrun Tempel, representing the Ambassador of the Federal Republic of Germany, and Mr Agus D.W. Martowardojo, Minister of Finance of the Republic of Indonesia.



Ms Heidrun Tempel (middle). and Mr Agus D.W. Martowardojo (right) accompanied by the Director General of Fiscal Balance, Mr Marwanto Harjowiryono (left)

1.3.1 Opening remarks by Ms Heidrun Tempel, Deputy Head of Mission, Embassy of the Federal Republic of Germany

Ms Tempel stressed the importance of property taxes as a potential source of local revenues as well as the importance of domestic resource mobilisation as such to finance development. She highlighted the role of ITC; created in 2008 as an informal and action-oriented exchange platform to promote effective, fair and efficient tax systems. This initiative shall contribute to combat tax evasion and inappropriate tax practices on a global scale. The importance of efficient tax systems is best estimated 100 billion Euro lost as public revenue each year due to tax evasion and tax avoidance.

Ms Tempel underlined that taxation does not just provide public institutions with necessary funds for public services, but beyond that it contributes to state building. As taxes engage citizens, taxation leads to claims for more transparency and accountability. According to Ms Tempel, various studies provide robust evidence underpinning this thesis. In this regard for local governments this is especially the case.



Ms Heidrun Tempel

Nonetheless, Ms Tempel drew the attention that managing property tax is still quite a demanding affair, bringing the example of Germany that even after 40 years of experience, continues to struggle with reforming its property valuation system. In conclusion, Ms Tempel highlighted that Germany will continue to be a reliable partner to Indonesia, supporting Indonesia's tax potential and reforming the tax systems, considering as well that the tax reform is also high on the G20 agenda.

1.3.2 Keynote Speech by Mr Agus D.W. Martowardoyo, Minister of Finance of the Republic of Indonesia

Mr Agus D.W. Martowardoyo outlined the importance and inter-linkages among fiscal policy, monetary policy, real sector policy, and balance of payment policy to boost economic development, highlighting that in the area of fiscal policy, the national budget is linked closely with local budgets.



Mr Agus D.W. Martowardoyo

As part of fiscal policy, the fiscal decentralization plays an important role. As a consequence of the political choice in 1999, Indonesia now focuses its fiscal decentralisation policy on the expenditure side

rather than on revenue side. Around one third of the country's national budget goes to sub-national budget in terms of balance fund. In addition, central government provides source of revenues to sub-national governments in accordance to the principle of 'money-follows-function'.

The Minister emphasized that in supporting local own revenue sources, Indonesia has devolved property taxes under local governments in 2010, this regulated in Law 28/2009. The main objective of this devolution is not only to leverage the local tax power but also to reduce high cost economy, due to the excessive local tax collection. Nevertheless a number of challenges arise in many areas of property tax collections, including IT support, property valuations, and the possibility of tax evasion and avoidance. In addition, wide disparities of property tax potentials among regions and low local capacities have been common issues that need special attention. Therefore, these issues need to be resolved systematically.

The Minister considered the seminar as an event helping to mutually learn from the good practices and lessons learned regarding property tax in order to feed-back conclusions into the policy decisions of the represented countries. Since property tax in each country has its own characteristics and challenges, sharing experiences and discussing the issues is a helpful approach to achieve this objective. A regular discussion beyond the seminar in this area would strengthen efforts to improve property tax collection.

The Minister also expressed his appreciation to all participants, speakers, panellists, resource persons, and developing partners including International Tax Compact (ITC), Australia-Indonesia Partnership for Economic Governance (AIPEG), and Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH for supporting and organizing the seminar.

1.4 Presentations and Discussions

Five country papers on the comparisons of property tax collections were presented during the seminar, namely:

- 1) **Challenges to Collect Property Taxes in Nepal**-written by Jyoti M. Pandey, Ram B. Chhetri, and Narayan P. Baskota. The authors are GIZ advisors, Sub-National Governance Program, Nepal; presented by Mr Ram Bahadur AryalChhetri.

- 2) **Challenges to Collect Property Taxes in Bangladesh** - written and presented by Mr M.A. Quader Sarker, Member of Tax Administration & Human Resource Management, National Board of Revenue, Bangladesh.
- 3) **Getting the right mix in property tax policies and administration** - written and presented by Ms Milwida M. Guevara, President and Chief Executive Officer of Synergia Foundation, Philippines.
- 4) **Property Tax System in India: Problems and Prospects of Reform** - written and presented by Mr Govinda Rao, Executive Director of Public Finance Institute, India.
- 5) **Challenges to Collect Property Taxes in Surabaya City** - written by Tri Rismaharini (*Mayor of Surabaya City*) and presented by Mr Suhartoyo (*Head of Local Revenue Office of Surabaya City*). To enrich the understanding about Indonesian Property Taxation, Mr Adijanto (*Director of Subnational Taxes and Charges, Ministry of Finance*) presented the 'Challenges to devolve property taxes in Indonesia' together with Mr Hartoyo (*Director of Tax Extensification and Assessment, Ministry of Finance*) presenting the 'Indonesian property tax reform'.

Each topic was commented by either one or two panellists who also answered and clarified questions or suggestions rose by participants.



*Left to right : Mr. Adijanto (MoF), Mr. Marwanto Harjowiryono (MoF),
And Mr. Tim Auracher (GIZ).*

1.4.1 Property Taxes in Nepal

Property tax is a major title for local governments in Nepal. During fiscal year 2010-11, the property tax revenue constituted 71% of local taxes, 33% of own source revenue, and 7% of the total local government revenues.



Mr. Ram Bahadur Aryal Chhetri and Mr. Rajendra Prasad Pokharel

With the Local Self-Governance Act, 1999, the authority to collect property tax has been devolved to local bodies. Municipalities can levy either Integrated Property Tax (IPT) or House and Land Tax (HALT) and land revenue/tax.

Municipalities have not been able to exploit the revenue potentials fully due to capacity and compliance gaps in property tax collection. There are three broad challenges faced by municipalities in property tax collection, namely:

- *Low capacity*- Municipalities are lacking of adequate human resources (mainly computer skills and revenue projection skills) as well as physical resources (such as computers, software and data backup systems) that lead to out of date tax registration, in-accurate tax revenue projection, and suboptimal effort for tax campaign.
- *Low compliance* - It arises from low willingness to pay taxes and poor enforcement capacity of the local bodies. Tax payers point to the low quality of services in return for their taxes and the general lack of faith in the local governments. While the lack of enforcement capacity has resulted in low penalty for non-compliance and lack of elected bodies.
- *Lack of incentives* - A key issue is the lack of incentives at both individual and institutional levels to address the issues and invest in tax efforts.

- Most taxpayers pay property tax only when they need to access municipal services. While the access to fiscal transfers and development partner funds have provided the bureaucracy with no incentive for tax efforts.

Some recommendations are discussed and proposed to tackle the issues:

- *Capacity building of municipalities* - A systematic capacity development strategy needs to be provided for municipal staffs in many areas including computer skills, revenue projections, taxpayer educations, and tax registration.
- *Boost compliance* - A sustained taxpayer educational program and demonstrating transparency and accountability in order to build the taxpayer's confidence, will raise voluntary compliance.
- *Boost incentives for the local bodies/tax officials* - An effective structure of incentives for both tax officials and taxpayers will increase the tax efforts.

Imposition of a hard budget constraint on certain expenditure titles - It is worth noting that the increasing fiscal transfers and access to funds from the development partners has meant reduced incentives for tax effort while the local bodies do not face hard budget constraints with pressure to deliver services.

1.4.2 Property Taxes in Bangladesh

There is no property tax law in Bangladesh yet. However, there are certain elements of taxes to be included as property tax: the land revenue administered by the Ministry of Land, and wealth tax that is being collected as a surcharge of income. The National Board of Revenue has been trying to impose tax on property, but until now it has not become possible.



Mr. M.A. Quader Sarker

There are ‘pros’ and ‘cons’ of property tax imposition in Bangladesh. Arguments in favour of property tax are mainly on revenue and economic development. A well designed property tax will improve fairness of a tax system and can effectively raise government revenue. It can also enhance economic growth and create significant forward and backward linkages which can potentially reduce economic inequality.

On the other hand, arguments against property tax are mainly on administrative difficulties, such as valuation and accounting difficulties as well as high management costs.

However, due to the following reasons and strategic considerations, imposing property tax in Bangladesh is currently seriously debated as an option:

- In a country like Bangladesh, where income inequality is acute, rural and urban household income and wealth distribution is widely dispersed, a well-designed property tax may yield a number of dividends to the economy.
- To implement a new property tax it needs a gradual transformation of the tax policy through a gradual introduction of this tax with a low rate.
- Technically, to support the property tax administration, it is important to consider the use of an adequate IT system especially for database management, fiscal cadastre maintenance, and tax payment administration.

The challenges that need to be tackled by the government are issues of: ownership identification, the irregularity of assessment, illicit collusion between tax payers and the assessors, and lack of political will to enforce penalties.

If a property tax is to be successfully introduced in Bangladesh, the revenue board needs to carefully consider a wide range of issues ranging from the cost of collection that may override total collection, valuation of property, to the needs of capacity building for the collection authority.

1.4.3 Property Taxes in the Philippines

The underlying theory that “property taxes are not easy to administer and they are not politically popular owing to their visibility” is clearly applied in the case of

Philippines. The land reform program or the distribution of land to tillers or tenants has made identification of taxpayers and collection of the property tax more difficult.

However, some cases of success show that it takes good local governance to make property taxation to work:

- Marikina city case illustrates that the residents are willing to pay local property taxes because they see the benefits in terms of efficient public services.
- Mandaluyong district and Naga city are good examples of how simple computerisation program can minimize irregularities in property valuation and minimise corruption in tax collection.



Ms. Milwida M. Guevara

In the districts, where local capacity is the issue, however, there is a call to re-centralise the property tax to make it more efficient and more transparent.

The main challenges faced in the Philippines looking at the property tax are the lack of incentives and the distortions in the land use due to different tax rates. These “complications” are difficult to administer and it makes property tax a difficult tax to implement, especially in terms of its valuation and in the development of its system of record management. Thus the real property tax is an underperformer in the Philippines.

Some conclusions were drawn from the discussions on property tax in the Philippines:

- In 2008, property tax only contributed 12% to total local own revenues.

- The grant (transfer) system has removed the incentive of local governments to fully utilize their taxing powers.
- The administration of the real property tax has been politicised.
- The power of municipal local governments (or towns) to impose the tax was withdrawn and lodged solely on provincial governments.
- In some provinces, property values have been stagnant for more than 10 years.
- The law mandates a revaluation of real properties once every 3 years but less than one-half of the LGUs in the country complied with the law in 2000.
- People's ability to pay the taxes has reduced.

1.4.4 Property Taxes in India

Theoretically, to have a good public service delivery and local autonomy, it is necessary to have substantive local own revenue sources. In order to link public services to hard budget constraints, property tax is ideal, since its tax object is immobile, stable, and predictable.

In India, states are empowered to deal with all matters related to property tax. Still there are problems: high cost of collection, low capacity, difficulties of valuation, high compliance cost, poor coverage and a poor information system.



Ms. Milwida M. Guevara and Mr. Govinda Rao

Experience from India shows that property tax has not been a significant revenue source for local governments (2011: 0.16 - 0.24 % of GDP). Having different property tax systems in different states, however, recent best practice from Bangalore shows that reforming property tax could lead to significant revenue gains. Among the salient features of the reform is the replacement of the capital value or rental value based taxes with area-based taxation. The rates are linked to the graded valuation depending on the location of the property and the type of construction. Yet, revising the values from time to time could face political problems.

1.4.5 Property Taxes in Cambodia

From the discussions, useful inputs were noted from Cambodian property tax systems:

- Property tax is the main source of tax revenue for Local Governments. However, Sub National Administrations collect the taxes on behalf of General Department of Taxation.



- The collection of *The Cambodian Delegates* property tax was implemented in 2011, and covered Phnom Penh and urban areas only.
- The General Department of Taxation is responsible for administering the proposed property tax, working closely with the Ministry of Land Management, Urban Planning and Construction and the Sub National Administrations.

1.4.6 Property Taxes in Indonesia

Property tax is one of the most feasible local revenue sources. For Indonesia, this is especially crucial given the fact that the fiscal decentralization strategy has been focusing on the expenditure side rather than the revenue side. Local revenue sources have been mostly from the central government as transfer funds.

Indonesia has undergone a number of strategic measures in the property taxation. Starting from 1985, property tax were imposed on land and building as a central tax. The first reform was done in 1994 by enacting Law 12/1994. The system was improved gradually as a mean to increase revenue. The second reform was implemented in 1997 where a new property transfer tax ('land and building transfer tax') was introduced as a central tax, too.

In 2010, the property taxes ('rural and urban land and building tax' and 'land and building transfer tax') were devolved to local governments (districts and municipalities) with 4 years of transition period as stipulated in Law No. 28 Year 2009. Some challenges were encountered in the devolution process, such as huge disparities of property tax potentials over regions, lack of local capacities, and limited local budget.

Facing the challenges, Indonesia has made significant efforts to assist local governments in preparing the collections of property taxes. Related central government units have provided legal assistance, technical guidance, and supporting facilities to local governments. In addition, a road-map for property tax devolution was developed to be used as guidance for related government units to plan strategic measures to ensure that all local governments can collect property tax by 2014.

Surabaya City (2nd largest city in Indonesia) started to collect property taxes in 2011. The city was the first local government to fully collect property taxes.

Using the prototype system, that was originally set up by the Directorate General of Tax (known as 'Tax Object Information Management Systems' or SISMIOP) the city government of Surabaya started to administer local property tax in 2011. Simultaneously, by reforming tax services in 14 areas (registration, land ownership database, rectification, cancellation of land titles, restitution, taxpayer

complaint handlings, etc.), the city has been able to dramatically increase the property tax revenues from IDR 341.7 billion in 2010 to IDR 540.4 billion in 2011 and it is projected to surge to IDR 790.6 billion in 2012. By this increase, property taxes revenue contribute to 51% of the Surabaya local own revenue.



The basic strategies being implemented in Surabaya are basically three-fold: (i) set up the rate that is appropriate for the local revenue potentials, (ii) use ICT to support transparent and objective valuation, and (iii) deal with

Mr. Suhartoyo (Head of Local Revenue Office, City Government of Surabaya), and Mr. Adijanto (Director of Subnational Taxes and Charges, DG Fiscal Balance, (MoF)

public complaints in a professional manner to ensure compliance and reduce tax evasion.

Devolution of property tax collection in most participating Asian countries is still a novelty. For Indonesia, even the system that has been successfully implemented in Surabaya is actually replicating systems that have been initially developed by central government. However, as the object, the tax rate, and all the features of property tax are by nature local, it is important to continue initiatives of decentralising property tax administration. In most Asian countries, property tax is still under-levied for various reasons. In order to create efficient, effective, accountable, and sustainable property tax at the local level, all the effort should be linked with initiatives of Some conclusions can be drawn from the Indonesian experience and the implementation strategy adopted by Surabaya City:

- The devolution of property taxes to local government is a significant tax reform as property taxes are considered to be proper local taxes.
- In the devolution process, local governments should collect property taxes as soon as they can and improve the systems, infrastructures, and human capacities gradually.
 - Central government should provide local governments with adequate and continuous support to enable them to collect property taxes optimally.
 - Considering the large disparities in tax potential over regions and low capacities in some local governments, adopting an asymmetric treatment and option for joint-administration in collecting property taxes are recommended.

1.5 Breakout and Cross-group Sessions

Three working groups were formed to discuss various aspects of property tax collections. The session was followed by a cross group session where a structured and moderated debate went into details on the following topics:

1.5.1 Data Management and IT Support in Property Tax Administration

The case of Bangalore state in India exemplified the role that IT can play in the management of property tax. The existing database and digital maps help to determine rental sales and building fees according to the appropriate zones. This example recommends developing two types of data: data on land and rental prices, and a spatial database using the GIS. By developing these basic elements of data the government of Bangalore has managed to increase property tax revenues from Rs. 4,480 million in 2007 to Rs. 12,000 million in 2011.



*Ms. Anna Marie Furtuito,
facilitating the break out discussion*

From the cases in respective countries, the working group participants compared three aspects in in property tax administration:

- Compatibility:** Are data transferrable between different software for statistical and other purposes?
- Competitiveness:** Is there a low-performing software monopoly?
- Local autonomy:** Can Local Governments decide themselves which software and which service provider they want?

Countries	Compatibility	Competitiveness	Local Autonomy
Indonesia	Yes	No	Yes
India	No	Yes	Yes
Nepal	Yes/No	No	Yes
Philippines	Yes	Yes	No

According to the working group participants, the main challenges faced by Asian countries in using IT for supporting the collection of property taxes are:

- a. **System acceptance:** It is important to ensure that all stakeholders and officials accept the importance of using IT and change the mind-set from manually managing data.
- b. **Capacity building:** It is critical to develop adequate local capacities by training and upgrading them regularly.
- c. **Cost-effectiveness:** Cost of procurement and maintenance of the system have to be proportionate to the benefit in terms of the tax yield and the institutional building at the local level.
- d. **Developing/upgrading a mature system:** It is critical that the local government has to be committed to developing its own system which, however, needs to fulfil two criteria: On the one hand it should be best-

suitable to local needs and circumstances; on the other hand it should have appropriate compatibility with a national IT system.

- e. **Sustainability:** Management of the system (hardware, software) obtained from donors, private sector and central government should be maintained by local governments with their own resources.

1.5.2 The Role of Appraisal/Valuation

Having a sound property valuation system is of key importance for property tax management, because it is the foundation to predict revenue and guarantee objectivity and fairness in taxation. However, valuation criteria and the responsibilities differ from country to country. Some countries for instance split functions of valuation and collection, tax rate setting, between levels of government, others have decentralised all functions to the same level. Participants of the working group agreed that it is better to keep all functions at one level of government to ensure consistency of tax policies.

The working group participants identified several challenges to property valuation by local governments such as a lack of trained staff, joint ownership of properties, uniform definition, and a general irregularity in the assessment of properties.

For better collection of property taxes, there is a need to identify strategic options and methodologies for local governments to deal with valuation challenges. The question is: what criteria should determine value?



Mr Said Rehman, facilitator of the break-out session on property valuation

There are qualitative and quantitative approaches like location (for land) and quality of construction (for constructed property) as in the case of Nepal. In general, there are three types of valuation: *rental based*, *capital value*, and *area based*. However countries without proper property markets face difficulties to set up a reliable valuation system.

The participants also agreed that the cost of valuation always needs to be considered when setting up a system. In the case of Indonesia, no completely accurate valuation for low-value properties is done; instead, such a category of properties is valued through a mass appraisal. For high value properties, more complex valuations methods are used as a benchmark for business purposes.

Another important aspect to increase efficiency in valuation is to classify property, according to regions, type of constructions and according to its use. The challenge is the trade-off between simplicity and fairness to capture accurate values. Thus, when designing the system there has to be an explicit agreement on this trade-off and its consequences.

For example, in Australia the principle of valuation is “expensive houses are on expensive land”, this takes out the complexity. However in developing countries we have to be aware of different aspects. In contrast to Australia for example, houses on the main road are most likely to be more valuable.

The working group participants recommended to continuously collaborating between different countries and regions in order to share experiences and to find the best way to value property. All agreed that there should be devolution of taxing powers to the local level, but not without accompanying and supporting them from central level institutions (“hand-holding”) and through inter-local government cooperation. This will lead to an improvement of accuracy in valuation over time.

1.5.3 Tax Evasion, Enforcement, and Accountability

Tax evasion occurs as the tax payers intentionally fail to comply with tax laws and regulations. Tax avoidance deals with behaviour of tax payers to reduce tax liability by taking advantage of possible loopholes. Avoidance can be legal or

illegal, while tax evasion dealing with not reporting or under-reporting to reduce the tax base is illegal and occurs in almost all countries.

Narwanta's work also has proven that there is tax evasion in property transactions with the following conclusions:

- Individual tax payers, tend to evade more than institutional ones, like companies.
- Residential property transactions tend to evade more than commercial property transactions.
- Agents that frequently do property transactions, tend to evade less than individuals whose property transactions are much less frequent.

The working group participants agreed on some fundamental statements during their discussion:

- Governments should develop ethics of their societies with regards to citizens' duties by increasing pressure and raising awareness for the obligation to pay taxes.
- If people know the benefit of paying taxes, their determination to avoid it will reduce. As tax revenue usually is not earmarked for specific expenditures, people do not know how tax revenue is spent. This reduces their trust.
- Tax evasion and avoidance also is influenced by a country's culture. Corruption and complicated tax systems enhance tax evasion.
- Some measures might be helpful to reduce tax evasion such as tax education, simplification of tax regulations, provision of more accountants, and law enforcement.

The following examples and comments from the participants enriched the discussions:

- In Nepal, the problem is that citizens only want to pay small amount of tax, usually below the official tax rates. For property tax, valuation is

normally done by municipal governments, but in some remote areas it is done by central government. There is one valuation committee in every municipality to determine the price of properties.

- In Australia, the process of data documentation and transaction and also the registration of property ownership play an important role in order to reduce tax evasion.
- In Indonesia, after both sides, buyer and seller, agree on a transaction, they have to go to notary for the documentation and registration. Before finalising the documents, the buyer pays property transfer tax (BPHTB) and the seller pays 'final' income tax (PPh). The minimum price for tax calculation is the officially estimated 'selling price of tax object' (NJOP) set by government.
- In Cambodia, the government determines the price of properties, so all details, including the value of transaction is well known. Nevertheless under reporting of transactions is still a problem.
- In some Indian municipalities, a guidance value is used. A comprehensive list of property and cadastre provides clear information to society. Sometimes the tax formula and also information on how tax revenue has been used is provided. A zoning system which categorises values helps to get a better overview. In case of perceived tax evasion it is quite common that the neighbourhood reports it so that tax officers can recheck property values and taxes due.
- The Philippines apply the assumed marked value to determine a property's value.

Property tax evasion and avoidance reduces revenues and inaccurate property administration. Some solutions that can be considered are (i) having valuation report from independent valuers as a precondition for property transactions, (ii) publishing formally market price data for every area in a region and use this as reference for taxable property values, and (iii) adjusting the selling price of tax objects (as the basis for calculating property tax), if necessary.

1.6 Conclusions

The inputs and discussions led to some general conclusions and lessons learned to improve property tax collection. Most participants considered cooperation among their countries to be valuable for optimising revenue, improving administration, as well as reducing evasion and avoidance of property taxation.



Mr Hefrizal Handra, moderator of the seminar

1.6.1 Lessons Learned

In general, property taxes are collected in almost every country with different ways and approaches. Most countries treat property taxes as local taxes due to its characteristics (visible, immobile) and importance (significant and stable source of revenue and accountability).

Some lessons can be learned from the presentations, discussions, and breakout sessions, such as:

- 1) Property taxes should be completely devolved to lowest level of government.
- 2) It needs political willingness to decentralise property taxes. Lack of capacity at sub-national levels should not be used as a reason for not decentralising the tax. Instead central government has the task to support local governments.
- 3) Local circumstances and challenges need locally adapted solutions. This counts for IT and data management as much as for reporting and valuation matters. Pragmatic approaches sometimes yield better

- 4) Results than following standard textbook approaches.
- 5) Start by a registration of all properties and provide information about land values to the citizens.
- 6) Central government should provide a framework (legal framework, guidelines, capacity building), which makes improvements at the local level possible and provides adequate support to local governments.
- 7) All countries face challenges with regards to data collection, incentive systems and legal issues; the participants formulated some suggestions on how to address them:
 - Every country needs a roadmap, a clear and systematic management plan of property tax implementation.
 - Start with collection rather than spending too much time to set up the system; but be transparent.
 - Educate the public about the reasons for taxing property and potential welfare gains due to additional public revenues.
 - Start from bigger cities (urban areas) to put the scheme together (plan a roughly 2 year process, to train tax administration).
 - Let first evidence of improved public services due to additional public revenue available speak for itself.
 - Publish tax revenue and its use to civil society.

1.6.2 Way Forward

As property taxes contribute significantly to local own revenues, the efforts to optimally collecting the said taxes is crucial. Proper arrangement of tax administration, valuation, and enforcement will be the main determinants for successful property tax collection. Therefore, a continuous sharing of knowledge and experiences among countries can help officials, decision makers, civil societies, as well as academia to improve the management of property taxes in their respective countries.

There are several ideas that need to be considered for the improvement of property tax collection:

- 1) Learn from other countries' practices and experiences to find the best way to value property;
- 2) Encourage practitioners, officials, and academia to make use of the network access for exchanging information and solving any problems in relation with property taxes. A list of the seminar participants is provided at Annex-2.
- 3) Find sources or donors to support regular seminars on the property taxes as a mean to exchange knowledge and experiences.

1.7 Closing Session

The seminar was jointly closed by Mr Ulrich Mohr, GIZ Country Director for Indonesia & Timor Leste, and Mr Hery Subiyantoro, Secretary to the Directorate General of Fiscal Balance, Ministry of Finance. The summary of their closing speeches are as follows:

1.7.1 Closing remarks by Mr Ulrich Mohr, GIZ Country Director for Indonesia & Timor Leste

Mr Ulrich Mohr expressed his gratitude for the excellent organization of the seminar and the good cooperation between GIZ and the Ministry of Finance. He also thanked ITC and AIPEG for their financial supports to make the international seminar happen. In particular; special appreciation was given to the organizing committee for the hard work in organizing this successful seminar.

1.7.2 Closing remarks by Prof Heru Subiyantoro, Secretary to the Directorate General of Fiscal Balance, Ministry of Finance of the Republic of Indonesia

Prof Heru Subiyantoro cherished the speakers, panellists, resource persons, and organising committee for their efforts and hard work to make the seminar a successful one. On behalf of the Minister of Finance, he extended sincere thanks to participating delegations from Cambodia, Bangladesh, India, Nepal, Pakistan,

the Philippines, and Indonesia who engaged in vivid discussions and interesting exchanges.

In brief, Prof Heru Subiyantoro also reiterated some key lessons learned from country presentations and discussions, such as:

- the necessity of including various stakeholders as to overcome challenges (*lesson from Nepal*);
- the challenge to avoid double taxation when setting up a property tax (*as currently assessed in Bangladesh*);
- a reminder that property tax management is first of all a governance issue, requiring awareness of citizens, accountability of public authority, and fairness in taxation (*from the Philippines*);
- the importance of pragmatic approaches and of creativity in tax policies, especially in the context of developing countries (*i.e. designing a property tax in slums as a housing service tax*);
- the fact that much can be achieved if there is just enough willingness (*the case of Surabaya in Indonesia*)

Prof Heru Subiyantoro also appreciated the support from ITC, GIZ, and AIPEG to make the international seminar a real success.



Supporter of the Seminar



The Seminar Participants





2. KEYNOTE SPEECH:

MINISTER OF FINANCE, REPUBLIC OF INDONESIA,

Agus D.W. Martowardojo

MINISTER OF FINANCE OF THE REPUBLIC OF INDONESIA
FOR
INTERNATIONAL SEMINAR ON
CHALLENGES TO COLLECT PROPERTY TAX

Jakarta, 27 November 2012

Assalamu'alaikumWr. Wb.

Good morning,

***Honourable Deputy Head of Mission, Embassy of the Federal Republic of Germany, Mrs. Heidrun Tempel,
Distinguished Speakers, Panelists, and Resource Persons,***

Ladies and gentlemen,

First of all, I would like to invite all of us to convey our sincere thanks and appreciation to God for His blessing and care, which makes it possible for us to attend this seminar on the challenges to collect property tax. I would like also to express my appreciation to ITC, GIZ, and AIPEG (AusAID) for arranging this seminar with the objective of discussing issues on the collection of property tax and the possibility of building a closer regional cooperation in improving property tax administration.

Ladies and gentlemen,

At national level, fiscal policy is one of the main tools for government in order to boost economic development, together with monetary policy, real sector policy and balance of payment policy. As we know, all of those policies are interconnected, therefore we need to maintain those policies are always in one direction and support each other. Fiscal policy itself implemented through revenues and expenditures policies, which has functions of allocation, distribution and stabilization. Within fiscal policy, we always try to maintain our fiscal health, especially to maintain our deficit at the manageable level therefore not to put our economy in jeopardy. As regulated in the Law, we maintain national deficit, which consist of central and sub national deficits under 3% of GDP. In the last three years, Indonesian national consolidated deficit are in a range of 2,5% up to 2,75%. As a result, Indonesia is one of very limited country which able to survive from global financial crises recently and able to maintain the economic growth above 5%.

In addition, the investment grade of Indonesia's credit rating is also a significant achievement of our hard work.

In term of fiscal policy, one key issue which is very important to be maintained is policy on fiscal decentralization. As the consequences of fiscal decentralization policy, one third of National State Budget goes to sub national level. The amount of central transfer to sub national level is always increasing, i.e. in year 2005, total transfer accounted to IDR 150,8 trillions while in year 2013 will amount to Rp528,6 trillion. Together with local tax, those transfers should be spent by sub-national government for improving the efficiency and effectiveness of governance, public services and infrastructure. Such improvements aim to encourage regional economic development thus providing opportunities for improved welfare of all people. It is our expectation that the regional economic development supports the national economic development.

Distinguished Guess,

From the commencement of Indonesia's big bang regional autonomy reforms in 2001, the path of implementation has thrown up many challenges as we seek to meet high expectations. Many of us had pessimistic views to the success of the significant transformation from very centralised to most decentralised government. However, after more than 11 years of implementation, the fiscal decentralization reforms which go hand in hand with reforms to political and administrative decentralization arrangements have been on the right track, though there are some improvements to be considered.

The intergovernmental relation in Indonesia, in general, has been taken to support the public services delivery for the whole government operation in Indonesia. The authority of giving public services mostly to three layers of government which are: central government, provinsi (provinces), kabupaten (rural districts) and kota (municipalities).

In order to support the fiscal decentralization, central government gives the source of fund to sub-national governments in accordance to the money-follow-functions principle. The fiscal decentralization in Indonesia is focused on the decentralization of expenditure side rather than revenue side, this as a consequence of 1999 political choice. Local governments are given the huge flexibility of spending, while

most of their revenue comes from central governments. Since the need of local financing is increasing, central government keeps trying to pursue local capacity especially in the local taxing power and to maintain the improvement on it.

The sustainability of fund has to be supported by increasing the role of local owned source revenue, which especially is supported by the devolution of rural and urban property tax, as regulated by Law 28/2009. The main objective of this devolution is not only to leverage the local tax power but also to reduce high cost economy due to excessive local tax collection.

Local governments have had the right to collect property tax since January 1, 2010. By January 1, 2014 the central government will cease collecting the said tax, regardless of whether local government decides to collect the tax or not. The four years transition period was given to provide enough time to collect the said tax. In year 2011, only the city of Surabaya imposed to collect the said tax. Another 17 local governments followed in 2012. In 2013, 105 other local governments are expected to collect the property tax. The rest of 369 local governments are still in the process of collecting the property tax by January 2014.

Some observations in our experience have shown that a number of issues are still outstanding in the effort of collecting property tax optimally. Property taxes are considered to be an ideal local tax as the tax base can't move quickly and is easily visible. With adequate discretion, in turn, local governments may attract investors for private corporate objectives. Indonesia has followed this argument by devolving property tax to local governments.

In the devolution process, a number of challenges arise. Local governments, in general do not have the same level of skilled staffs and equipment as the national level administration does. This is especially true as seen in the rural areas, where economies of scale may play a role in administering such taxes. Therefore, practice may challenge the above textbook wisdom.

From the administration point of view, there are some issues that still needed to be resolved, such as, the role of IT support in property tax administration. In large number of tax objects, the use of IT systems in property tax administration is necessary, so that, the formulation of an adequate IT strategy requires a substantial effort.

Another issue is the role of appraisal or valuation. In maintaining and increasing the 'willingness to pay', the valuation of property tax should be conducted objectively.

For this purpose, the use of adequate methods of property assessment is required, also the capability of the value human resources capacity to apply a good methodology.

The other issue is the possibility of property tax evasion and avoidance. General practices of tax evasion and tax avoidance need to be identified to find ways to reduce it. The use of an effective method to combat such practices can help to increase property tax compliance.

Ladies and gentlemen,

The above issues on property tax as well as other challenges need to be solved systematically. I believe that property tax in each country has its own characteristics and challenges. By sharing experiences and discussing the issues openly will help us to mutually learn about good practices and lessons learned regarding property tax in order to feed-back conclusions into the policy decisions of our respective countries.

In this two day seminar, a number of experts and practitioners in the field of property tax from various countries of South-East, East, and South Asia, will present the challenges to collect property taxes in their respective countries. It's an opportunity to enrich our knowledge about practices of property tax collection in other countries. In addition, discussions on IT strategy, valuation, and tax evasion will strengthen our efforts for better property tax collection.

With sincere heart I would like to welcome all speakers, panellists, and resource persons from several countries in this region such as Bangladesh, Cambodia, India, Indonesia, Nepal, Pakistan, and the Philippines. I am confident that by working together, we can produce concrete and workable conclusions from this seminar.

Besides sharing experiences, I hope that experts and practitioners areal so able to develop a strong network among countries in this region to continuously discuss and share experiences for the improvement of property tax administration and reducing tax evasion and tax avoidance.

Finally, I would like express my sincere appreciation to all participants who have made time to attend this seminar. Special thanks go to International Tax Compact (ITC) and Australia-Indonesia Partnership for Economic Governance (AIPEG) for having supported this seminar. My appreciation also goes to GIZ for making significant efforts to arrange this seminar. I highly appreciate the efforts of the

speakers, resource persons, moderator, and the committee of this seminar for participating and contributing to this seminar. I hope all these efforts will be blessed by our Almighty God.

By pronouncing *bismillahirrahmaanirrahiim*, I declare this seminar officially opened. Thank you.

Wassalamu'alaikum Warahmatullahi Wabarakatuh.

Minister of Finance
The Republic of Indonesia,
Agus D.W. Martowardoyo

3. COUNTRY PAPERS

ID	Topic	Country / Writer
1	Challenges To Collect Property Taxes In Nepal	NEPAL Jyoti Pandey, Ram Chhetri, & Narayan Baskota
2	Challenges To Collect Property Taxes In Bangladesh	BANGLADESH M. A. Quader Sarker
3	Getting The Right Mix In Property Tax Policies & Administration	PHILIPPINES Dr Milwida Guevara
4	Property Tax System In India: Problems & Prospects of Reform	INDIA Dr Govinda Rao
5	Challenges to Collect Property Taxes in Surabaya City, Indonesia	INDONESIA Tri Rismaharini
6	Challenges to Devolve Property Taxes in Indonesia	INDONESIA Adijanto
7	Indonesia Property Tax Reform	INDONESIA Hartoyo

3.1 NEPAL: Challenges To Collect Property Taxes in Nepal

(Jyoti M. Pandey, Ram B. Chhetri, and Narayan P. Baskota)

Abstract

The Local Self-Governance Act (LSGA) 1999 devolved the authority to collect property tax to local bodies – districts, villages and municipalities - in Nepal. This paper will discuss the challenges associated with collecting municipal property tax.

The LSGA offers two options to the municipalities with regards to property tax: house and land tax (HALT) and land revenue/land tax or integrated property tax (IPT) which integrates house and land as well as land without any construction on it. So far, 42 out of the 58 municipalities have implemented IPT.

While property tax is a major local tax, property tax revenue constitutes only a small share of municipal revenue. In FY 2010-11, municipal property tax constituted 71% of the local taxes, 33% of the own source revenue (OSR) and a mere 7% of the total revenue.

Municipalities face three broad challenges in property tax collection: low capacity, low compliance, and lack of incentives.

The first and most important challenge is low capacity in tax administration as municipalities lack adequately trained human resource for tax administration. Mainly, low capacity has meant no regular updates of the tax register and suboptimal use of the tax software.

The second major challenge is low compliance due to low willingness to pay taxes and poor enforcement capacity of the municipalities. Most taxpayers pay property tax only when they need to access municipal services. Promoting voluntary compliance is a key challenge and a particularly difficult one at the moment due to the absence of elected bodies at the local level. As third challenge, municipalities lack the will and the capacity to enforce compliance.

Thirdly, a lack of incentives exacerbates the aforementioned challenges. Municipalities as institutions and municipal staff as individuals have very few incentives to strengthen property tax collection. Increasing fiscal transfers as well as access to funds from the development partners has meant reduced incentives for

tax effort. Tax effort is not rewarded at the personal or institutional level. Finally, local bodies do not face hard budget constraints with pressure to deliver services. There is a great potential to increase property tax revenue by addressing the issues of municipal capacity and compliance. However, the issue of incentives must be addressed to prevent the efforts at tackling capacity and compliance gaps from being supply-driven.

3.1.1 Introduction

The state is believed to be responsible for providing various services to people living within its jurisdiction directly or indirectly. While the range of such services provided varies from state to state, a key source of revenue for such service provision is taxation across the states. Besides the central government, local bodies are increasingly assigned responsibilities for delivering services. To fulfil their mandates, local bodies are authorized to generate local revenue through taxation.

Local bodies in Nepal – districts, municipalities, and villages – are financed by a combination of own source revenue and block transfers from the central government. Municipalities have various revenue instruments, which include local taxes, user charges, fees and fines. Local taxes include property tax, vehicle tax, professional tax, and entertainment tax

Property tax is considered a good revenue instrument for local bodies, as it is a highly visible tax with a stable tax base. Better property tax collection can boost local autonomy by increasing own source revenue and strengthen local governance by underscoring the shared responsibility of citizens and public authorities for urban development (De Cesare, 2012).

Property tax is a key source of local revenue for urban local bodies or municipalities in Nepal. The Local Self-Governance Act (LSGA) 1999 devolved the authority to collect property tax on house and land to local bodies in Nepal. While municipalities have been collecting tax on both house and land, Village Development Committees (VDCs) have only been levying land revenue. This paper will only discuss municipal property tax.

The LSGA offers two options to the municipalities with regards to property tax: house and land tax (HALT) and land revenue/land tax or integrated property tax

(IPT) which integrates house and land as well as land without any construction on it. So far, 42 out of the 58 municipalities have implemented IPT.

Property tax collection faces several challenges, particularly, across the developing world. Nepalese municipalities face three broad challenges in property tax collection: low capacity in tax administration, low compliance and a lack of incentives to address the first two. This paper will argue that a lack of incentives at the individual and institutional level keeps the first two issues being addressed sincerely.

Although major local tax, these challenges have meant that property tax revenue has not been fully exploited. It constitutes only a small share of municipal revenue, a mere 7% of the total revenue in FY 2010-11.

The paper will proceed as follows: the remainder of chapter 1 will discuss the national policies on property tax and compare IPT and HALT, chapter 2 will present the current status of property tax collection, chapter 3 will discuss the major challenges to tax collection, and chapter 4 will conclude and offer some recommendations.

3.1.2 National Policies on Property Tax

Formal property tax in Nepal dates back to when the central government began collecting house and land revenue tax via tax offices across the country.

Nagar Panchayat Act - 1949& 1962

This act authorizes *Nagar Panchayat-s*¹ to levy tax on the houses and the land occupied by the houses within its jurisdiction.

Property Tax Act - 1960

This act allowed for tax on urban house and land.

House and Land Tax Act – 1962

Under this Act, house and land occupied by the house and its compound in the urban areas are charged a tax. The valuation of property as well as the tax collection was done by tax officers appointed by the government.

¹ *Nagar Panchayat* – Urban Local Governments

Property Tax Act - 1990

This act taxes all property fixed and liquid assets. Property valuation and tax collection was to be done by tax officers. This act was never really implemented. However, it has never been repealed.

Municipality Act - 1990

This act authorized municipalities to levy a “*Dhurikar*²” on the house and land occupied by the house based on size, type, structure and area occupied by the house. This would not be applicable where municipalities were levying House and Land Tax under the House and Land Tax Act of 1962.

The Local Self-Governance Act 1999 (LSGA)

The Local Self Governance Act 1999 (LSGA) and the Local Self Governance Regulations 1999 (LSGR) devolved this authority to municipalities allowing them to levy property taxes locally.

LSGA was introduced with the express aim of promoting participation of people in governance and development thereby local autonomy and decentralization. It sought to devolve powers, responsibilities, means and resources to make local bodies capable of self-governance including the authority to generate revenue through local taxes.

The LSGA offers two options to the municipalities with regards to property tax: house and land tax (HALT) and land revenue/land tax *or* integrated property tax (IPT) which integrates both house and land. HALT is governed by the House and Land Tax Act of 1962.

² *Dhurikar* – Rooftop tax

Local Self Governance Act - 1999

Chapter 8: Taxes, Fees, Service charges, and Fares

136. Land Revenue and House and Land Tax:

(1) The Municipality may levy house and land tax, as prescribed, on each house and land within its jurisdiction on the basis of the size, type, design, construction and structure of the house and compound and area covered by the house, as approved by the Municipal Council.

(2) The Municipality may impose land revenue and land tax as prescribed on the land within the municipal area.

140. Property Tax:

The Municipality may levy an integrated property tax, within its jurisdiction at the prescribed rate.

3.1.2.1 Comparing IPT and HALT

Definitions

House and land tax (HALT) is levied upon the net taxable value of house and the plot on which the house is located. If an individual owns more than one house, each property is taxed separately.

Land without any construction on it is charged land revenue (*malpot*) or land tax (*bhumikar*). Thus, municipalities, which implement HALT, administer HALT alongside land revenue or land tax.

Integrated property tax (IPT) is levied upon on net taxable value of all properties of a taxpayer, i.e. land and buildings combined. Unlike HALT, multiple properties of the same owner are combined and tax is levied on the total value.

IPT & HALT Rates

The tax rates are defined in the LSGR (1999). HALT is levied on the basis of a graduated rate schedule. The first one million is exempt from tax and the next slab of property up to one million is charged a lump sum rate of Rs 300. Beyond that, rates are progressive as shown in Table 1. IPT rates are shown in Table 2.

Initially, under IPT, the maximum taxable value of property was set at Rs. 5 million which was taxed Rs. 1500. This discouraged the bigger municipalities with large property owners and valuable land to implement IPT. They chose HALT, which did not fix a ceiling on the amount of taxable property. The IPT rates were revised in the

second amendment of LSGR in 2004, which removed the ceiling on taxable property.

As the tables below demonstrate, while HALT rates are fixed, municipalities have some discretion in setting rates within the limits prescribed in the LSGR.

Table 1: Rates of House and Land Tax (LSGR, second amendment 2004)

Taxable value	Tax rate
Up to Rs. 1 million	Exempt
Next Rs. 1 million	Rs 300 (lump sum)
Next Rs. 3 million	0.05%
Next Rs. 5 million	0.25%
Next Rs. 10 million	0.50%
Above Rs. 11 million	1.50%

Table 2: Rates of Integrated Property Tax (LSGR 1999)

Taxable value	Tax rate (annual)
Up to Rs. 1 million	Rs. 25 to Rs. 200
Rs. 1 million to Rs. 2 million	Rs. 250 to Rs. 400
Rs. 2 million to Rs. 3 million	Rs. 500 to Rs. 1,000
Rs. 3 million to Rs. 5 million	Rs. 1,000 to Rs. 3,000
Rs. 5 million to Rs. 10 million	Rs. 3,500 to Rs. 10,000
Rs. 10 million to Rs. 20 million	Rs. 12,000 to Rs. 20,000
Rs. 20 million to Rs. 50 million	Rs. 25,000 to Rs. 60,000
above Rs. 50 million	Rs. 2 per Rs. 1,000

Valuation & Tax assessment

Under HALT, a strictly area-based valuation approach is used to value built structures whereby per square feet value is fixed in the LSGR. Houses are valued minimally at the rate of NPR 624 per square foot. To value the land occupied by the houses, a valuation committee can be formed at the municipal level. Land is valued rather highly under HALT compared to IPT. Where such a committee does not exist, the land will be valued according to the rates set by land revenue office.

In municipalities where HALT is levied, land revenue is levied alongside HALT. It is levied on all land within municipality including the land that has a construction on it which is charged under HALT. Technically, the land occupied by houses is taxed twice. Land is classified according to agricultural productivity and levied a charge according to the area. Double taxation is a technical complication in this case.

For IPT, a valuation committee is formed at the municipal level, which recommends valuations. The LSGA prescribes that market value form the basis of valuation. However, this is not in practice mainly because market value is essentially unobservable in a country like Nepal (De Cesare 2012). Also, using market value as

the basis would result in rather high tax obligations. Hence, in practice the valuation committee follows an area-based approach after classifying the land into different categories.

With regards to tax assessment, under HALT each property of the same owner is taxed separately. One owner with several properties each worth less than a million is exempt from paying any tax. Under IPT, the values of all properties of each taxpayer are summed up and the total is taxed. Since all taxpayers pay a minimum, no one is exempt. This allows for **broader tax base** for the municipality and assures a more equal treatment of taxpayers.

The switch to IPT

Initially, most municipalities imposed the HALT and land revenue instead of IPT. The central government has been encouraging municipalities to adopt IPT, which is considered more scientific in its valuation approach and more efficient in terms of administration. IPT implementation is a criterion in municipal performance measurement system Minimum Conditions and Performance Measures (MCPM). A municipality, which has implemented IPT, gets one out of a 100 points and a municipality, which has improved its tax collection with the implementation of IPT, gets an additional one point. However in overall three out of 15 criteria are of minimum conditions, which must be satisfied by municipalities to get additional capital grants from central government, are related to internal revenue administration. Similarly 16 out of 100 points are allocated in performance measurement for efficient and effective revenue administrative system.

Gradually, most municipalities have switched to IPT with 42 out of 58 municipalities currently implementing IPT. Among those not implementing IPT, Kathmandu metropolitan city, all four sub-metropolitan cities and 10 smaller municipalities levy HALT and land revenue. The remaining only one municipality collects only *dhurikar* and land revenue but is preparing to switch to IPT.

The biggest hurdle in switching to IPT is the administrative challenge of establishing complete property cadastre. By the very design of the IPT, it is necessary to establish a cadastre of the entire municipality before it can be implemented. In case of HALT, an owner could be paying tax on one property and not on another. This is an administrative challenge often too big for the larger municipalities.

In addition, due to the differences in tax rates, under HALT, large taxpayers pay a much higher tax than they would for the same property in IPT. For example, for property valued at NPR 40 million, the tax due under HALT would be NPR 364,300 but the corresponding sum under IPT can be a maximum of NPR 60,000. For bigger municipalities, which have many large taxpayers, HALT is therefore still more appealing in terms of its revenue generating capacity.

Given this, municipalities like Kathmandu Metropolitan City fear a loss of revenue if they switch to IPT despite recognizing that IPT is a more scientific tax system. Since there are no exemptions under IPT, the tax base will certainly be broader. However, it is difficult to say that the revenue loss due to lower individual obligations would be compensated by the expansion in tax base.

The municipalities lack a comprehensive database and manpower to project comparative revenues under the two systems. Until the municipalities become confident to state that switching to IPT does not incur revenue losses, they are hesitant to make the switch.

3.1.3 Current status of property tax collection

Municipalities in Nepal are financed by a combination of Own Source Revenue (OSR) and loans, and block transfers from the central government. Municipal OSR is composed of local taxes, user charges, fees and fines. Local taxes include property tax, vehicle tax, professional tax, and entertainment tax. Besides, municipalities receive a local development fee (LDF), which has been provided in lieu of a local trade tax called *Octroi*.³

In the past, municipalities levied a local trade tax called *Octroi* on all goods entering the municipality for consumption. This tax introduced distortions in allocation and consumption decisions as it falls differentially on residents and non-residents defeating the idea of collecting local taxes for expenditure by local government and it provided protection to those industries located within the municipality vis-à-vis goods produced in other locations (Kelly 1998). Besides practical difficulties in administering the tax, which encouraged opportunities for misadministration and corruption, it posed hindrances to smooth flow of goods across the country as it

³ Octroi - The Octroi is an internal trade tax levied on all good entering into a local jurisdiction. The tax is assessed on the value, weight or number of items and is collected through collection agents at Octroi stations (Kelly, 1998)

was collected at each municipal border (Kelly 1998). Following strong opposition, *Octroi* was abolished in 1999.

LDF was proposed as an interim solution. Municipalities would receive LDF in lieu of *Octroi* from the Ministry of Local Development (MLD)⁴. LDF is derived from an additional tax of 1.5% of the total value of goods levied alongside customs duty on goods entering the country. This tax was collected in a central account and transferred to municipalities as a block transfer on the basis of *Octroi* revenue it generated in the base year. The system thus did not correct the inconsistencies of *Octroi* namely, economic distortions, domestic protection and incentives for tariff evasion (Kelly 1998).

LDF was instituted as an interim solution; however, a durable solution became necessary with Nepal's accession to the World Trade Organization (WTO) in 2004, which required the LDF to be abolished by 2011 as it is seen to distort trade. The additional tax of 1.5% has now been abolished. The abolishment meant a huge reduction in the revenue for municipalities. To compensate for that, the municipalities got a fiscal transfer equivalent to LDF in FY 2010-11. The Ministry of Federal Affairs and Local Development (MFALD) lobbied the Ministry of Finance to make this possible. Whether this transfer will continue in the future is uncertain and will depend on the lobbying powers of MFALD.

3.1.3.1 Property tax collection in context of municipal OSR

Property tax is the largest revenue title among the local taxes. Total property tax collection has increased over the past few years from just over NPR 5 million rupees in FY 2000-01 to about NPR 543 million in FY 2010-11.

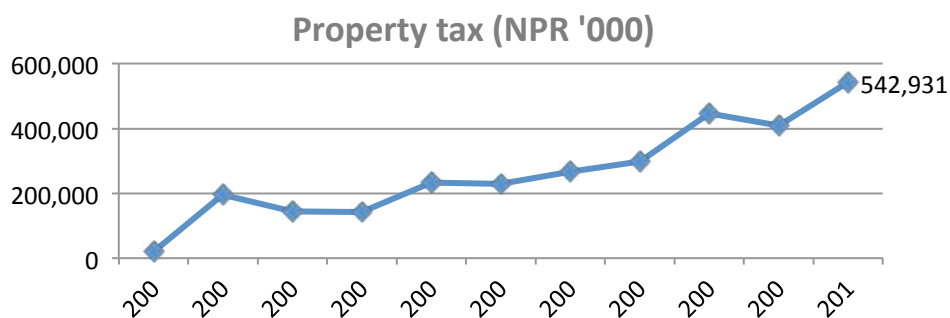


Figure 1: Annual property tax collection since 2000-01 □□

⁴ Now renamed the Ministry of Federal Affairs and Local Development (MFALD)

While property tax is a major local tax and total property tax revenue has increased over the years, it constitutes only a small share of total municipal revenue. As Figure 2 shows the share of property tax has remained resolutely below 8% of the total revenue over the last decade since 2000-01. It is clear that the full revenue potential of property tax has not been exploited. There is a heavy reliance on central government fiscal transfers, which have increased dramatically in the past few years. In FY 2010-11, the property tax constituted 33% of OSR and 7% of the total revenue.

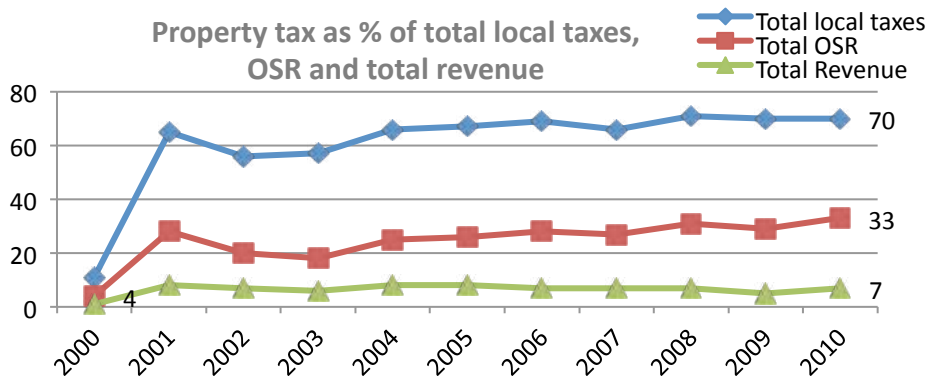


Figure 2: Property tax as a share of total local taxes, total OSR and total revenue^{□□}

Figure 3 shows the composition of local taxes. In FY 2010-11, property tax constituted 71% of the local taxes. Figure 4 shows the composition of municipal own source revenue. Property tax constituted 33% of the total OSR in the same fiscal year.

^{□□}Source: Annual Report on Detailed Revenue and Expenditure Breakdown 2010-11 published by MLD/MMD, LBFC and GIZ/SUNAG

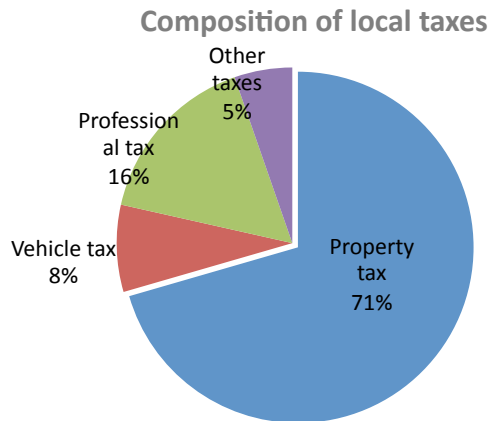


Figure 3: Property tax as share of local taxes (2010-11)^{□□}

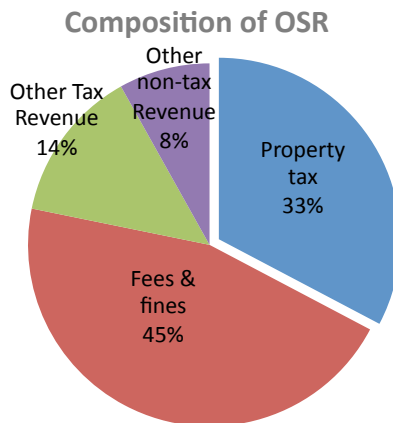


Figure 4: Property tax as share of OSR (2010-11)^{□□}

Figure 5 shows the composition of the total municipal revenue. Property tax constituted a mere 7% in the FY 2010-11. The figure also shows that OSR is only 21% of the total revenue.

^{□□}Source: Annual Report on Detailed Revenue and Expenditure Breakdown 2010-11 published by MLD/MMD, LBFC and GIZ/SUNAG

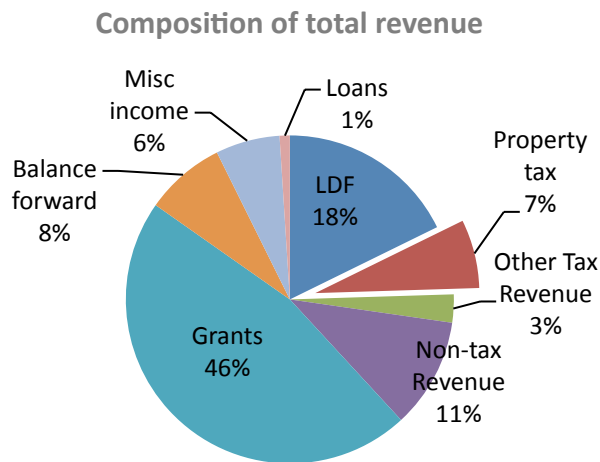


Figure 5: Property tax as a share of total revenue (FY 2010-11)[□]

Strengthening property tax and thereby OSR is even more important due to the abolition of Local Development Fee (LDF), which constituted 18% of the total revenue in FY 2010-11. Due to the large share of LDF in the revenue, it cannot be compensated for by an increase in local taxes. The gap in revenue has to be addressed by a restructured fiscal transfer system. However, a boost in local taxes, particularly property tax, can contribute towards filling the gap left by the abolition of the LDF.

The above provide a glimpse of aggregate property tax revenue in the context of total municipal revenue. There are 58 municipalities in Nepal spread across the country and there is great variation among them with regards to geographic location, area, population, and inevitably their revenue generating capacities. Please refer to 3.1.7 for the list of municipalities and their corresponding population. Since the municipalities vary widely, it is useful to disaggregate the property tax data a little for meaningful analysis.

As mentioned earlier, on average, property tax constituted 7% of the total revenue in FY 2010-11. The share ranges from a negligible 0.05% to 34.1%. Interestingly, the

[□]Source: Annual Report on Detailed Revenue and Expenditure Breakdown 2010-11 published by MLD/MMD, LBFC and GIZ/SUNAG

municipality with the highest share is a small municipality in the mid-western region of the country. If 6 municipalities where the highest share of property tax are excluded, then the average share of property tax in the total revenue falls to 2.7%. These six include Kathmandu metropolitan city and two sub-metropolitan cities. As shown in Figure 6, in 52 out of the 58 municipalities, property tax constitutes less than 10% of the total revenue. In 45 of the municipalities it constitutes less than 5% of the revenue.

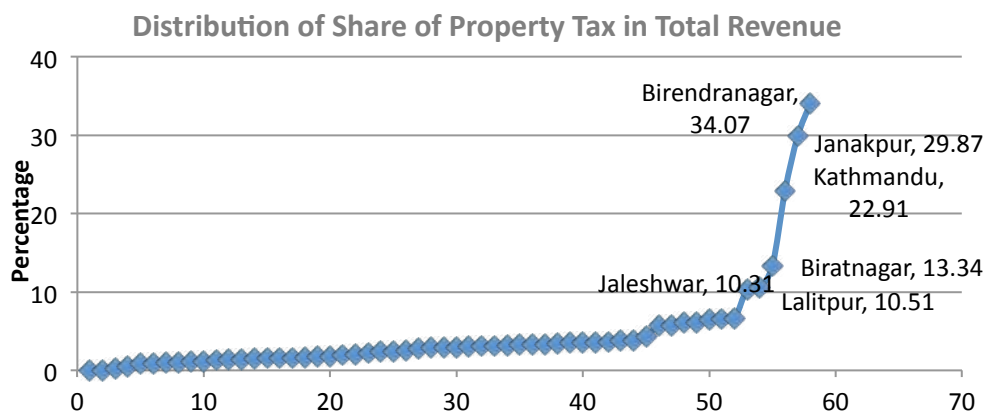


Figure 6: Share of property tax in total revenue across municipalities

This wide range in the contribution of property tax to municipal revenue offers more ground to argue that property tax potential has not been fully exploited. The next chapter will delve into the challenges to collect property taxes in Nepal.

3.1.4 Challenges to collect property tax

Improving local tax collection is a challenge for local bodies worldwide. It is particularly challenging in developing countries where the state-citizen relationship is weak and citizens are much less willing to pay taxes. Local bodies in Nepal face similar challenge in collecting local taxes.

Property tax is a major local tax in Nepal but as mentioned before it constituted a mere 7% of the total revenue in FY 2010-11. There are various challenges associated with property tax collection. Chief among them are low capacity and low compliance. While these challenges are known, there is little incentive to change

the situation. The question of incentive is a particularly complex one in Nepal at the moment, due to the absence of elected local representatives.

The Local Self-Governance Act (LSGA) introduced in 1999 was seen as milestone legislation in the area of decentralization. It sought to devolve powers, responsibilities, and means and resources to make local bodies capable of self-governance including the authority to generate revenue through local taxes.

However, implementation of LSGA reforms was hampered by the armed conflict that ensued in 1996. The last local elections were held in 1997. The elections due in 2002 could not be held. Since then, local governments have remained without elected representatives and are administered by deputed central government bureaucrats. After the signing of Comprehensive Peace Agreement in 2006, a transitional *All-Party Mechanism* was established with the objective of advising and supporting these civil servants to consider local priorities. The government following directives from the anti-corruption body, Centre for Investigation of Abuse of Authority (CIAA), dissolved this mechanism in January 2012. Allegedly, the CIAA stated that the all-party mechanism was illegal and was found to be promoting corruption (Himalayan Times, 2011; Kantipur, 2011). Thus, the local bodies are back to being administered by bureaucrats delegated from the centre.

The following will discuss capacity, compliance and incentives in collecting property taxes.

3.1.4.1 Low capacity

Efficient tax administration requires technical expertise and administrative capacity. Nepalese municipalities suffer low capacity in administering property tax.

A study of 5 municipalities conducted in 2011 showed the cost of property tax administration to be 10.44% of the total property tax revenue generated. While this is a reasonable figure, the cost ranged from 7% to 31% (Koirala & Sharma, 2011, p13) showing low efficiency in some municipalities. This can be taken as an indicator of poor capacity.

Lack of skilled manpower

Competent human resource is crucial to any tax administration. Revenue sections in Nepalese municipalities are not adequately staffed. Smaller municipalities usually have only 2-3 members of staff in the revenue section. The larger municipalities, the metropolitan and sub-metropolitan cities do have more staff but while understaffing is one issue, lack of skills among the existing staff is another issue.

Many staffs can't use computer and run the tax administration software, they can only work manually. Even those who operate the software are not always using it optimally.

Another aspect where the human resource is weak is in the area of taxpayer education. Taxpayer education is a multidisciplinary issue requiring a level of knowledge on various subjects including psychology, communication, and public finance. However, the requisite skills for a taxpayer education strategy are lacking among revenue section staff. Admittedly, political will is also a big factor in pursuing taxpayer education. For politicians, the engagement in taxpayer education is the easiest, the more they together with local administration can show where the money goes and what is done with it.

Lack of resources

The other aspect of capacity is resource. Revenue sections must be well equipped for efficient revenue administration. Many of the municipalities however lack requisite resources.

Revenue sections lack sufficient hardware, data backup systems and a regular supply of electricity to deliver services effectively. Many revenue sections operate with only one computer. Some smaller municipalities are administering the tax without using software.

Consequences

Lack of competent staff and resources has four key consequences.

Firstly, the tax register is not updated regularly. Due to lack of manpower to coordinate with the district land revenue office on property transactions, new transactions are not always recorded on the tax register. Many new taxpayers could be missing from the tax roll. The municipalities lack the human resource to keep track of the transactions and update the register regularly. Also, in municipalities

where initial data has been collected through self-declaration of property, the data is not verified by field surveys due to lack of staff.

Secondly, the municipalities do not have a good record of who has and who has not paid their taxes which makes it difficult to pursue the evaders. Further, most municipalities do not send tax bills to taxpayers' homes due to lack of staff to do so. Taxpayers have to come to the municipality to collect and pay their tax bills. Sending tax bills home could potentially increase compliance.

Thirdly, the employees lack the capacity to project property tax revenue and work accordingly. Most municipalities do not have up to date data on the total number of taxpayers. Only a few municipalities have implemented house-numbering system, which facilitates data collection.

Finally, low capacity of the revenue section has meant that tax campaigns are not pursued with vigour. Taxpayer education is a process that requires a long-term strategy, a vision and persistent effort. Not enough has been done in educating the taxpayers about their obligations towards the local government and what the tax revenue is used for. While many municipalities spend on advertisements towards the end of the fiscal year urging taxpayers to pay their taxes to varying results, hardly any municipality has a strategic taxpayer education program. The central government has not issued any comprehensive guidelines or tool kits either.

A related capacity issue is that of software used for property tax administration. Different municipalities are using different software hence there is no organized technical backstopping available to the municipalities. Further, there is lack of standardization and verification by the relevant ministry.

3.1.4.2 Low compliance

Tax compliance comes either from voluntary compliance where people pay willingly or strict enforcement where people pay out of fear. The first requires citizens to trust their government and the second requires a state with strong enforcement capacity. Both factors are in short supply in Nepal.

It is difficult to derive figures for compliance, as data on total number of taxpayers is unavailable or unreliable. A study of 28 municipalities conducted in 2011 shows that on average 61% of the registered taxpayers pay their taxes. However, the rates

range from a minimal 25% to 98% indicating a great need to expand coverage in certain municipalities (Koirala & Sharma, 2011).

High compliance cost is often considered a hindrance to tax collection particularly in case of income tax. The compliance cost in case of property tax is rather minimal. Besides the first time when taxpayers have to declare their property, taxpayers do not need to fill out extensive forms each time they pay their taxes. So non-compliance in Nepal comes from resistance and weak enforcement capacity of the municipalities.

Low morale of the municipal residents

Municipal residents are generally aware of their tax obligations but the willingness to pay their taxes is low. Two factors can help explain the morale of taxpayers: quality of services available in return and the level of confidence in the government.

Low quality of services in return

Taxpayers expect public service in return for the taxes paid. A common refrain among taxpayers in Nepal is why pay taxes to the municipalities when it is not providing any services in return. Municipalities are mandated by the LSGA to perform various duties. They are fully or partially responsible for physical development including construction and maintenance of local roads, water resource management and sanitation, primary education, promotion of industry and tourism, culture, provision of basic healthcare, and other miscellaneous duties. While many services like waste collection and drinking water are funded by user fees, taxes contribute towards provision of local roads and environmental management, basic health care, disaster control, etc. are paid for by tax revenue. The quality of services is generally perceived to be poor. Taxpayers point to the lack of or poor quality of municipal services as a reason to withhold taxes.

Another common perception is that municipalities are overstaffed and that taxes go towards paying salaries not for development of the municipality. The charge of overstaffing is partly true as local leaders in some instances have been irresponsible in influencing recruitment of staff close to them without regard to qualification or competence (Jaisi, 2011). Once recruited, it is hard to terminate any of the positions. Hence, many taxpayers only pay their taxes when they need to access other municipal services, particularly those related to property transaction or when tax clearance is required for mortgaging the property.

□ **Low confidence in the local government**

The state-citizen relationship is a strained one in Nepal. This is particularly the case due to the absence of elected local representatives since 2002. Residents do not own their municipality and do not think that it represents them. At the moment, executive officers, who are delegated central government bureaucrats, have the full authority to make decisions in the municipality.

Besides, municipalities are accused of lack of transparency and accountability as well as corruption. If the municipality cannot account for the taxes paid, residents are unwilling to pay taxes. The normal accountability mechanism is not functional at the moment due to the absence of elected bodies. Taxpayers cannot hold municipality officials accountable through elections as they would do with elected officials. The absence of elected bodies also means that the regular planning process in the municipalities is interrupted. In fact, citizens have few incentives to engage with the state (Tamang & Malena, 2011).

The need for trust and confidence in the government is even more pronounced in the case of local governments as the tax collection agency and the service provision agency is one and the same unlike at the central government level where the revenue department is a separate agency of the government that does not deliver public services by itself. Hence, transparency and accountability is even more important in building voluntary compliance.

Low enforcement capacity

The other aspect of compliance is the enforcement capacity of the municipalities.

Municipalities do not have good records of who has not paid their taxes. Even when known, the municipalities do not pursue the taxpayers strongly. Bills or reminders are not sent to taxpayers' homes. Municipal tax policies prescribe fees and fines on arrears but this is not prohibitive enough to enforce payment.

Municipal authorities could withhold other services besides those related to property transaction. However, either due to lack of coordination between the revenue section and other sections in the municipality or due to unwillingness to enforce property tax, municipalities very rarely withhold other services besides those related to property transaction.

Absence of elected bodies makes it difficult for municipalities to pursue aggressive enforcement policies and local leaders are reluctant to pursue tax collection for

political reasons (Kelly, 2011). Taxation is inherently unpopular and as the leaders do not have full control over how the revenue generated is mobilized, it is difficult for them to rally for tax compliance.

Legal challenges to compliance

Besides the low morale and poor enforcement capacity, there are some legal challenges which inhibit compliance. The issues vary in the case of integrated property tax (IPT) and house and land tax (HALT).

Integrated Property Tax

The Local Self Governance Rules (LSGR) prescribes that valuation and tax rates be set for 5 years. This has meant that the tax revenue has not kept up with the dramatic increases in land value. Also, this has meant that any rate revision after a five-year period has faced strong resistance from the taxpayers as it has often meant a big increase in tax obligations instead of a gradual change over the years.

House and Land Tax

The House and Land Tax under LSGA, guided by the House and Land Tax Act of 1962 which exempts several properties from tax including “buildings used by hotels for dining, accommodation, motor vehicle parking and garden and the land occupied by these buildings.” However, the remaining area inside the hotel compound is taxable. But the hotels have refused to pay HALT to the Kathmandu municipality claiming that hotels have been redefined in 1998 to cover all area inside their compound including swimming pool, restaurants, health club and other amenities (Republica, 2012). This legal issue has deprived Kathmandu metropolitan city of a lot of property tax revenue.

3.1.4.3 Lack of Incentives

So far in this section, the paper has described two key challenges to property tax collection at the moment: low capacity for tax administration and low compliance. What exacerbates these two issues is the lack of incentive to address them.

With easier access to funds from the central government as well as development partners, local bodies are not forced to raise own source revenue. Tax effort is not rewarded at the individual or institutional level. In this situation, even citizens tend to assume that funds have to come from the centre anyway. Given the frequent

transfers bureaucrats do not have incentives to invest in raising revenue either. Finally, local bodies do not face hard budget constraints with pressure to deliver services. The following will elaborate on these issues.

Easier access to intergovernmental transfers and donor funds

Intergovernmental transfers negatively affect property tax revenues. Regardless of the level of fiscal autonomy, local tax efforts decrease with higher transferred revenues (De Cesare 2012, p 15). This seems to be the case in Nepalese municipalities too where the share of OSR has hardly increased in parallel to the increasing fiscal transfers to the local bodies.

The total municipal revenue has increased greatly in the last decade from just over Rs. 2 billion in FY 2000-01 to over Rs. 8 billion in FY 2010-11 as shown in Figure 6. However, the increase has mainly come from increased intergovernmental transfers not from increased own source revenue. The gap between the OSR and total revenue has widened over the years.

Fiscal transfers increased dramatically in the past few years, particularly, since the introduction of Local Governance and Community Development Programme (LGCDP) in 2008 which channelled funds to the local bodies. LGCDP was introduced with an aim to bring about improvement in the living standard for the masses through good local governance based on a democratic value system. It promoted an inclusive and participatory development agenda. It emerged from the need to ensure a tangible peace dividend to the people in the post-conflict context.

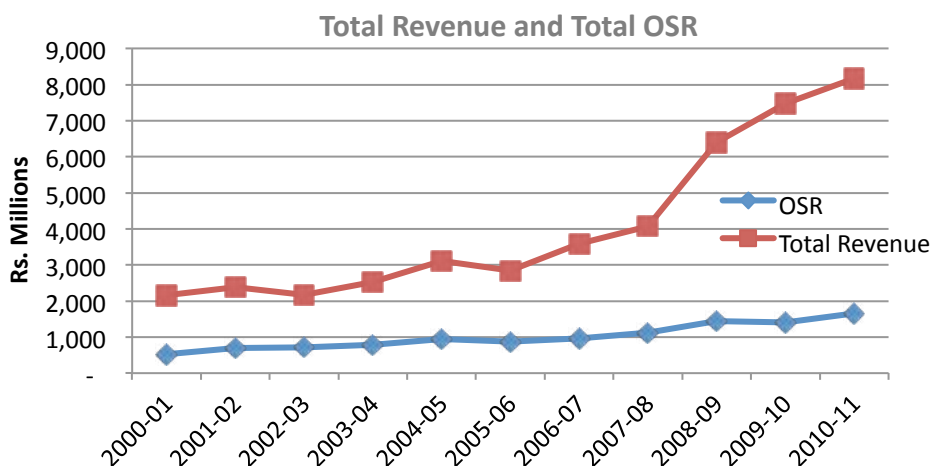


Figure 7: Comparing own source revenue to total revenue

Own source revenue makes only a small share of total municipal revenue in Nepal. In FY 2010-11, share of OSR was a mere 20% of the total revenue. As Figure 6 shows, the share has gradually declined from a peak of 33% in FY 2002-03. It has improved by one percentage point in the last fiscal year.

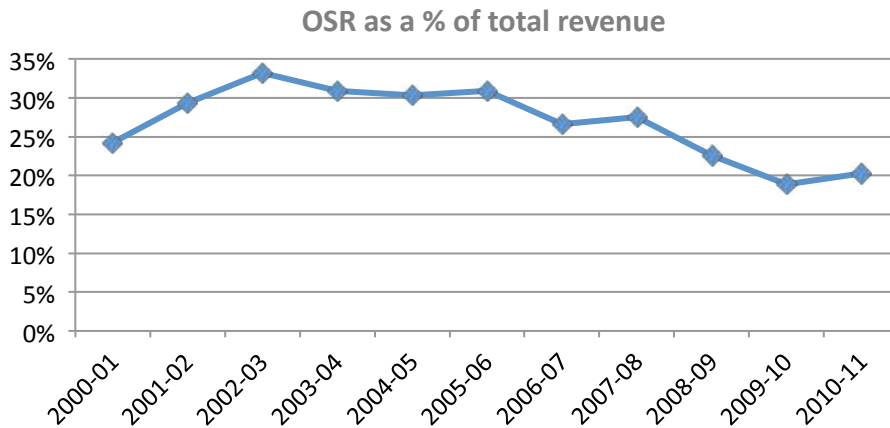


Figure 8: Own Source Revenue as a percentage of the total municipal revenue

Thus, local bodies have easier access to formal government transfers, which undermines incentives to strengthen OSR. In addition, municipalities receive project-based grants from line ministries as well as funds from development partners. Given the easy access government grants or donor funds, municipalities have no incentives to increase the own source revenue (Kelly, 2011).

Besides grants, municipalities also have access to loans from the Town Development Fund, the private sector as well as development partners. As local bodies lack elected representatives at the moment, executive officers, who are deputed central government bureaucrats, are the ones who sign on these loans. However, these bureaucrats do not really have any liability - financial, electoral or otherwise towards the loan. Big loans mean big infrastructure projects with opportunities for big kickbacks. This perversely increases the loan seeking behavior and undermines incentives to boost OSR. Any minimal liability they have is further reduced due to the quick transfers of these bureaucrats. The following section will elaborate this further. Admittedly, even elected representatives would have incentives to borrow funds without regard to loan-bearing capacity of the municipality to finance public projects and improve their political standing.

The bureaucracy

The municipalities in Nepal are in the hands of bureaucrats deputed from the centre. Executive officers now have the authority that an elected mayor would normally have. Given that the civil service is highly politicized and the evaluation system and the transfers are not linked to performance (Tamang & Malena, 2011) this has direct consequences on the performance of municipalities. There are few incentives for accountable and responsive service delivery.

Although the Civil Service Act states that bureaucrats must remain in their positions for a minimum of two years, municipalities suffer frequent transfers of executive officers. Such frequent transfers without regard for performance discourage any sustained efforts to improve tax collection, which will benefit the municipality over a longer time horizon. This leaves the executive officers with little incentive to invest in enhancing tax collection. Enforcing tax collection invites unwelcome attention and resistance from various corners. Bureaucrats focus on staying their term without major issues. Given the absence of local representatives, they also have a good excuse as to why they cannot be more aggressive in pursuing higher tax collection.

The local body performance measurement system Minimum Conditions and Performance Measures (MCPM) does have an indicator for tax effort under performance measures. If a municipality has expanded its revenue by implementing integrated property tax, the municipality obtains 2 points out of a 100. However, this only applies to IPT not HALT. The 2 points awarded for tax effort do not seem to be a sufficient incentive for municipalities to pursue expansion of IPT aggressively.

MCPM scores are linked to performance based grant system. Municipalities which pass the minimum conditions and score well on the performance measures are rewarded with additional grants. However, the system requires a period of three years for municipal performance to have its impact through an additional grant from MCPM. Municipalities are assessed every year on their performance in the last year and the results feed into the additional grants in the following year.

Given the frequent transfers of executive officers, their performance cannot be linked to the municipal MCPM scores. Current executive officers will have to deal with the legacy of previous officers. This reduces the incentive offered by the indicator with regards to invest in improving property tax collection.

Besides the executive officers, the other staff in the municipality have hardly any incentive to boost own source revenue. Their salary or benefits are not linked to the revenue generated by the municipality unlike in the case of Internal Revenue Department where staff get a performance based salary.

Absence of hard budget constraints

Fiscal decentralization, the allocation of tax and spending powers to lower levels of government, is now an established policy objective, in many developed and developing countries. Moreover, it is actively promoted as a development strategy by organizations such as the World Bank (Azfar et al. 2001, World Bank 2000). However, in many countries, fiscal decentralization is not balanced in terms of tax and expenditure assignments, generating vertical fiscal imbalances. In practice, vertical fiscal imbalances are resolved either by centrally provided transfers to local governments or by sub-national borrowing. But this may generate new problems. Indeed, it is increasingly claimed that one of the costs of fiscal decentralization is that sub-national governments may face soft budget constraints (SBC) (Besfamille and Lockwood, 2007). A budget constrained organization faces a hard budget constraint (HBC) as long as it does not receive support from other organizations to cover its deficit and is obliged to reduce or cease its activity if the deficit persists (Kornai et al. 2003).

Hard budget constraint implies that local governments with fiscal autonomy must balance their budget without recourse to year-end assistance from the central government (Bahl, 1999). In this system central governments do not rescue the local governments when they face financial trouble. While in Nepal Municipalities have not been operating as autonomous or corporate institutions, there is no practice of spending more than the budget available i.e. exists tendency of spending only that amount which is available. As a result not a case of financial bankruptcy of local body has been found. However the local bodies in Nepal have to balance their budgets, they do not face hard budget constraints with pressure to collect revenues to deliver services. Expenditures are largely considered permissive, not mandatory, with no consequences for failure to deliver (Kelly 2011). Thus it is concluded that one of the reasons for being reluctant to make effort for tax collection is absence of hard budget constraints.

This chapter has discussed three key challenges to property tax collection in Nepalese municipalities: low capacity, low compliance and poor incentives. Capacity and compliance gaps are real, widely known and discussed. However, poor incentives mean that there is no real effort to address these two issues. Efforts to address capacity and compliance gaps have been mostly supply-driven.

3.1.5 Conclusions

Property tax revenue, which constituted 71% of the local taxes and 33% of own source revenue in FY 2010-11, is a major revenue title for local governments in Nepal. However, municipalities have not been able to exploit the revenue potential fully due to capacity and compliance gaps in property tax collection.

Low capacity in terms of human and material resources has meant that the tax registers are not updated regularly; tax revenue projection is not done on the basis of data and potentiality, and tax campaigns are not pursued with vigour.

Low compliance arises from the low willingness to pay taxes and poor enforcement capacity of the local bodies. Taxpayers point to the low quality of services in return for their taxes and the general lack of faith in local government.

Both these challenges are complicated by the absence of elected local representatives. However, a key issue is the lack of incentives at both individual and institutional level to address these issues and invest in tax effort. The incentive structure must therefore be addressed in order to tackle the issue of capacity and compliance.

3.1.6 Recommendation

Capacity building of municipalities

A systematic capacity development strategy is needed for municipal staff in revenue section. On the human resource side, issues to be addressed include: computer skills, capacity for revenue projection and taxpayer education programs including skills to formulate a taxpayer education strategy and capacity for regular update of the tax register.

To address the issue of lack of staff, municipalities could conduct a thorough internal restructuring and reassign staff where they are needed the most.

On the resource side, municipalities need support for computerisation of all tax administration and adequate data backup systems.

Once local elections will have taken place again, elected bodies will have to benefit too from capacity building measures regarding local taxes.

Boost Compliance

Municipalities need a sustained strategy to raise voluntary compliance through taxpayer education. Crucial to this is demonstrating transparency and accountability to build taxpayer confidence in the local government. Local governments need to communicate that the taxpayer money is being utilized properly.

- Promote transparency and accountability
Regular public/social audits should be done to show where the property tax revenue goes and demonstrate a link between taxes paid and services provided.

- Taxpayer education

The Ministry could facilitate the development of a taxpayer education tool kit that the municipalities could adapt to their particular contexts. The toolkit should focus on strategies for informing the public about their tax obligations and providing services to the taxpayers to make tax payment more convenient. The intervention could be to capacitate the local staff to formulate a taxpayer education campaign.

Boost incentives for the local body/tax officials

There are efforts at enhancing both capacity and compliance. However, given the lack of incentives these efforts have been more supply-driven and not institutionalized. The incentive structure has to be addressed for genuine capacity building in strengthening own source revenue.

A key issue identified was easier access to intergovernmental transfers as a disincentive to tax effort. While this is a real challenge, the answer cannot be a drastic reduction of transfers which would have severe consequences. The challenge is to find a balance that does not discourage tax effort (De Cesare 2012, p 15). A way to address it would be to reward tax effort in other ways.

Reward tax effort

Tax effort is not rewarded at the personal or institutional level. Changes can be introduced to reward tax effort at both individual and institutional level.

Monetary incentive for revenue section staff

Revenue section staff can be rewarded with a share of the increased property tax revenue at the end of each fiscal year if there is a significant increase in the revenue generated. This is practiced at the central level in the Internal Revenue Department where staff's salary is linked to their performance.

Monetary incentive for the municipality

As mentioned before, the total number of points awarded for property tax effort in MCPM is 2 out of a 100. Any municipality demonstrating an increase in property revenue due to implementation of IPT is awarded those two points. Scores of property tax effort could be increased in MCPM so it has a more significant role in the performance based grant that the municipalities receive.

An alternative to incentivise tax effort could be to provide the municipalities with an additional grant that is tied solely to their performance in own source revenue generation.

For any additional financial incentive to be functional, the executive officers must be stationed at a municipality for at least a period of two years. Hence, the Civil Service Act provision must be enforced.

Imposition of a hard budget constraint on certain expenditure titles

Intergovernmental transfers exist to ensure basic service delivery and to equalize the fiscal capacity of local bodies across the country. However, given that expenditures are not mandatory but permissive; municipalities are not under any pressure to deliver services from OSR although it is mentioned in Local Bodies Financial Administration Regulation (LBFAR). Hence, if a provision could be instituted to make certain mandatory expenditures be borne by OSR, municipalities will make effort to increase the OSR.

3.1.7 List of Municipalities

ID	Municipality	Population [□]	Type of Property Tax	Property tax collection in FY 2010-11 (NPR) [□]	Share of Property tax in total revenue in FY 2010-11 (%) [□]
1	Amargadhi	20,293	IPT	536,902.92	0.86
2	Baglung	27,686	Land Revenue & <i>dhurikar</i>	1,867,409.18	3.28
3	Banepa	19,587	IPT	1,568,272.31	2.25
4	Bhadrapur	21,305	IPT	1,150,547.00	1.19
5	Bhaktapur	84,428	HALT & Land Revenue	2,668,306.73	0.98
6	Bharatpur	138,569	IPT	8,859,357.33	3.29
7	Bhimdutta	102,744	IPT	4,726,500.43	2.56
8	Bhimeshwar	24,618	IPT	934,118.00	1.46
9	Bidur	23,806	IPT	886,441.00	1.68
10	Biratnagar	209,988	HALT& Land Revenue	28,853,006.85	13.34
11	Birendranagar	41,666	IPT	3,309,643.10	34.07
12	Birgunj	174,500	HALT& Land Revenue	17,384,543.89	6.63
13	Butwal	122,054	IPT	12,106,774.75	5.75
14	Byash	38,162	IPT	3,436,964.31	3.51
15	Damak	65,904	IPT	4,435,045.75	3.52
16	Dasarathchand	18,678	IPT	316,955.00	0.46
17	Dhangadi	97,672	IPT	7,324,209.86	6.45
18	Dhankuta	24,483	IPT	1,724,123.00	2.37
19	Dharan	132,205	IPT	7,026,825.00	3.14
20	Dhulikhel	13,290	IPT	2,416,981.54	3.16

[□] Source: Annual Report on Detailed Revenue and Expenditure Breakdown 2010-11 published by MFALD/MMD, LBFC and GIZ/SUNAG

ID	Municipality	Population [□]	Type of Property Tax	Property tax collection in FY 2010-11 (NPR) [□]	Share of Property tax in total revenue in FY 2010-11 (%) [□]
21	DipayalSilgudi	37,272	IPT	134,229.63	0.24
22	Gaur	30,875	HALT & Land Revenue	764,515.06	1.3
23	Ghorahi	61,382	IPT	3,593,816.88	3.85
24	Gorkha	31,638	IPT	1,278,038.32	1.56
25	Gulariya	66,630	IPT	1,249,461.25	1.42
26	Hetauda	84,777	IPT	9,905,623.97	3.01
27	Ilam	19,577	IPT	2,701,146.00	2.96
28	Inaruwa	28,469	IPT	1,857,066.25	3.46
29	Itahari	60,717	IPT	6,746,281.47	6.15
30	Jaleshwar	26,347	HALT& Land Revenue	390,583.60	10.31
31	Janakpur	97,653	HALT& Land Revenue	17,268,014.00	29.87
32	Kalaiya	53,130	IPT	874,660.16	1.39
33	Kamalamai	42,846	IPT	1,603,911.25	1.53
34	Kapilbastu	41,078	IPT	1,801,826.55	2.36
35	Kathmandu	1,024,522	HALT& Land Revenue	274,330,315.68	22.91
36	Khandbari	24,913	IPT	853,402.50	2
37	Kirtipur	51,900	HALT& Land Revenue	4,714,026.54	3.6
38	Lahan	38,684	IPT	1,519,578.02	2.94
39	Lalitpur	222,140	HALT& Land Revenue	36,748,187.21	10.51
40	Lekhath	54,928	HALT & Land Revenue	1,834,468.02	1.57
41	MadhyapurThim	68,555	HALT& Land Revenue	3,663,018.91	2.86
42	Malangawa	23,493	HALT& Land Revenue	1,102,266.78	5.74

ID	Municipality	Population [□]	Type of Property Tax	Property tax collection in FY 2010-11 (NPR) [□]	Share of Property tax in total revenue in FY 2010-11 (%) [□]
43	Mechinagar	62,902	IPT	3,923,759.38	3.13
44	Narayan	23,446	IPT	469,970.00	0.99
45	Nepalgunj	68,155	IPT	7,162,931.23	6.11
46	Panauti	31,094	IPT	1,497,642.22	1.14
47	Pokhara	244,578	HALT& Land Revenue	23,107,477.68	6.52
48	Putalibazar	33,621	IPT	1,681,471.00	3.52
49	Rajbiraj	37,246	HALT & Land Revenue	619,632.55	0.85
50	Ramgram	26,571	IPT	1,320,547.10	2.07
51	Ratnanagar	54,727	IPT	3,415,914.62	3.84
52	Siddharthanagar	67,994	IPT	5,463,266.08	4.33
53	Siraha	26,002	HALT & Land Revenue	68,811.93	0.05
54	Tansen	29,587	IPT	1,002,613.50	3.26
55	Tikapur	56,075	IPT	1,694,049.01	1.76
56	Triyuga	78,696	IPT	3,375,168.10	2.81
57	Tulsipur	48,635	IPT	1,633,850.50	1.82
58	Waling	24,397	IPT	26,308.53	0.05

Location of Municipalities in Nepal



3.1.8 Facts about NEPAL

Nepal, officially the **Federal Democratic Republic of Nepal**, is a landlocked sovereign state located in South Asia. With an area of 147,181 square kilometers (56,827 m²) and a population of approximately 27 million (and 2 million absentee workers living abroad), Nepal is the world's 93rd largest country by land mass and the 41st most populous country. It is located in the Himalayas and bordered to the north by the People's Republic of China, and to the south, east, and west by the Republic of India. Specifically, the Indian states of Uttarakhand, Uttar Pradesh, Bihar, West Bengal, and Sikkim border Nepal, while across the Himalayas lies the Tibetan Autonomous Region. Kathmandu is the nation's capital and largest metropolis.

Nepal has a rich geography. The mountainous north has eight of the world's ten tallest mountains, including the highest point on Earth, Mount Everest, called *Sagarmatha* in Nepali. It contains more than 240 peaks over 20,000 ft² (6,096 m) above sea level. The fertile and humid south is heavily urbanized.

Hinduism is practiced by about 81% of Nepalese - making it the country with the highest percentage of Hindu followers. Buddhism, though a minority faith in the country, is linked historically with Nepal.

A monarchy throughout most of its history, Nepal was ruled by the Shah dynasty of kings from 1768, when Prithvi Narayan Shah unified its many small kingdoms. However, a decade-long Civil War by the Communist Party of Nepal (Maoist) and several weeks of mass protests by all major political parties led to the 12 point agreement of 22 November 2005. The ensuing elections for the constituent assembly on 28 May 2008 overwhelmingly favored the abolishment of the monarchy and the establishment of a federal multiparty representative democratic republic.

Population Structure	
Data	Size
Population	26,620,000 (2011)
Growth Rate	1.6%
Population below 14 Years old	39%
Population of age 15 to 64	57.3%
Population above 65	3.7%
The median age (Average)	20.07
The median age (Male)	19.91
The median age (Females)	20.24
Ratio (Male: Female)	1, 000:1,060
Life expectancy (Average)	66.16 Years
Life expectancy (Male)	64.94
Life expectancy (Female)	67.44
Literacy Rate (Average)	68.2% (According to the UNDP report 2011)
Literacy Rate (Male)	NA
Literacy Rate (Female)	NA

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3.2 BANGLADESH : Challenges To Collect Property Taxes in Bangladesh

(M A Quader Sarker)

3.2.1 Introduction

Emergence of globalization has immense impact on tax structure and on its systems of redistribution. Due to trade liberalization trade revenue is reducing day by day. In this situation revenue collection from internal resources should be the main source to the government exchequer to play the redistributive role as well as to perform other development activities. To attain the Millennium Development Goal (MDG) and to carry out the development process the country needs to rationalize its revenue collection composition with great emphasis on collection from internal resource. Property taxes can play a vital role for a developing country like Bangladesh for raising internal resources. If a property tax is to be successfully introduced in Bangladesh, the revenue board needs to carefully consider a wide range of issues and challenges.

3.2.2 Tax structure of Bangladesh - National Level

According to Article 152(1) of the Constitution of Bangladesh, taxation includes the imposition of any tax, rate, duty or impost, whether general, local or special, and tax shall be construed accordingly. Rate is a local tax imposed by local government on its residents or the property owners of the locality, a duty is a tax levied on a commodity, and an impost is a tax imposed for an entry into a country. Under the provision of article 83 of the Constitution, "no tax shall be levied or collected except by or under the authority of an Act of Parliament". The imposition, regulation, alteration, remission or repeal of any tax is dealt with by the 'Money Bill', but except in case of reduction or abolition of any tax, the 'Money Bill' cannot be introduced in the Parliament without the President's recommendation.

Bangladesh inherited a system of taxation from its past British and Pakistani rulers. The system, however, developed on the basis of generally accepted canons and there had been efforts towards rationalizing the tax administration for optimizing revenue collection, reducing tax evasion and preventing revenue leakage through system loss. The national board of revenue (NBR) is the apex tax authority of Bangladesh and it collects around 93% of total taxes. The NBR portion of total taxes includes:

- Customs Duty,
- Value Added Tax (VAT),
- Supplementary Duty (SD),
- Excise Duty,
- Income Tax,
- Foreign Travel Tax,
- Electricity Duty,
- Wealth Tax (collected as a surcharge of income),
- Turnover Tax (TT),
- Air Ticket Tax,
- Advertisement Tax,
- Gift Tax and Miscellaneous insignificant taxes,

Other taxes (amounting to around 7% of total taxes or 5% of total revenues) are often referred to as 'non-NBR portion' of tax revenue. These taxes include:

- Narcotics duty (collected by the Department of Narcotics Control, Ministry of Home Affairs),
- Land revenue (administered by the Ministry of Land and collected at local Tahsil offices numbered on average, one in every two Union Parishads),
- Non-judicial stamp (collected under the Ministry of Finance),
- Registration fee (collected by the Registration Directorate of the Ministry of Law, Justice and Parliamentary Affairs),
- Motor vehicle tax (collected under the Ministry of Communication).

In Bangladesh, the principal direct taxes are personal income taxes and corporate income taxes, and a value-added tax (VAT) of 15% levied on all important consumer goods. The top income tax rate for individuals is 25%. For the 2011/12 tax year (July 1, 2011–June 30, 2012) the top corporate rate was 45%. However, publicly traded companies registered in Bangladesh are charged a lower rate of 27.5%. Banks, financial institutions and insurance companies are charged the 45% rate. All other companies are taxed at the 37.5% rate. Effective 1 July 2011. The tax-GDP ratio was only 3.4% in 1972-73 and it remained below 9% until the introduction of VAT in the

country in 1991. The ratio was 9.8% in 1992-93 and although it was more than 9% in the successive years, it has only reached at 10%.

The present **land revenue** system of Bangladesh has its base in the east Bengal state acquisition and tenancy act 1950 which established a direct contract between the taxpayer and the government. Before the independence of Bangladesh, the total revenue demand of the government for agricultural land was taka 6.47 per acre: taka 3.75 as land revenue and taka 2.72 as other taxes (development and relief tax, and local rates). In 1972, the government exempted all owners having land up to 25 big has (8.33 acres) from paying land revenue by a Presidential Order. The revenue demand from landholders above 25 big has was kept as before (i.e., taka 6.47 per acre), but owners having land up to 25 big has were subject to only other tax of taka 2.72 per acre. In 1976, the Land Development Tax Ordinance was passed by which land revenue and other taxes were merged together to be called '**land development tax**' (LDT). Immediately after the independence, land revenue fell sharply because of a liberal attitude of the tax collection machinery and reduction in tax-base. In 1972-73, the land revenue was only taka 25 million (1.5% of total tax) and it increased continuously in nominal terms over the years.

The most important tax on the value of transferred property is the **non-judicial stamp tax** (levied under the Stamp Act 1899), which has been in existence since January 1899. The judicial stamp tax is being levied under the Court Fees Act 1870, although the levy of court fees originated in the introduction of the Bengal Regulation No. 38 of 1795.

Local level resource mobilization

Local level resource mobilization in Bangladesh has been very poor. There are two sources of resources for local governments: **(a)** collection of taxes and non-tax revenues such as various fees and tolls, income from hats, bazaars, sairat mahals and ponds, etc. and **(b)** grants from the central government.

Local governments depend heavily on the central government grants. Except Municipalities and City Corporations, they rely on very few sources of raising revenue. The main source of raising revenue by Zillah Parishads (District Councils) is the 'immovable property transfer tax (IPPT). Union Parishads (Councils) mainly collect chowkidari (village militia) tax, which barely covers wages and salaries of staff. Municipalities (Paurashavas) and City Corporations have varied sources of

revenue: taxes on the annual value of lands and buildings (commonly known as municipal tax), lighting rate, octroi (tax on import of goods for consumption, use or sale in the municipality; abolished in 1982), tax on professions, trades and callings, tax on advertisement, tax on vehicles other than motor vehicles and boats, tax on cinemas, dramatic and theatrical shows, etc. More than three-fourths of their income come from own sources. Tax collections are, however, affected by tax defaults and evasions.

3.2.3 Property Taxes in Bangladesh and Global Perspective

A property tax is a levy on property that the owner is required to pay. The tax is levied by the governing authority of the jurisdiction in which the property is located; it may be paid to a national government, a federated state, a county/region, or a municipality. A property tax is somewhat similar to a wealth tax, which existed in Bangladesh in the past.

However, unlike a wealth tax, in this case only a certain portion of an individual's tangible wealth is taxed at a certain rate, which is often a flat rate, but may vary under different circumstances or jurisdictions. The tax base may include, but is not limited to, a variety of assets such as real estate, land, family home, investment property, and private firms and forests lands.

Arguments in favour of a property tax

Arguments in favour of a property tax are many. First and foremost, a well-designed property tax improves fairness of a tax system and can effectively raise government revenue. Second, it can enhance economic growth through injecting investment in relatively more productive sectors of an economy, which may create significant forward and backward linkages. Finally and most importantly, such a tax has positive social effects as it can potentially reduce economic inequality.

Arguments against a property tax

There are arguments against a property tax as well. Due to valuations and accounting difficulties, property taxes systems often face high management costs, for both the taxpayer and the administrating authorities. For instance, in the Netherlands, the aggregated cost of the tax's yield was roughly five times than that of income tax. Similarly, in France, an introduction of the tax caused capital flight, brain drain, loss of jobs, and ultimately, a net loss in the tax revenue. As such, there

is a need to carefully examine the risks and uncertainties surrounding the tax in Bangladesh prior to its introduction.

The majority of the people in Bangladesh are highly likely to support the tax due to the fact that they will not fall under the purview of this new tax. However, the revenue board needs to be more cautious while designing the tax, particularly in providing exemptions and deductions. The fact is that a poorly designed tax could jeopardize the main objectives of the tax's introduction and can cause a premature demise, as seen in many developing and economically advanced economies.

Any well-designed tax can be a good source of revenue and can outweigh the negative aspects of the tax. In a country like Bangladesh, where income inequality is acute, rural and urban household income and wealth distribution is widely dispersed, which means a well-designed property tax may yield a number of dividends to the economy. For instance, revenue collected through this tax could be used to pay for local schools, parks, community sports, cultural and health centres and other amenities.

However, a solely revenue-driven tax policy may not achieve the desired objectives of this tax. To make it a success, there is a need for societal support, which is possible through an open and transparent engagement with potential taxpayers and other stakeholders, including the key political parties.

Furthermore, any introduction of a new tax could cause a tax culture shock, which is evident in developing economies but can also be seen in economically advanced economies. For instance, the introduction of a mining super profit tax in Australia caused a premature demise of a very popular prime minister in 2010. In a country like Bangladesh, where tax culture has yet to be established, any introduction of a property tax should be done with the utmost care and attention. If not, it may cause political discontent and voter dissatisfaction. To further complicate the matter, this could cause chaos in the society, which has long been controlled by a tiny segment of wealthy but politically influential group of people.

According to tax policy experts, the best way to implement a new tax is always a gradual transformation of the tax policy through a gradual introduction of this tax, and in the case of a property tax, an ideal solution could be imposing the tax in a lower rate. Further, the tax base needs to be defined.

The main areas of property tax may include investment properties such as unit or apartments, house, land including swamps and water bodies which could be used for real estate and housing. Lakes, swamps, canals and rivers in most cities in Bangladesh are often encroached upon by highly influential real estate developers. Including such future development sites into property tax may help reduce such encroachment.

Expensive family homes could also be included in the tax base, which could help reduce the existing high level increase of home or unit prices. However, there is a need to have a tax-free threshold for less expensive owner occupied homes or units. For instance, in a recent tax review in Australia, only family homes valued at \$2 million or more were proposed for such tax. Taxation experts and social welfare groups supported this measure as a way of making the tax system more equitable.

3.2.4 Economics of Property Taxation

Economists are well aware of the power, potential and elegance of land taxation. Being a fixed factor, land is bound to accumulate value over time as demand grows. The owners of this fixed factor therefore earn a huge rent that can and should be taxed at a reasonable rate both to finance government spending on public goods and also to avoid providing a tax haven for idle accumulation. Being a tax on rent, this taxation is very efficient because the tax incidence cannot be shifted by the landholders for whom the tax is intended.

This was the argument used by the well-known classical economists Adam Smith and David Ricardo in advocating the case for land taxation. Subsequent economic thinking has refined this argument to allow for the fact that capital improvements on land can add value and therefore excessive taxation could hurt these capital investments and reduce incentives to enhance the productivity of land. Modern property taxation therefore makes a distinction between pure land and capital invested in land to make it productive (farming, commercial structure, housing, etc.). The taxation is basically aimed at taxing the rent accruing to pure land owing to scarcity value.

Economists also argue for land taxation because in the absence of taxation, investment incentives can easily be distorted in favour of land holdings and real estate and away from taxed assets and activities that have a more positive effect on growth and employment. Indeed, without taxation there will be an excess demand

for land and real estate that can easily have a spiral effect on prices especially in a densely populated economy like Bangladesh with extremely limited land resources. So, properly designed property taxation can have a hugely positive effect in checking the growth of prices of urban properties in Bangladesh. Indeed, international evidence suggests that fiscal policy is one of the most potent instruments for influencing land pricing and land use.

Equity considerations can also be incorporated in the design of proper property taxation. In countries like Bangladesh much of the land holdings in rural areas are small and the farmers are mostly poor. Land taxation is not advocated for small holding farmers. The primary target for land and property taxation is land holdings and real estate in urban areas that have accumulated huge rents with no taxation. Much of the urban land owners are very rich and their wealth has soared with no effort simply through rocketing land prices. Even so, the property tax design could exempt the tax on owners of low-cost housing.

3.2.5 Status of Property Taxes in Bangladesh

The volume of foregone revenues from the absence of effective property taxation is obvious. While property transactions pay a nominal capital gain tax of 5.0% and other fees, these are assessed at artificially low official prices. The values were reset recently. Even so, these values are still four-five times below the market prices. Property owners also pay some minimal charges to the municipalities.

The National Policies on Property Taxes in Bangladesh

Property tax has been yet been directly introduced in Bangladesh and no national policies on property tax in Bangladesh have been yet formulated. The National Board of Revenue has been trying to impose tax on property, but till now it has not become possible. After long debate and discussion, only surcharge 10% of the tax of the assessed has been introduced by the Finance Act, 2011 in effect from 1st July, 2011. But such surcharge is applicable on the individual assessed whose net wealth exceeds 20 million TK (\$0.24 million).

There was a specific law named The Wealth Tax Act, 1963 for taxing the wealth which was repealed late on. There is another law named the Gift Tax Act for taxing the gift of both movable and immovable property with some exceptions. But the collection of Gift Tax is very much insignificant. Apart from the above scenario,

there are some provisions of property tax in various laws of Bangladesh and there are some scopes to collect property tax in Bangladesh. Property tax is collecting both in national and local level to some extent.

There is no definition of property in the Income Tax Ordinance, 1984 under which we are imposing tax on income from house property or on some other assets to some extent. But there is a definition of capital asset to impose tax on the gain or profit arising out of the transfer of capital asset.

Tax on the income from house property income

The annual income from house property is taxable as the other head of income under the Income Tax Ordinance, 1984 of Bangladesh. As per Section 20 of the said Ordinance there are seven heads of income. Section 20 runs as following:

“Save as otherwise provided in this Ordinance, all incomes shall, for the purpose of charge of income-tax and computation of total income, be classified and computed under the following heads of income, namely:

(a) Salaries

(b) Interest on securities

(c) Income from house property

(d) Agricultural income

(e) Income from business or profession

(f) Capital gains

(g) Income from other sources

So we see that income from house property is being taxed under the income tax law of Bangladesh.

Annual value is the basis to determine the income from house property. Clause (3) of section 2 of the Income Tax Ordinance, 1984 defines the term **annual value** as following:

“annual value” shall be deemed to be-

(a) in relation to any property let out, -

- (i) *the sum for which property might reasonably be expected to let from year to year and any amount received by letting out furniture, fixture, fittings etc.;*
or
- (ii) *where the annual rent in respect thereof is in excess of the sum referred to in paragraph (i), the amount of the annual rent;*

Income from house property is taxable under section 24 of the Income Tax Ordinance, 1984. Section 24 runs as following:

“(1) The tax shall be payable by an assessed under the head “Income from house property” in respect of the annual value of any property, whether used for commercial or residential purposes, consisting of any building, furniture, fixture, fittings etc. and lands appurtenant thereto of which he is the owner, other than such portions of the property as he may occupy for the purposes of any business or profession carried on by him, the income from which is assessable to tax under this Ordinance.

(2) Where any such property as is referred to in sub-section (1) is owned by two or more persons and their respective shares are definite and ascertainable, such persons shall not constitute and shall not be deemed to be, an association of persons; and for the purpose of computation of the income of an assessed in respect of that property, only such part of such income as is proportionate to the share of the assessed shall be reckoned as his income from that property.

House property investment analysis: If unexplained, then income

In the Income Tax Law of Bangladesh, there is no provision to tax on property directly, but the investment in the house property must be explained with the source of fund of the assessed. If the investment in the property is unexplained, the tax shall be imposed on the invested amount.

Previously sections 19B and 19BB of the Income Tax Ordinance, 1984 dealt with the tax on the investment on the house property where there was no explained source of fund regarding such investment. The sections run as following:

(19B) Special tax treatment in respect of investment in house property–

Notwithstanding anything contained in this Ordinance or any other law for the time being in force, no question as to the source of any sum invested by

any person in the construction or purchase of any building or apartment shall be raised if the assessed pays, before the assessment is completed for the relevant assessment year, tax at the rate of –” omitted by Finance Ordinance 2007

“(a) taka three hundred per square meter in the case of a building or apartment the plinth area of which does not exceed two hundred square meter for the area of Gulshan Model Town, Banani, Baridhara, Defence Officers Housing Society (DOHS), Dhanmondi Residential Area, Lalmatia Housing Society, Uttara Model Town, Bashundhara Residential Area, Dhaka Cantonment, Motijheel Commercial Area, Dilkusha Commercial Area, Kawran Bazar Commercial Area of Dhaka and Khulshi Residential Area, Panchlaish Residential Area of Chittagong ;

(b) taka five hundred per square meter in the case of a building or apartment the plinth area of which exceeds two hundred square meter for the areas mentioned in clause (a);

(c) taka two hundred per square meter in the case of a building or apartment the plinth area of which does not exceed two hundred square meter for the area other than the areas mentioned in clause (a);

(d) taka three hundred per square meter in the case of a building or apartment the plinth area of which exceeds two hundred square meter for the area other than the areas mentioned in clause (a)]” {Subs by F.A. 2006 subsequently by F. O. 2007}

“19BB. Special tax treatment in respect of investment in land property.-

Notwithstanding anything contained in this Ordinance or any other law for the time being in force, no question as to the source of any sum invested by any person in purchasing of any land shall be raised if the asses see pays, before the assessment is completed for the relevant assessment year, tax at the rate of seven and half per cent] of the deed value of the said land.]” {INS by F.A. 2002, subsequently omitted by FO 2007 (Subs. for “five per cent” by F. A. 2006}

At present there is no such provision. But one has to explain his/her/its investment in house property like any other investment to be explained with the source of fund. If it is unexplained, it will become taxable i.e. the cost of the property which is unexplained shall be taxable as income from other sources.

Capital gains on Property

When a property is transferred, provided that it is a capital asset, tax is payable on the gain of such transfer. The relevant provisions of law are given below:

Definition of Capital Asset: As per Bangladesh Income Tax Law, “capital asset” means property of any kind held by an asses see, whether or not connected with his business or profession, but does not include: (a) any stock-in-trade (not being stocks and shares), consumable stores or raw materials held for the purposes of his business or profession; (b) personal effects, that is to say, movable property (including wearing apparel, jewellery, furniture, fixture, equipment and vehicles), which are held exclusively for personal use by, and are not used for purposes of the business or profession of the asses see or any member of his family dependent on him; and(c) agricultural land in Bangladesh, not being land situated -

(i) in any area which is comprised within the jurisdiction of Dhaka, Narayanganj and Gazipur districts, Chittagong Development Authority (CDA), Khulna Development Authority (KDA), Rajshahi Development Authority (RDA), a City Corporation, Municipality, Paurashava, Cantonment Board; or

(ii) in any area within such distance not being more than five miles from the local limits of Rajdhani Unnayan Kartripakya (RAJUK), Chittagong Development Authority (CDA), Khulna Development Authority (KDA), Rajshahi Development Authority (RDA), a City Corporation, municipality, Paurashava, Cantonment Board referred to in paragraph (i), as the Government may having regard to the extent of, and scope for, urbanization of that area and other relevant considerations, specify in this behalf by notification in the official Gazette;(Section 2, clause 15)

For capital gain the Transfer of property is must. The term transfer is defined as following:

“Transfer”, in relation to a capital asset, includes the sale, exchange or relinquishment of the asset, or the extinguishment of any right therein, but does not include-

- (a) any transfer of the capital asset under a gift, bequest, will or an irrevocable trust;
- (b) any distribution of the assets of a company to its shareholders on its liquidation; and
- (c) any distribution of capital assets on the dissolution of a firm or other association of persons or on the partition of a Hindu undivided family;

(Section 2(66) of the Income Tax Ordinance, 1984)

Provisions of charging capital gain

As per Bangladesh Income Tax Law, *“Tax shall be payable by an asses see under the head “Capital gains” in respect of any profits and gains arising from the transfer of a capital asset and such profits and gains shall be deemed to be the income of the income year in which the transfer took place.*

(1) The income under the head “Capital gains” shall be computed after making the following deduction from the full value of the consideration received or accruing from the transfer of the capital asset or the fair market value thereof, whichever is higher, namely:-

- (a) any expenditure incurred solely in connection with the transfer of the capital asset; or*
- (b) The cost of acquisition of the capital asset and any capital expenditure incurred for any improvements thereto but excluding any expenditure in respect of which any allowance is admissible under any provisions of sections 23, 29 and 34.*

(2) For the purpose of this section, “cost of acquisition of the capital asset” means-

- (i) Where it was acquired by the asses see by purchase, the actual cost of acquisition; and*
- (ii) where it became the property of the asses see-*
 - (cc) under a deed of gift, bequest or will; or*
 - (ccc) under a transfer on a revocable or irrevocable trust; or*
 - (d) on any distribution of capital assets on the liquidation of a company; or*

(e) on any distribution of capital assets on the dissolution of a firm or other association of persons or the partition of a Hindu undivided family; the actual cost of acquisition to the previous owner of the capital asset as reduced by the amount of depreciation, if any, allowed to the previous owner; and where the actual cost of acquisition to the previous owner cannot be ascertained, the fair market value at the date on which the capital asset became the property of the previous owner:

- (3) Where in the opinion of the Deputy Commissioner of Taxes the fair market value of a capital asset transferred by an asses see as on the date of transfer exceeds the full value of the consideration declared by the asses see by an amount of not less than fifteen per cent of the value so declared, the fair market value of the capital asset shall be determined with the previous approval of the Inspecting Joint Commissioner.*
- (4) Where in the opinion of the Deputy Commissioner of Taxes the fair market value of a capital asset transferred by an asses see as on the date of the transfer exceeds the declared value thereof by more than twenty-five per cent of such declared value, the Government may offer to buy the said asset in such manner as may be prescribed.*
- (5) Notwithstanding anything contained in this section or section 31, where a capital gain arises from the transfer of a capital asset which immediately before the date on which the transfer took place was being used by the asses see for the purposes of his business or profession and the asses see has, within a period of one year before or after that date, purchased a new capital asset for the purposes of his business or profession, then, instead of the capital gain being charged to tax as income of the income year in which the transfer took place, it shall, if the asses see so elects in writing before the assessment is made, be dealt with in accordance with the following provisions of this sub-section, that is to say-
 - (a) if the amount of the capital gains is greater than the cost of acquisition of the new asset,-
 - (i) the difference between the amount of the capital gain and the cost of acquisition of the new asset shall be charged under section 31 as income of the income year, and***

(ii) for the purposes of computing in respect of the new asset any allowance under the Third Schedule or the amount of any capital gain arising from its transfer, the cost of acquisition or the written down value, as the case may be, shall be nil, or

(b) if the amount of the capital gain is equal to or less than the cost of acquisition of the new asset,-

(i) The capital gain shall not be charged under section 31, and

(ii) for the purposes of computing in respect of the new asset any allowance under the Third Schedule or any income under section 19(16) or the amount of any capital gain arising from its transfer, the cost of acquisition or the written down value, as the case may be, shall be reduced by the amount of the capital gain

Provided that where in respect of the purchase of a new capital asset consisting of plant or machinery, the assessee satisfies the Deputy Commissioner of Taxes that despite the exercise of due diligence it has not been possible to make the purchase within the period specified in this sub-section, the Deputy Commissioner of Taxes may, with the prior approval of the Inspecting Joint Commissioner, extend the said period to such date as he considers reasonable.

- (6) Notwithstanding anything contained in this section or section 31, where a capital gain arises from the transfer of a capital asset being Government securities then no tax shall be charged under section 31.*
- (7) Notwithstanding anything contained in this section or section 31, where a capital gain arises from the transfer of capital being buildings or lands to a new company registered under the Companies Act, 1913 (VII of 1913) or Companies Act, 1994 for setting up of an industry, and if the whole amount of capital gain is invested in the equity of the said company, then the capital gain shall not be charged to tax as income of the year in which the transfer took place.*
- (8) Notwithstanding anything contained in this section or section 31, where a capital gain arises from the transfer of a capital asset of a firm to a new company registered under the Companies Act, 1913 (VII of 1913) or Companies Act, 1994, and if the whole amount of the capital gain is invested in the equity*

of the said company by the partners of the said firm, then the capital gain shall not be charged to tax as income of the year in which the transfer took place.

Collection of Tax from persons engaged in real estate or land development business

Section 53FF of the Income Tax ordinance, 1984 has the provisions regarding the collection of Tax from persons engaged in real estate or land development business which runs as following:

“Any person responsible for registering any document for transfer of any land or building or apartment, under the provision of Registration Act 1908 (XVI of 1908), shall not register the document unless tax is paid at the following rate by the transferor who is engaged in real estate or land development business, (a) in case of building or apartment, constructed for residential purposes, situated:

- (i) at Gulshan Model Town, Banani, Baridhara, Motijeel Commercial Area and Dilkusha Commercial Area of Dhaka, taka two thousand per square metre;*
 - (ii) at Dhanmondi Residential Area, Defence Officers Housing Society (DOHS), Mahakhali, Lalmatia Housing Society, Uttara Model Town, Bashundhara Residential Area, Dhaka Cantonment Area, Karwan Bazar Commercial Area of Dhaka and Panchlaish Residential Area, Khulshi Residential Area, Agrabad and Nasirabad of Chittagong, taka one thousand and eight hundred per square metre;*
 - (iii) in areas other than areas mentioned in sub-clauses (i) and (ii), taka eight hundred per square metre;*
- (aa) in case of building or apartment or any space thereof, constructed not for the residential purposes, situated:*
- (i) in areas mentioned under sub-clause (i) of clause (a), taka eight thousand per square metre;*
 - (ii) in areas mentioned under sub-clause (ii) of clause (a), taka six thousand per square metre;*
 - (iii) in areas mentioned under sub-clause (iii) of clause (a), taka two thousand per square metre;*

(bb) (i) in case of land situated in any City Corporation, Paurashava or Cantonment Board to which the document relates and on which stamp duty is chargeable under the Stamp Act, 1899 (Act No. II of 1899) at the rate of five percent up to August 31, 2009 and two percent from September 1, 2009 on the deed value of the property:

(ii) in case of non-agricultural land situated outside the jurisdiction of any City Corporation, Paurashava or Cantonment Board to which the document relates, and on which stamp duty is chargeable under the Stamp Act, 1899 (Act No. II of 1899)] at the rate of five percent, up to August 31, 2009 and one percent from September 1, 2009 on the deed value of the property.”

Local Capacities in Collecting Property Taxes

Local governments in Bangladesh have several options at hand to finance their activities and pursue their fiscal policy. These options include the imposition of taxes and the generation of non-tax revenues through fees, levies, cost recovery and user charges, property and investment income, domestic and foreign borrowing, the sale of assets and domestic and foreign grants.

Urban Local Governments (ULGs) in developing countries are in dire need of resources not only for investment to meet the increasing demand of growing urban population but also for maintenance of the existing services. But the resources of the municipal bodies are inadequate; infrastructures are in poor condition and services maintenance is neither enough nor would cover the new expansions. Inefficient governance of the municipal bodies is partly responsible for this. Holding tax plays an important role in own revenue of Pourashavas. About 35-45% revenue comes from holding tax.

If the amount of holding tax is increased, this will help Pourashavas gradually become self-financed. With the rapid urban growth all over the world, the demand for various services and facilities are increasing radically. But due to resource constraint, authorities cannot provide all these services. Financial support is necessary to provide these facilities. The municipality has to depend on its own revenue collection.

The resources of the municipal bodies are inadequate, infrastructures are in poor condition and maintenance of services is neither enough nor covers the new expansion. It also failed to make the reluctant residents to pay taxes. The shortage

of finance has always plagued the urban government in attaining the optimum level of infrastructure and basic services. Under the present system, few urban government units are capable to generate sufficient resources to meet their capital and recurrent costs. Moreover, they have little incentive to take responsibility for their actions, including the collections of taxes.

In Bangladesh, municipalities need to rely on the fixed amount allocated in the annual budget. Except some municipalities, none has potential earning sources (like harbour, expensive hotels, airports, etc.) excluding taxation. Again the sources of collecting tax are limited. Holding tax is the part of property tax and everyone has to pay it. But the amount is not increasing according to the population size because of the ineffectiveness in revenue collection. Municipality has its own ordinance and under the ordinance there are some specific rules. Any municipalities may collect/gather fiscal amount by enforcing these rules/laws.

So, efficient law enforcement will certainly raise the amount of holding tax. It is important for municipalities to introduce a standard and consistent policy for collecting accounts receivables, and for dealing with delinquent and defaulting payers. By instituting consistent policies and procedures, customers and taxpayers may be encouraged to pay their due taxes to avoid actions against non-payment.

Process of Property Tax Assessment by Local Authority

Taxes and rates are charged in terms of the percentage of the annual value of buildings and lands, conservancy rates and street light in the municipalities. The assessors are appointed by such municipalities. Assessors as regular employees who prepare the assessment valuation list both for regular assessment and general assessment/reassessment. The method of rental valuation is employed in reassessing properties in the Municipalities as per the Municipal Committee (Taxation) Rules, 1960.

Although according to the Pourashava Taxation Rules, 1960 annual value is determined by the submission of forms which includes returns of rent, the correct description of the building from owners and the inspection of the assessor to justify it. The tax assessors seldom go for checking the actual rent. The assessors generally ask the house owner, but in some cases the tenants inform the rental rate of a house.

The rental value per unit of building space for different types of structures, are then applied some what judgmentally, to other similar structures in the area. In case of publication of notice for assessment, very few public announcements are done by the authority in the locality. As local representatives, the mayor and the ward commissioners are very well known to the people, who can easily serve such types of notice. The tax payers are allowed to appeal against assessed value within one month of the preparation of the assessment list (Municipal Committee Taxation Rules, 1960).

3.2.6 Problems Associated with Holding Property Taxes in Bangladesh

Ownership identification: Ownership identification for imposition of property tax is the major reason for the problem of determining annual rental value. In case of joint ownership, tax imposition may sometimes become a problem. Some of the owners in the non-income group may actually be unable to pay taxes. But in case of income earners, the problem arises as to who should pay on other's behalf. Again, there may be absentee land owners. The tenant or agent of a property may not like to pay tax.

- ***Irregularity of assessment***

In case of record keeping during reassessment, the assessor cannot keep complete record when an addition to a building is made and rent value is increased. Assessor and assistant assessor prepare the assessment valuation list both for regular assessment and general assessment or reassessment that is done periodically at an interval of five years.

But regular assessment is seldom performed by the local authority. Since property does not become taxable until it is built upon, it is not easy to say who would be liable for tax payments without watching regularly the new constructions, additions and alterations. Lack of information makes it difficult to change additional tax on a person even when it has become due on him. This situation also increases the possibility of corruption and tax evasion. Again because of irregular maintenance of collecting information and records, some of the holdings cannot physically be identified.

- ***Illicit collusion between tax payer and assessor***

Because of the illicit collusion between tax payer and assessor, the rental value per unit of building space for different types of structures are applied, somewhat judgmentally, to other, similar structures in the area which indicates a great undervaluation in property assessment in all jurisdiction. It was, however, not the purpose of this study to look into assessment of how much property value is undervalued for such reason.

- ***Lack of political will***

One of the fundamental reasons that hinder regular assessment is fear of adversely affecting the popularity of the elected officials of the Municipality. The elected personnel seem to believe that regular reassessment would certainly increase tax burden on the Municipality holdings, which in turn would jeopardize their chance of re-election.

- ***Lack of assessors***

The most striking feature of the current assessment regime is severe deficiency in human resources. The quality and quantity of assessment resources of the Municipality are simply inadequate to perform the job.

- ***Irregularity of billing***

The tax collectors deliver the tax bills from door to door. Investigation revealed that tax bills are not regularly handed over to the tax payers. Authority cannot properly execute its duty frequently, because of the indolence of the municipal officials.

- ***Ignorance of people***

Most of people do not know about the rate of the Holding (Property) tax and the collection procedure of the holding tax. So they have a little chance to know what should be the correct holding tax rate. So, very few people appeal against assessment. Ignorance has great impact on assessment procedure too. At the time of filling the forms, people do not provide the actual information they have to put. They put the information based on their assumption.

- ***Unfavourable collection procedure***

Collection procedure is followed by both manually and through bank in the study area. In case of manual dealings, there is scope for occurring corruption, especially

tax evasion, which is occurred because of the illicit collusion between tax payer and collectors.

- ***Lack of political will to enforce penalties***

There is a punitive way of tax collection available to the Municipality. Government empowered the Municipality to recover all arrear through Distress Warrant (DW), sale of movable property or even by attachment and sale of immovable property belonging to the person concerned. Sometimes there is lack of political will and initiatives to enforce penalties permitted by law.

IT Strategy to Support Proper Tax Administration in Bangladesh

In the age of technological revolution all the tax offices keep their records and provide the service to the taxpayers manually, which results time consuming. As a result the revenue authority cannot provide the service to the tax payers in a timely manner according to the expectation which hinder the accountability and transparency in the tax administration.

Recently the income tax department has introduced Management Information System of Taxes (MIST) and some other initiatives under which all taxes zone as well as circle will be under IT coverage

On the other hand different customs house is using the modern technology to facilitate the service to the clients. National board of revenue web page also is helping the tax payers to have some sorts of information regarding existing tax laws and rules, tax return etc. but not the information is not periodically updated and detailed, as to people's needs. The automation system taken by NBR seems fragmented, partial and not comprehensive. Still there is lack of coordination between the different government agencies to share the information related to tax. But the whole system should be integrated in the massive advanced technology use to capitalize the benefit of the technological progress.

The Property Tax Administration, with its huge database is a regular need for updating information through computerization. Maintaining a fiscal cadastre with information of households of holdings and updating it with the latest change in status such as change in tax payment and arrears in itself is a huge task. An encouraging factor is that some Municipalities in Bangladesh have already introduced computers under the IDA-funded Municipal Services Project (MSP).

Potential Area for Evading and Avoiding Property Taxes

- *No link between NBR and Local Authorities*

The local authority allocates holding numbers for the house property. But till now, they do not share this information with NBR. In fact many house properties have even no holding number. So NBR has no actual number of house properties in its hand. Hence there are logical chances to evade and avoid property taxes.

- *Determination of Annual value/Valuation of income*

The house rent has been increasing in Bangladesh day by day rapidly. Over the last 5 to 6 years, it has become almost double. But the tax on the rental income of the house property is not rising with the same rate.

- *No database of house property*

The proper database of house property is a must for the proper collection of tax income from house property. But in Bangladesh, the taxing authorities have no database of house property. So the determination of income on house property and the collection of tax from income from house property prove to be quite difficult in Bangladesh.

3.2.7 Challenges of Collecting Property Taxes in Bangladesh

The road to effective tax reform is always difficult, and Bangladesh is no exception. If a property tax is to be successfully introduced in Bangladesh, the revenue board needs to carefully consider a wide range of issues.

Effective tax reform will require open and transparent engagement with stakeholders, clear communication through the media to help people understand the implications of this new tax, making the tax as simple as possible to minimize compliance costs for taxpayers, as well as administrative and compliance costs for the board and the taxpayers. A poorly designed and untested tax reform is always risky and can cause unrest and chaos as well as political unrest and discontent.

Thus, to make the property tax in Bangladesh a successful and sustainable tax reform, the board should adopt a fair and transparent approach and conduct an in-depth analysis of the robustness of the property tax before its large scale introduction in Bangladesh for overcoming the challenges. However, the following challenges have to be considered while introducing property taxes in the country:

- Cost of collection may override total collection of property tax
- Cost of paying tax may also be high at assessor's end
- Administering property tax may be difficult
- Valuation of property is difficult in Bangladesh as there is no specific valuation agency
- People are already overburdened of different types of taxes. They pay municipal tax for the property to the local authority, pay income tax for rental income, pay capital gain tax for gain on sale of property and also surcharge for owning more than TK. 20 million wealth
- Poor recording system of land & building is another challenge for collecting taxes
- Limited use of ICT tools is one of the challenges
- Property tax base is very low
- Needs capacity buildings of collecting authority

Strategic Plan for Collecting Property Taxes

It has been observed that there is certain scope to collect property tax mainly from the income from house property. In true sense, there is no property tax law in Bangladesh. Meanwhile, there is a healthy on-going debate in Bangladesh on the subject of the introduction of property taxation.

Opponents of this tax argue that this is a difficult tax to administer and the yield would be low relative to the cost of collection. In this analysis, I will argue the critical need for introducing this taxation not only with a view to making this a potent source of revenue for urban financing, but even more importantly to correct the severely distorted incentives for resource allocations and also to moderate the spiralling urban land prices.

The tax is also highly recommended on equity grounds. The cost of collection argument in this twenty first century of information technology is overstated and to my mind it is more a convenient excuse to avoid taxation by the rich and powerful who own most of the property and have a huge presence in politics, business and government.

The way forward

The past cannot be changed but strong actions can be taken now to check the further growth of land prices, divert resources to productive sectors and provide substantial revenues to the government through a well-designed urban land and property taxation. A number of factors will be important for the proper design of this taxation, these are:

- i. A proper survey and computerization of land and property ownership is needed.
- ii. Property must be valued appropriately in line with current market prices.
- iii. Capital gains tax must be implemented with no exception irrespective of the source of the gain, i.e. including gains from property ownership and stocks.
- iv. The tax rate must be set at a reasonable level both for capital gains when property is transacted and for property ownership. For example a rate of 15% on true capital gains from property transactions seems reasonable. Similarly an annual property tax of 1.0% on the market based value of property would appear to be a reasonable way to start. Low-cost home owners may be exempted. Other costs of property transactions must be streamlined to reduce transaction costs and promote the housing market.

Implementation will face challenge as the lobby against property taxation can be powerful in view of the ownership pattern of property.

One way to address this challenge is to link property taxes with municipal services. Property taxes than become akin to betterment taxes. Municipal or city governments will typically be assigned this tax who will then use these resources to provide better urban services.

A second challenge is the weak implementation capacity of city governments. To address this constraint, the property tax implementation can initially start with focus on the five major areas of Dhaka: Gulshan, Baridhara, Banani, Eskaton and Dhanmandi. Once proper valuation and ownership registration of properties in these areas are completed and lessons of the pilot are internalized, implementation can then be expanded to the rest of the urban centres of the country.

With modern information technology, registration, valuation and record keeping can be hugely simplified. Payments of taxation can be done online. The technology is simple and easily available and implementable. To avoid the risk of non-payment, capital gains on property taxation can be collected at the time of transaction involving registration of ownership transfer. If there is a strong political will, implementation of an effective system of property taxation need not be an impossible challenge.

3.2.8 Conclusion

Any well-designed tax can be a good source of revenue and can outweigh the negative aspects of the tax. In a country like Bangladesh, where income inequality is acute, rural and urban household income and wealth distribution is widely dispersed, which means a well-designed property tax may yield a number of dividends to the economy. For instance, revenue collected through this tax could be used to pay for local schools, parks, community sports, cultural and health centres and other amenities.

However, a solely revenue-driven tax policy may not achieve the desired objectives of this tax. To make it a success, there is a need for societal support, which is possible through an open and transparent engagement with potential taxpayers and other stakeholders, including the key political parties.

In a country like Bangladesh, where tax culture has yet to be established, any introduction of a property tax should be done with the utmost care and attention. If not, it may cause political discontent and voter dissatisfaction. To further complicate the matter, this could cause chaos in the society, which has long been controlled by a tiny segment of wealthy but politically influential group of people.

The road to effective tax reform is always difficult, and Bangladesh is no exception. If a property tax is to be successfully introduced in Bangladesh, the revenue board needs to carefully consider a wide range of issues. Effective tax reform will require open and transparent engagement with stakeholders, clear communication through the media to help people understand the implications of this new tax, making the tax as simple as possible to minimize compliance costs for taxpayers, as well as administrative and compliance costs for the board and the taxpayers.

A poorly designed and untested tax reform is always risky and can cause unrest and chaos as well as political unrest and discontent. Thus, to make the property tax in Bangladesh a successful and sustainable tax reform, the board should adopt a fair and transparent approach and conduct an in-depth analysis of the robustness of the property tax before its large scale introduction and overcoming the challenges in Bangladesh.

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3.3 PHILIPPINES : Getting the right Mix in Property Tax Policies & Administration

(Milwida M. Guevara)⁵

3.3.1 Introduction

Time was when the real property tax raised one-fourth of the revenues of local governments in the Philippines. Its revenue importance began to weaken starting 1991 after the central government devolved more resources and additional responsibilities to local governments. The Local Government Code of 1991 transferred 40% of the internal revenue collection to local government units (LGUs), compared with a former 20% share.

In exchange, the LGUs were made primarily responsible for delivering services on basic health, community-based forestry programs, agricultural services, social welfare, tourism, solid waste disposal, and low cost housing. Devolution of responsibilities brought about an increase in the expenditure share of LGUs from 9.3% in 1990 to 23.87% in 2008.

Level of Government	1990	2001	2002	2003	2004	2008
Central	90.7	75.10	75.59	78.72	71.72	76.13
Local	9.3	24.90	24.41	21.28	28.28	23.87

With the increasing pressure to finance devolved services, a logical common assumption is that LGUs would take the challenge of strengthening their revenue collection. A study by Roy Bahl and J. Martinez-Vazquez found that “fiscal decentralization drives the intensity of use of the property tax.”⁶

⁵ Undersecretary, Department of Finance, Republic of the Philippines, 1994-2000, currently, President, Synergia Foundation, Inc. www.synergia.org.ph

⁶ Roy Bahl and J. Martinez-Vazquez, “Tax in Developing Countries: Current Practice and Prospects”, Andrew Young School of Policy Studies, Georgia State University, December 2006

However, such relationship has not been observed in the Philippines. The property tax has scaled down in importance. In 2010, it only accounted for 10.74 percent of total revenues of local governments. It has been dwarfed by transfers from the central governments that have doubled in magnitude. What has stymied the growth of the real property tax? It is the wrong mix of policy and administration.

Table 2 Distribution of Revenues of Local Governments in the Philippines, by Source

Year	Total (milpesos)	Grants (%)	Real property Tax(%)	Business taxes(%)
1989	14,461	34.36	25.43	12.45
1995	66,489	63.32	12.50	11.04
1999	121,550	63.58	10.91	11.53
2004	175,398	64.92	12.35	12.44
2010	316,173	64.82	10.74	10.22

3.3.2 The Potential of the Real Property Tax (RPT)

The RPT can be a policy tool to raise revenues for LGUs, promote fairness in tax action, and support intensive land utilization. In addition, the tax is imposed on local residents and prevents tax exporting where some of the tax burden is passed on to residents of other LGUs. Fiscal accountability is enhanced when the costs of public services are financed by residents who benefit from them through local taxes or user charges.

The property tax can be a stable revenue source since market values are relatively more stable compared to income and sales. Land and building are visible and difficult to hide and makes tax evasion less likely.

The property tax can be a fair tax. Ownership of properties is an indicator of the ability to pay. Increases in property values that are attributable to government infrastructure are considered “unearned increments” and can be ploughed back to the public through the property tax. Corollary, property assessments that based on the “highest and best use of the land” can induce intensive land utilization. The proposal to impose an idle land tax in the Philippines was based on this concept, i.e. an idle land should be assessed based on the prevailing land use in a locality.

3.3.3 Real Property Taxation in the Philippines⁷

Provinces, cities, and municipal governments within the Metropolitan Manila area are given the power to impose levies on real properties. The tax applies to all forms of real property such as land, buildings, improvements, and machinery. Exemption is given to real properties owned by government, charitable institutions, church as cooperatives, and those that are used in the supply of water and electric power. Equipment for pollution control and environment protection is not subject to tax.

The base of the tax, or the assessment level, is only a fraction or a percentage of the market value of the land. The assessment levels are differentiated depending on land use:

Land use	Assessment Levels
Residential	20%
Agricultural	40%
Commercial, Industrial and Mineral	50%
Timberland	20%
Special classes: cultural, scientific	15%
Hospital, and water districts	10%

Assessment levels for improvements are also differentiated based on land use and market value. For example, residential buildings with a market value of P 10.0 million (\$240,963) and above are taxed on 60 percent of market value. The assessment level is higher at 80 percent if the building is used for commercial purposes.

The local legislative councils are mandated to enact the assessment levels to be used in their localities. However, these cannot exceed the maximum levels that are authorized under the Code. The Code sets a minimum rate of 0.25% (0.5% for cities) and maximum rates that can be imposed on real properties:

⁷ The back ground on real property taxation was written by the author as part of a book on **Land Taxation in Practice: Selected Case Studies** that was authored by Richard Bird and Enid Slack, World Bank, March, 2002.

Taxing Authority ⁸	Tax Rate
Province	1%
City and Municipality in Metro Manila	2%

Under the principle of fiscal autonomy, assessment levels and tax rates can vary among different local government units (LGUs) as long as they are within the ceilings that are prescribed under the law. Local legislative council share mandated to enact the assessment levels to be used in their localities. However, these cannot exceed the maximum levels that are authorized under the Code.

3.3.4 Other levies in Property Tax

Local governments are given the power to additional levies based on real properties:

- A Special Education tax (SEF) of one percent is imposed on the same base i.e. assessed values of real properties. The proceeds are ear marked for public education.
- An idle land tax can be imposed to optimize land utilization and discourage land speculation. It is an additional levy of five percent (5%) on: 1) agricultural lands with an area of more than one hectare an done-half of the land remains;2) non-agricultural lands with an area of 1,000m² which remain unimproved ; and3) unimproved residential lots in subdivisions.
- A special levy on lands benefited by public work projects that are financed by national or local governments can be collected. The levy should not exceed sixty percent of the actual costs of the project and should be apportioned among concerned land owners based on a formula to be established by the local legislative council.

⁸ The province is composed of a cluster of municipalities and component cities. The provincial government is responsible for providing tertiary health services, agriculture extension services, and enforcement of laws on environment, social welfare services, and provincial infrastructure. The municipality is composed of a cluster of barangays (villages) and is responsible for primary health care.

3.3.5 Administration of the Tax

Real properties are appraised based on “current and fair” market value. This is established based on samples of sales transactions in the locality where the property is located. Machinery and improvements are valued based on their replacement costs, or acquisition costs with provision for depreciation. Local assessors prepare a schedule of market value of real properties and submit it to the local legislative assembly for legislation. The tax begins to accrue on the first of January of every year and can be paid in four equal instalments before the office of the local treasurer. A discount (10% to 20%) is available to tax payers who pay it in advance while late payments are subject to a 2% surcharge every month to a maximum of 36%. Real properties can be sold by LGUs at public auction to recover delinquent taxes.

3.3.6 The Politics of it all

Prior to the enactment of the Local Government Code in 1991, municipal governments had the power to impose the real property tax. The Philippine Congress withdrew such power, except for the municipalities within Metro Manila. The Code mandated provincial governments with the power to impose the real property tax. Collection is shared among the province (35%), municipalities (40%) and the barangay/village (25%) where the property is located. In the case of Metro Manila, the 35% share is given to the Metropolitan Manila Authority. Cities retain seventy percent (70%) of the collection and 30% is allocated to the barangay/village share.

The withdraw of the power of municipal governments to impose the tax has led to animosities between the province and its component municipalities. Municipal governments complain that since they do all the work, they should not remit any part of their collection to the provinces. In turn, provinces do not remit what is due to municipal governments in time.⁹

But the most serious consequence of this tug-of-war is not just political but economic. Provinces have sat on the up dated values that have been proposed by municipalities. Among others, this is because the schedule of market values has to

⁹ The Commission on Audit in its 2008 Annual Financial Reports for LGUs reported that the provinces of Abra, Camarines Norte, Masbate, Sorsogon and Isabela, Palawan as well as Calamba City, Iriga City, Legaspi City failed to remit the shares to their component municipalities and barangay.

be enacted by the local legislative council. As a result, values have remained stagnant. In some LGUs, the values are of vintage 1996.

The revision of market values is also subject to intense debates in city councils, which contributes to the failure of many LGU store value properties regularly. The Department of Finance notes that less than one – half of LGUs in the country complied with the revaluation requirement in 2000. The number of compliant LGUs dwindled further to 24% in 2003.¹⁰

3.3.7 Structural Infirmities of the Tax¹¹

The full - market value of the real properties is not fully captured into there venue-stream. The tax base or the assessed value is merely a fraction of the market value. If this is not enough to weaken the base, Congress prescribed different percentages depending on land use;¹² 20% for residential and timberlands; 40% for agricultural lands, and 50% for commercial and industrial lands.

Buildings are also taxed on a fraction of their market values and the ratios vary depending on whether buildings are residential, commercial or industrial. Differentiated assessment levels introduce biases on land uses and distort decisions on how lands should be utilized. The lower assessment level on residential lands 20% versus 40% on agricultural lands presents an incentive for land owners to convert farm lands into subdivisions. Differentiated assessment levels introduce opportunities for tax avoidance and corruption through the use of discretion on land use classification.

The structural infirmities of the law on property taxation, the absence of regular property valuation, and inefficiencies in tax administration result to a low tax burden. The effective tax rate (ETR) or the ratio of actual collection to the tax base was estimated at 0.75%. If tax collection were related to market values, the ETR is only 0.067% implying that the realty tax paid by the tax payer is only P0.07 for every

¹⁰ Erlito Pardo, “Issues in the Effective Exercise of LGU Taxing Powers” in Local Government Bureaucracy and local Fiscal Administration, Preschle and Sosmena, eds. **Local Government Development Foundation**, 2006.

¹¹ Milwida M. Guevara, “Finance and the City , Plus Provinces and Municipalities : An Assessment of Local Tax Systems” a Study prepared for the Decentralization Program, GTZ, July 2010.

¹² The Department of Finance proposed the use of market values as the tax base in 1991 but its proposal was rejected by Congress.

P100 of market value.¹³ Similar studies estimated low ETRs, one-tenth of 1%¹⁴ and 0.6% for residential lands and 0.3% for residential buildings.¹⁵ Dillinger estimated a tax liability of US \$3.80 of P157.70 per property.¹⁶ This figure is within the national average of P92.67 to P231.35, the average revenue per parcel of land from cities.¹⁷

3.3.8 A Difficult Tax to Implement

Contrary to perceptions, the administration of the real property tax is not a simple matter. Taxable properties have to be identified and correctly valued which require support-infrastructure such as tax maps, cadastral surveys, and competent personnel. Basic computer systems are needed in data encoding, records managements, issuance of tax bills, recording payments, and tracking changes in land ownership. Processes in quality control have to be in place to prevent manual manipulations in property values. Weak controls in some LGUs, e.g. Pasay City, allow unintended interventions in data encoding that result to under assessment.¹⁸ On the average, LGUs spent P0.23 to collect a peso of the property tax. The dispersions from the average are large. For cities, the average costs range from P0.04 to P0.83; for provinces, from P0.36 to P4.00. For extreme cases, the costs of administration are four times more than the revenue that the property brings.¹⁹ Dillinger notes that the effective rate of the tax is so low that may not be worth the collection costs.²⁰

The most difficult phase in tax administration is collecting the tax itself. Political will has to be added to efficiencies in valuation. It takes firm leadership to tell delinquent tax payers that their properties will be sold at public auction. More firmness is required to make this warning real. Only a few LGUs have shown real toughness in tax enforcement, e.g. Quezon City, Taguig, and Pasig. In many LGUs,

¹³ Jay K. Rosengard, *Property Tax Reform in developing Countries*. Boston: Kluwer Academic Publishers, 1998.

¹⁴ Dillinger, op.cit

¹⁵ Jay K. Rosengard, *Property Tax Reform in developing Countries*. Boston: Kluwer Academic Publishers, 1998.

¹⁶ Dillinger, op. cit

¹⁷ Guevara, Gracia, and Espano, op.cit

¹⁸ Commission on Audit, op.cit.

¹⁹ Guevara, Gracia, Espano, op. cit.

²⁰ Dillinger, op. cit.

laxity is still a prevalent practice.²¹ The 2011 audit report of the Commission on Audit (COA) continuously notes the failure of many of many LGUs to intensify collection effort by enforcing the provisions of law to collect delinquencies.²² COA adds the failure of LGUs to update revenue codes, as a contributory factor to the low collection efficiency of the real property tax.

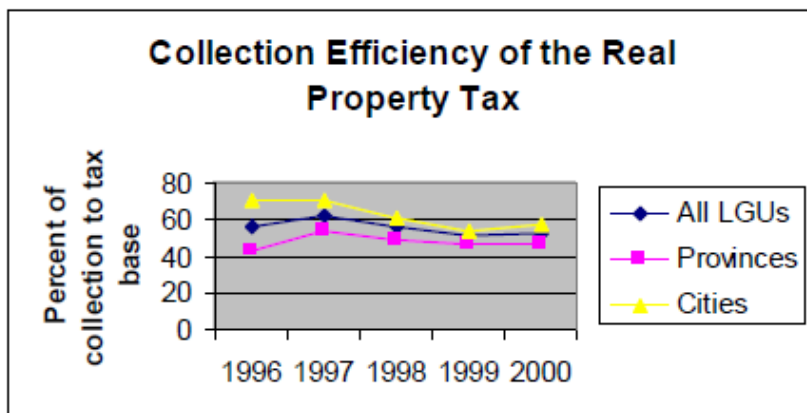


Chart1- Collection to the Real Property Tax Base

The property tax is a true under-performer. On the average, LGUs collect only 54% of the tax base. This is a result of inefficient policies, inadequate investments in tax administration, low valuation of properties, and poor governance.

3.3.9 The Fairness of Property Tax

The motivation behind the imposition of the differentiated assessment levels and tax rates could be the attempt to make the property tax a fair tax. Assuming that owners of commercial lands have a greater ability to pay, their property tax is based on 40% of the value of the land. A lighter burden is imposed on residential land owners because of a lower assessment level, i.e. 30% of market value. But the effects on a progressive distribution of the tax burden are not straight forward. The tax burden progressively rises as income increases for the first three income deciles, i.e. low income class, tapers down ward for the next two deciles, rises again for the

²¹ The COA notes that more revenues should have been collected by LGUs such as Pateros, Rizal, Calamba City, and Bais City if they used the legal remedies provided under the law to collect delinquencies.

²² Commission on Audit, "2010 Financial Report on LGUs"

middle income class and then falls for the higher income deciles. The distribution of the tax burden is has an irregular” pattern.²³

Aberrations in the distribution of tax burden are likely due to the practice of discretion in valuation and in the collection of delinquent accounts. The study is out dated, but the findings are relevant considering that no significant changes have been noted in the distribution of income in the Philippines. “From 1961 to 2009, the upper 50% of families had 80% of income and lower half had 20%.”²⁴

3.3.10 Promoting Efficiency in Land Use

The idle land tax is a policy tool to curb land speculation. If a land is withheld from development, the law mandates the imposition of a 5% tax on: 1) agricultural lands with an area of more than one hectare and one - half of the land remains; 2) non-agricultural lands with an area of 1,000m² which remain unimproved; and 3) unimproved residential lots in subdivisions. The idle land tax brought in P25, 482,000 or 0.07% of total property tax collection in 2010. This is equal to the costs of a five single- room condominium unit in Makati City.

The miniscule amount represents either structural defect in the law or feeble attempts to use it. The area requirement for a land to be considered idle is too large and a marked departure from the original proposal of 300m² which his the average size of residential urban lands.²⁵

The special levy on lands benefited by public work projects of the national or local government is intended to recoup unearned increments enjoyed by taxpayers. LGUs have selectively used it and added only P16.11 million to local finance in 2010, or 0.047% of total property tax collections.

3.3.11 Optimizing the Potential of the Property Tax

The elbow room to use property taxation to raise more resources for local governments is relatively wide. The current tax burden is light, collectibles are large, and administration and compliance can be greatly enhanced.

Policy changes need to be made. Valuation has to be isolated from politics by

²³ Joint Legislative – Executive Tax Commission, **A Study of the Tax Burden by Income Class**, Manila, Philippines, 1964.

²⁴ Tomas Africa, “ Family Income Distribution in the Philippines, 1985-2009, Essentially the Same, March18, 2011.

²⁵ National Tax Research Center, “Idle Land taxation in the Philippines”, 1977

dropping the requirement for the schedule of market values to be approved by local legislative councils. There are adequate provisions in the law for redress against unfair valuation practices. Tax payers can lodge their protests before the Board of Assessment Appeals.

There is enough reason to use the full market values as the tax base instead of fractions of the value or assessment levels that are differentiated according to land use. Differentiated assessment levels do not enhance the progressivity of the tax. They only introduce distortions in land use and arbitrariness in tax administration.

The special levies on properties are not functional and a more realistic definition can be crafted. But since amendments to the Local Government Code have been languishing in Congress for the last 22 years, LGUs on their own can implement significant changes in administering the tax. Their paradigms have to be transformed however.

Changes are not just brought in by improvements in technology. The most important factor in tax reform is enforcement. The “Property Tax Administration Project in the Philippines” bears to this conclusion. The project produced tax maps and up dated property assessments but yielded in significant revenues because poor collection practices were never addressed.²⁶ Efforts were concentrated on the upstream stage of property tax administration, i.e., discovery and valuation of properties to the neglect of collection, i.e. sorting records to identify delinquents and enforcement of penalties.²⁷

Improvements in property identification and valuation are important, but enforcement is equally important. These two components of are form should progress in lockstep.

Many LGUs in the Philippines have shown the way:

- **Naga City** is a model on participatory governance and transparency. The budget for education which the Special Education Fund finances is demand-driven and crafted with intensive consultation from citizens. The website of the city provides the budget, contracts, infrastructure, and

²⁶ Bahl and Martinez-Vasquez, op. cit.

²⁷ Dillinger, op. cit.

costs for delivering social services. Every citizen is provided with a copy of the “Citizens’ Charter” which informs them of the services they are entitled to, from whom the services can be obtained, and the steps to obtain them.

- **Muntinlupa City, San Fernando City, Valenzuela City, and Quezon City**, among the many others used basic property tax tools such as tax maps and cadastral surveys to develop comprehensive tax rolls. But they did not stop there and used these tools to collect tax payments. They regularly send tax bills, streamlined the processes of tax payments, and enforced collection of delinquent accounts through sale of properties or/and through public auction. They treat tax payers as customers through the provision of comfortable tax payment offices, one stop shops, courteous employees, and simple perks like coffee.
- **Nueva Vizcaya** enlists the help of teachers in tax education and deputizes village officials to conduct house-to-house campaigns and collections.

The Department of Interior and Local Governments (DILG) under the leadership of the Secretary Jesse Robredo has paved the way for mainstreaming these innovative practices so that they do not remain as silos but as a way of life. Secretary Robredo instituted a performance incentive system (PIS) that will include efficiency in the collection of local taxes, such as the property tax as basis for giving of transfers and grants to LGUs. LGUs have responded enthusiastically to progressive PIS. Almost 77% of the LGUs have reached the entry level to the Seal of Good House keeping. The PIS is an august way to influence LGUs to use their revenue-raising powers to respond to the needs of their constituents.

The momentum of change has to be seized to put property taxation in its correct trajectory.

3.4 INDIA : Property Tax Sistem in India, Problems and Prospects of Reform

(M. Govinda Rao)

Abstract

An important rule of sound fiscal decentralization is that assignment of functions should be according to comparative advantage and the local governments should have access to adequate revenue sources to finance the public services they are mandated to provide. It is also important that to avoid transfer dependency and ensure hard budget constraint, there should be a strong 'Wicksellian linkage' – the linkage between revenue and expenditure decisions. The principle implies that the local services should be paid for by the beneficiaries who are the local residents, and the services with inter-jurisdictional externalities should be financed through specific purpose grants with matching rations equalling the extent of spill-overs (Bahl, Martinez-Vazquez and Youngman, 2008). Of course, in practice, it is difficult to estimate the spill-overs accurately and design the transfers.

Of the various revenue handles, tax on real properties is found to be the most suitable candidate for assignment to local governments. These are relatively immobile, and are based broadly on benefit principle (Bahl and Martinez-Vasquez, 2008). As most of the public services provided by local governments are of quasi-public nature, it is possible to link benefits with property values and therefore, property taxes evoke better compliance as well. In developed countries, local public services, *ceteris paribus*, are capitalized into property values and the tax based on the values of these properties broadly follows the benefit principle. Furthermore, as the market for real properties is organised, the valuation is easy and the levy becomes simple and transparent. Not surprisingly, in most of the developed countries, overwhelming proportion of public services is financed by property taxes and user charges.

In developing countries, however, property tax has not been a significant revenue source for local governments. The contribution of property taxes in developing countries is estimated at about 0.6% of GDP. In India, the revenue from the tax is abysmal and the estimates vary from 0.16 - 0.24% of GDP (India, 2011). There is a significant gap between the revenue potential from the tax and the actual revenues collected. What is more, the tax is inelastic. Even as there has been a significant

growth in the real properties in urban areas, the revenues have been stagnant. The recent studies have shown that the major causes of low revenue productivity and low income elasticity of the tax is due to poor coverage of properties for assessment, obsolete methods of valuation, profligate of exemptions and poor enforcement.

India has different property tax systems in different states. Some have property taxes based on capital values, others have rental values and more recently, many of the municipal corporations have been moving over to an area based presumptive tax. Capital value based property tax has suffered from valuation problems as the market for real properties is largely unorganised with registered values of properties being only a fraction of the actually transacted values. The existence of rent control acts in many states undervalues the assessment based on rental values (Bagchi, 1997). Presumptive area based tax on properties need to be revised from time to time to adjust for changing values due to increase in prices and other factors.

The recent reforms in property taxation have been to replace the capital value or rental value based taxes with area based taxation with graded valuations depending upon the location of the property and type of construction. Bangalore Municipal Corporation has been able to reap significant revenue gains from reforming the property tax system with revenue increasing by almost three and a half times in eight years from a mere Rs. 2.3 billion in FY 2004-05 to Rs. 8.4 billion in FY 2011-12. This offers interesting lessons for others.

In an economy where the market real properties remain unorganized, in the medium term the strategy for reforming property taxes will have to be towards a presumptive taxation based on area of property on the lines implemented by Bangalore Municipal Corporation (Rao and Bird, 2011). However, revising the values from time to time could face political problems. One method should be to automatically index the values every year based on the realty price index to be estimated by an independent agency. At present, the National Housing Bank estimates such an index for major cities in the country. This, combined with the use of GIS mapping could increase the revenue productivity of property taxes and its buoyancy. Methods also should be found to include the values of alterations and additions to properties in the base of the property tax.

3.4.1 Introduction

The design and implementation issue relating to property tax among of the relatively less researched areas. This is particularly so in developing countries where the property market is largely unorganized and therefore, valuations are extremely difficult, information available to the tax authorities is restricted, extent of decentralization is limited, the local elite or “distributional coalitions”²⁸ are powerful and there are serious capacity limitations for the levy designing and implementing the property tax. In fact, in most of the developing countries, the vicious cycle of low service quality, low tax compliance leading to further low level of local public services continues to persist. While it is acknowledged that the metropolitan areas are the places which generate economic dynamism, breaking this vicious cycle is at the heart of creating this in developing countries. As property tax is the most suitable source of revenue of local governments, its reform is critical to breaking this vicious cycle.

As stated in Rao and Bird (2011), cities are the leading edges of economic dynamism in every country. They generate agglomeration and network economies for enterprises and individuals, generating externalities that facilitate transactions, production, and distribution activities. However, the degree of success in this task depends on their ability to ensure sustained provision of a wide range of urban public services that promote both private sector activities and the well-being of the urban population such as water, sewers, garbage collection and disposal, drainage systems, police and fire protection, and transportation. Underlying all this, a ‘good’ city needs a political and governance system that can respond to the changing requirements and needs of its people swiftly, flexibly, and efficiently.

India is a country in which over 377 million people live in 7935 urban areas, which has 53 cities with over a million people including the three of the largest metropolises in the world (Mumbai, Delhi and Kolkata). Although India’s urban population growth has been decelerating over the past 3 decades, this deceleration

* The author is grateful to Mr. U. A Vasanth Rao and Mr. Mayank Sharma for providing useful information on the property tax systems in Bangalore and Delhi respectively. The usual disclaimers, however, apply.

²⁸ The term “distributional coalitions” owes its origin to Mancur Olson who used it to describe the special interest groups who strive to redistribute the resources/incomes in their favour rather than contributing to the generation of new resources/incomes. See, Olson (1982).

is not expected to continue in the years ahead as India enters into a phase of rapid growth and major structural transformation in favor of labor-intensive industry and services sectors in the years ahead. The urban sector contributes about two-thirds of GDP in 2009-10 and this share is likely to increase to 75% by 2031 (HPEC, 2011).

In terms of both governance, finance and service delivery, Indian cities have considerable catching up to do as detailed in the Report of the High Powered Expert Committee (HPEC) on Urban Infrastructure and Services (HPEC, 2011). Only 70.6% of urban population has access to individual water taps, about 81% of urban households have access to any form of latrine facility, 71% of urban households have a drinking water facility within their premises, and only 62% of waste is treated before disposal. Urban transportation problems are similarly acute; public transportation is congested and inefficient. Housing too is problematic, with almost 25% of the urban population of India living in slums. The HPEC (2011) estimates the cumulative capital investment requirements for urban infrastructure at 2009-10 prices for the period 2012-31 at over Rs.39,000 billion (excluding investment in primary education, health, and electricity distribution. This figure also does not include the cost of acquiring land for new infrastructure). An additional Rs 20,000 billion is estimated as the requirement for the operation and maintenance of the old and new assets.

The exponentially growing urban infrastructure and service requirement would require augmenting resources from a variety of sources. The HPEC has analyzed the issue of financing urban infrastructure and finances in detail, estimated the volume of investments needed to enable the urban local governments to provide a certain acceptable standards of services and infrastructure and pointed out a number of areas where reforms have to be undertaken to impart dynamism to the cities to make them the engines of growth. This includes mobilizing revenues through higher user charges on urban services, providing urban local governments with additional revenue handles including piggy-backing on the goods and services tax, higher transfers linked to market based reforms, levy of developmental charges to finance improvements in urban infrastructure.

Given that property tax is the most suitable tax handle with the local governments, enhancing its revenue productivity is one of the most important items in the reform agenda. This is also an important conditionality in the ongoing mission on which

provides substantial assistance to the cities for improving their infrastructure and services namely, the Jawaharlal Nehru Urban Renewal Mission (JNURM).

As stated by the HPEC (2011; p. XXVII), “Urban local governments in India are among the weakest in the world both in terms of capacity to raise resources..... the tax bases of ULBs are narrow and inflexible and lack buoyancy....”Unfortunately, reliable information on the collection of revenue from property tax in the country is not available. The available anecdotal information shows that as compared to the developing country average of about 0.7% of GDP, the revenue realized through property taxation is estimated at about 0.2% of GDP. Considering the poor revenue collection from the tax, the HPEC (2011; p. 133) recommended that a “...time bound comprehensive reform of property tax should be undertaken by all states”.

This paper analyses the property tax system in India, examines the reasons for its low revenue productivity, reviews the recent reform initiatives and identifies further reform areas.

Section 2 analyzes theoretical rationale for levying property taxes at the local level and its role and revenue importance in developed and developing countries.

Section 3 reviews the evolution of the systems of property tax in India, identifies their shortcomings and analyses its revenue importance in different states.

Section 4 reviews some of the recent initiatives and identifies reform areas.

The concluding remarks are presented in the last section.

3.4.2 Property Tax at Local Level: Theoretical Issues

In the Musgrave-Oates tradition, in a multilevel fiscal system, assignment of functions and sources of finances according to comparative advantage implies that macroeconomic stabilization and redistribution should be predominantly a central responsibility and local governments would have principal role in the allocation function (Oates, 1972). This implies that all broad based and progressive tax bases go the Central government and local governments will have to carry out large and growing expenditure responsibilities. This could result in excessive dependence on federal transfers resulting in softening of the budget constraints and severing of the relationship between revenue-expenditure decisions or local governments carrying on unfunded mandates resulting in poor service delivery. Either of these outcomes would imply adverse implications for efficiency and accountability.

Empowering local governments would imply avoidance of heavy transfer dependency, imposing a hard budget constraint and ensuring adequate resource handles for the provision of public services the local governments are mandated to provide. Therefore, an important implementation rule of fiscal decentralization is that there should be a strong 'Wicksellian linkage' – the linkage between revenue and expenditure decisions (Breton, 1996). This linkage ensures transparency and the taxpayers force the governments to provide public services commensurate with the tax payments.

Thus, according to the principles of fiscal federalism, local services, by and large, should be paid for by the beneficiaries who are the local residents. User charges are appropriate for financing locally provided services of a 'private good' nature. Local public goods should be financed paid for by the residents and the cost of financing services whose benefits spill over jurisdictions should be shared through specific purpose transfers.

A local tax designed to satisfy these requirements should in principle have the following characteristics (Bird 2006):

- (i) The base should be relatively immobile to allow the local authorities to vary the rates without losing the base.
- (ii) The tax should yield adequate revenues to meet local needs and should be sufficiently buoyant over time.
- (iii) The tax should be stable and predictable over time.
- (iv) It should not be possible to export the tax burden to non-residents except to the extent that such burdens capture benefits non-residents obtain from local services.
- (v) The tax base should be visible to ensure accountability.
- (vi) The taxpayers should perceive the tax to be reasonably fair.
- (vii) The tax should be relatively easy to administer.

Based on the above considerations, Bird and Slack (2007) review the various possible candidates for local taxes and consider that the most appropriate tax at the local level is the tax on real properties. There are a number of advantages of

assigning the property tax to local governments²⁹. These are relatively immobile and therefore less distorting, visible and relatively simple and easy to administer at the local level. In fact, at the local level it is easy to identify the tax base and compile the information on it and therefore, local governments have comparative advantage in levying the tax. The tax base is large and if properly designed, these can be elastic and productive. The tax assumes the role of a quasi-benefit charge and therefore, is more acceptable and thus evokes greater degree of compliance. The property tax takes the character of a benefit tax as owners of property benefit from public services provided by the local governments. It is also argued in the literature that fiscal differentials at the local levels get capitalized into property values (Oates, 1969). This characteristic of the tax also makes it a progressive tax.

Despite these advantages, levying property tax in developing countries has not been easy as determination of the tax base as well as enforcement of the levy is best with a number of difficulties. The advantages of revenue productivity as well as equity can be realized only when the size of the tax base is captured accurately. There are severe problems associated with determining the values of immovable properties, particularly in developing countries. Visibility of the tax and often, lack of association between the tax paid and benefits from local public service received makes the tax unpopular. The cost of valuation may be high resulting in high cost of collection and as the markets for immovable properties is often nascent, officials may have the discretion to determine the tax base and this could result in rent seeking and high compliance cost. Given that public goods always induce 'free-riding' behaviour, it is often difficult to enforce the tax on local elites who are the owners of large immovable properties.

While much of the arguments about the suitability of property as a neutral (immobile) tax base and a real local tax may be applicable to the tax on residential properties, tax on non-residential properties can be distorting (Slack, 2011). From economic efficiency point of view, it is argued that less responsive (to taxes) tax bases should be taxed at higher rate. The businesses are more responsive (mobile) than the residents and therefore, should be taxed at lower rates. However, most municipal governments find it easier to levy heavier taxes on non-residential properties as this is an easy way to shift the tax burden to non-residents. The levy of

²⁹ For a detailed analysis of the qualities of property taxation, see Bahl, Martinez-Vazquez and Youngman (2008).

the tax on commercial and industrial immovable properties may be shifted forward to the consumers of the products or backward to labour and this could cause both distortions and inequity.

In addition to being a tax on the beneficiaries of the local public services, it is argued that the property tax has a progressive distribution of the burden. Given that there is a high correlation between property ownership and income levels, if properly designed, the distribution of the tax burden could be progressive. Thus, it is argued that tax on immovable properties satisfies both the 'benefit' and 'ability to pay' principles of taxation. The general equilibrium incidence view on property taxation is that capital is mobile, but is fixed in supply and therefore, the incidence falls on the owners of capital (Mieszkowski and Zodrow, 1989). However, in the long term, capital immobility is not extreme and it is possible to shift a part of the burden.

Furthermore, when the tax is levied on non-residential (commercial and industrial) properties, the tax may be shifted forward to the consumers of products or shifted backward to labour depending upon price elasticity of demand for the products and factor intensity and substitution. In this situation, it is not possible to conclude that property tax is definitely progressive³⁰. It is also possible that the local governments may use the non-residential property taxes more heavily to export a part of their tax burden to non-residents and the incidence of this component is difficult to ascertain.

Despite the difficulties and sometimes, the unpopularity of the levy, the world over, taxes on immovable properties have been the mainstay in financing municipal services. The study by Bahl and Martinez-Vazquez (2008) shows that (i) property tax is a significant source of revenue for local governments both in developed, developing countries as well as transitional countries (Table 1). (ii) In terms of percentage to GDP, the contribution of property tax in OECD countries was over 2%, whereas, it was about 0.6 to 0.7% in developing and transitional countries. (iii) In the case of developing countries, the contribution of property tax remained has not

³⁰ Sennoga, Sjoquist and Wallace (2008), using a computable general equilibrium model with a large informal sector and less than perfect mobility of capital – the structural features to represent developing and transitional countries show that the burden of property taxes is primarily borne by owners of land and capital and thereby the distribution of tax burden is progressive.

shown any appreciable increase both as a ratio of GDP and as percentage of total expenditures of local governments. However, in OECD countries, the property tax revenue as a percentage of GDP, after remaining stable for two decades, showed a significant increase after 1990s. Similarly, the transitional countries were able to virtually double the contribution from property tax in 2000 from the level prevailing in 1970.

Empirical studies show that the volume of property tax collection depends on the level of development of the country and the extent of its fiscal decentralization (Bahl and Martinez-Vazquez, 2008). The level of development determines, *inter alia*, the extent of organized market development for immovable properties, improved capacity of tax administration and better information on values of properties. The degree of fiscal decentralization determines the intensity in the use of property tax handle. However, it is also seen that fiscal decentralization is positively correlated with the level of development. Furthermore, there can be a two-way relationship between property tax collections and fiscal decentralization.

Table 1: Per Cent of Property Tax Revenue in GDP				
	1970s	1980s	1990s	2000s
OECD	1.24(9.7)	1.31(9.9)	1.44(13.65)	2.12(12.40)
Developing	0.42(18.7)	0.36(15.97)	0.42(13.49)	0.60(18.37)
Transitional	0.34(3.67)	0.59(4.92)	0.54(7.75)	0.68(9.43)
ALL	0.77(14.49)	0.73(12.89)	0.75(11.63)	1.04(3.40)

(Figures in the parenthesis show percentage of property tax in total revenues of municipal bodies) Source: Bahl and Martinez-Vazquez, 2008

Despite visibility, localized nature, correspondence of the tax with the beneficiaries of public services and progressivity, the tax on immovable properties has not been successful in many developing and transitional countries as seen by the revenue performance³¹. There are a number of reasons for the poor revenue productivity of the tax in these countries and these include:

³¹ In fact, even in OECD countries, the property tax is considered to be the “most hated tax” (Brunori, 2003. P. 7)

- (i) ambiguity in ownership and poor information and records about the properties;
- (ii) predominance of the informal sector in the market for immovable properties and poor information system;
- (iii) low capacity, lack of interest in reforms and high cost of tax administration in developing and transitional countries to design and enforce the tax;
- (iv) visibility of the tax and its unpopularity with the voters as the benefits received are generally not commensurate with the tax paid, and other forms of properties do not attract a similar tax;
- (v) predominance of vested interests and large scale exemptions and concessions;
- (vi) arbitrary, uncertain and mysterious ways of determining the tax base;
- (vii) static nature of the tax base and political difficulties in undertaking periodic valuations;
- (viii) wide discretion to the tax officers and high compliance cost associated with the tax;
- (ix) adding the values of additions and improvements to properties to make the tax base responsive to changes in the values of property in the tax base. Not surprisingly, the actual revenue realization has not been commensurate with the potential.

3.4.3 Property Tax Systems in India

In Indian federation, the Seventh Schedule of the Constitution assigns the legislative powers of the Union and State governments. Entry 4 in the state list empowers the state governments in all matters relating to local governments, including “...the constitution of powers of municipal corporations, improvement trusts, district boards, mining settlement authorities, and other local authorities for the purpose of local self-government or village administration”. Under Article 243-W, the legislature of a State, at its discretion, is authorised to devolve powers to the municipal governments on functions listed in Schedule 12 of the Constitution. Similarly Article 243-X authorises the State governments to devolve the power to

levy taxes, duties, fees, tolls according to the limits set and procedure laid down by the legislature of the State government.

The above assignment system has entailed three important features. **First**, while there is a separate schedule indicated for the devolution of functions of municipal governments, though the specific function to be devolved and the extent of devolution lies with the state government, there is no separate list of taxes indicated in the Constitution for assignment to the municipal governments. As there is no separate list for local governments, the State governments are required to assign the tax powers to local governments from the State List in the Seventh Schedule. **Second**, the assignment of functions and sources of finance to municipal bodies is to be done at the complete discretion of State governments. **Finally**, the local governments are given the power to levy taxes, duties, fees and tolls in accordance with the procedures and limits specified the State governments.

Entry 49 empowers the State governments to levy 'taxes on land and buildings' which has been devolved to the local governments. However, in the statues governing the municipal governments, the State governments lay down the procedures for valuation, exemptions and concessions, the floor and ceiling rates of tax and administrative and enforcement mechanisms on matters such as delays, arrears, and evasion.

Thus, although taxes on immovable properties are considered to be a local levy, local governments have very limited autonomy in determining the base, fixing the rates and enforcing the tax. In fact, the State government of Rajasthan abolished the house tax in 2006 and Haryana abolished the tax on self-occupied residential properties in 2008, but re-imposed it after the grants for urban development by the Central government was linked to property tax reform. The state of Punjab although agreed to withdraw the exemptions by December 2008, to fulfil the conditionality under a central grant programme, did not do so (HPEC, 2011). These states did not care even to inform about their decision to abolish the tax, leave alone providing alternative revenue sources to them. The lack of revenue autonomy and arbitrary actions of abolishing the local taxes by the State governments without providing alternative revenue source leaves the local governments with unfunded mandates with adverse impact on service delivery.

According to 2011 census, In India, 377 million people constituting 31.2% of population were spread over 475 urban agglomerations, 981 outgrowths and 7935 towns of various population sizes. As many as 53 cities and towns have a population of million plus. Three of the largest metropolises in the world (Mumbai, Delhi and Kolkata) are in India. Urban areas generate about 65% of the GDP in the country³². During the last decade, urban population has shown an average annual growth of 2.4% and this is expected to accelerate in the coming years with significant migration of rural population to urban areas.

Unfortunately reliable data on revenue collections from property tax by various municipal bodies is not available in India. Both the 13th Finance Commission and the HPEC, in their reports, have used the estimates made by Mathuret et al (2008) which has questions of reliability. In their study, data on property tax collections were collected for 36 large municipal corporations for the year 2006 and this is blown up to estimate the revenue collection for the country by making three alternative assumptions. The three assumptions were:

- (i) the collections in the remaining 5125 small municipalities would be equivalent to the average collections of four municipalities with the smallest populations in the large city sample;
- (ii) the collection in these municipalities would be equivalent to those showing the poorest collection among the 36 largest cities;
- (iii) Poorest per capita collection among 36 large cities in the sample in each of the states would apply to all the municipalities in the State. The most optimistic estimate made on the basis of the above assumptions shows that in FY 2006-07, on an average, per capita property tax collections was Rs. 486 (about USD.10.6) and total collections ranged from 0.16 per cent to 0.24 per cent of GDP.

The lack of reliable information on the base and revenue collections from property tax is a major shortcoming in designing and implementing property taxes by municipal governments in India. The State Finance Commissions which are supposed to recommend transfers from the State to local governments do not

³² According to the Mid-Term Appraisal of the Eleventh Five Year Plan the urban share of GDP was 62-63 per cent. See, India (2010).

seem to have bothered to compile the figures, nor has the State government taken in putting together these estimates. As shown above, in the absence of any other alternative, even the official committees have simply taken the estimates made in Mathuret.al uncritically³³. Each of the state governments has a full-fledged urban development department, but they do not compile fiscal information on the urban local bodies.

While reliable estimates of the revenue from the tax are not available and it is important to build these estimates for calibrating policy relating to property taxation, the available information on 36 largest municipal bodies shows that property tax contributes very small amounts to the finances of municipal bodies in India. The more recent information collected for a sample of 32 municipalities for the period 2004-2008 with population ranging from 0.057 million (Baramati) to 98 million (Mumbai) shows that per capita collections in 2008 was Rs. 457 and in 2006, it was Rs. 269. This includes collections from current demand as well as arrears, which implies that, on average, per capita property tax collection in Indian urban areas in 2006 was less than Rs. 1 per day.

There are a number of shortcomings in the prevailing property tax system.

First important issue is the low revenue productivity. As mentioned earlier, the per capita tax collection in 36 large municipal corporations in 2006 was just about Rs. 486 and the annual growth rate observed during the three year period (2003-2006) was 7.9% which is marginally higher than the inflation rate which implies that revenues in real terms were virtually stagnant. With the nominal GDP increasing at over 14% during this period, the revenue from the tax as a ratio of GDP has actually shown a decline.

Second, it is difficult to state that the prevailing property tax system promotes either vertical or horizontal equity. The violation of equity considerations arise from the poor coverage of the tax, wide ranging exemptions, low collection efficiency and the failure to revise the tax base from time to time to take into account the changes in the status of the properties and improvements to the properties.

³³ The information compiled for 23 municipalities with less than one million population in different states for a more recent study shows that the average per capita tax collections for the year was Rs. 66.5 which is higher than the average of 4 lowest collecting municipal bodies (Rs. 40) which is one of the three options adopted in Mathur's estimates. If the average of 73 is taken, the tax – GDP ratio works out to

Third, the claim that property tax is a local tax and is neutral is considerably diluted by the fact that a significant portion of the tax falls on non-residential properties. In Bangalore Municipal Corporation, for example, revenue collection from non-residential properties during 2008-11, constituted about 38-40% and residential cum non-residential properties contributed to another 7-9%. The situation is similar with other municipal corporations. This implies that the property tax is far from being neutral in Indian context and a considerable proportion of the tax is exported to non-residents.

Table 2: Property Tax Revenue from Residential and Non-Residential Properties					
	Non-Residential	Residential	Vacant Land	Residential cum Non-Residential	Total
2008-09	2844.6(38.02)	3845.6(51.41)	243.7(3.26)	547.0 (7.31)	7480.9 (100.0)
2009-10	3259.5(40.9)	3592.7(45.08)	375.2(4.71)	742.6(9.32)	7970.0(100.0)
2010-11	4028.7(36.36)	5341.0(48.2)	815.6(7.36)	894.7(8.07)	11080.0 (100.0)
2011-12	4400.6(36.37)	5721.6(47.29)	979.0(8.09)	998.8 (8.25)	12100.0(100.0)

Note: Figures in parenthesis denote percent of total

Source: Brihat Bangalore Mahanagara Palike

There are a number of reasons for the low revenue collections from the property tax and its slow growth. The most important reason for the low collections is the poor coverage of the tax and its low collection efficiency. Poor coverage is due to:

- (i) wide ranging exemptions;
- (ii) poor information system and lack of up-to-date registry of land and properties by municipal bodies;
- (iii) the existence of vacant properties

Exemptions vary from state to state and from one municipal body to another, but there are some common exemptions. Article 285 of the Constitution provides

exemption to all properties belonging to the Union government³⁴. The adverse revenue impact of this is particularly severe in capital city like Delhi. One major reason why the Municipal Corporation of Delhi could not increase its revenue yield even after the reforms is the exemption to central government properties including the sprawling residences of important bureaucrats and politicians. While the demand and ensure high standards of municipal services, there is no commensurate payments by way of property tax and the service charges cover only a small fraction of the cost. The big metropolitan cities also have large unauthorized buildings and properties not included in the municipal register which while availing the municipal services do not pay the tax.

Other important exemptions include places of religious worship, educational institutions, charitable institutions, ancient and historical monuments, burial and cremation grounds, government land and buildings set apart for free recreational purposes, offices of trade union associations, buildings and lands of urban development authority constituted under the respective state government acts, institutions providing free medical relief and education and certain types of vacant lands and buildings³⁵. In addition, there may be exemptions and concessions for the properties owned by ex-servicemen and their families. The volume of exemption, thus vary from one local government to another. In Delhi for example, the exemption will be large due to the overwhelming proportion of Union government properties, unauthorized buildings and addition to buildings which may not be the case in other places.

A major problem with the property tax administration in municipal bodies is the poor information on property tax base with them. The important pre-requisites for efficient property tax system are that there should be clarity in property ownership or tenancy rights and a cadaster that uniquely identifies properties and their owners. In addition, there should be appropriate mechanisms for periodic market based valuation of properties and systems and processes for tax collection and enforcement (Smoke, 2008). Ambiguity in ownership and tenancy rights and inability to adopt market based valuation are severe constraints in increasing the

³⁴ The municipal bodies can, however, levy service charges.

³⁵ In Delhi, for example, exemptions are govern to vacant lands and buildings exclusively used for agricultural purposes, small properties (less than 100 sq.mtrs), owned by original owners

revenue productivity of the tax. More importantly, most municipal bodies have not made attempts to update the registers relating to property ownership and tenancies not do they coordinate with the registration department for getting information on the properties transferred and their values.

In addition to lack of clarity on ownership and tenancy rights, in Indian context, for a long time the rent control laws have been a major constraint in realizing the potential of the tax. Although there were inconsistent judgments, Supreme Court in the case of *Municipal Corporation of Indore versus Rathna Prabha* in 1976 clearly observed the need to move away from the rental valuation principle as per the rent control acts. However, there are always problems in adopting valuation according to market rents whenever the rental valuation is adopted as the base of the tax.

Market based valuation and its periodic updating has been a problem not just in developing and transitional countries but also in OECD countries. Very few municipal governments in the world update the property values for taxation purposes every year (Slack, 2011). The simple fact is that who ever is the base taken – the annual letting value, capital value or an area based value, the value finally taken as the base is presumptive. Given that a ‘representative’ value has to be taken for each locality, the value chosen will be the minimum rather than average. In other words, any presumptive value of the tax base will be accepted only when this is substantially lower than the actual value of the properties. Furthermore, increases in the market values for the property owners is only an accrual and will not be realized unless they sell their properties and therefore, it will be difficult to include higher value of the property that has accrued and not realized in the tax base. Not surprisingly, even as the immovable property values in urban areas have been increasing at a rate much faster than general inflation rate and even as there has been significant increase in the number of houses in urban areas, the revenue productivity of property tax has continued to be low.

Many municipalities have simply not updated their property tax registers and many properties are simply not included in the tax base. The Administrative Reforms Commission has noted that only about 60-70% of the properties in urban areas are actually assessed. Besides exempted properties and vacant lands, significant numbers of properties are not simply included in the registers of the local governments. A large number of property owners seem to be simply not paying the tax although they benefit from the local public services. The Commission

recommended the matching of the properties paying the tax with those in the Geographical Information System (GIS) to identify those that are not paying the tax. Considering that the number of missing properties in the tax register is high, the Commission has recommended the use of GIS maps to verify the coverage and the recent reform initiatives under the Jawaharlal Nehru National Urban Renewal Mission (JNURM) have helped to improve the coverage by matching the taxpaying properties with properties in the GIS maps.

The problem of low coverage of properties is compounded by poor collection efficiency. Low level of efficiency in revenue collection arises from the actual values of properties assessed are significantly lower than the market values and increases in properties on account of both improvements to existing properties and increase in prices of the properties is not adequately captured in the tax base. Mathur et.al. (2009) suggest that assessed values are as low as 8-10% of the market values and on an average about 30% of the market values in 36 largest municipal corporations. Any attempt to increase the value from such a low base to resemble market values will meet with severe opposition.

Equally important cause of poor collection efficiency is the considerable gap between the tax demand raised and actual collections. The average collection rate for 36 largest municipal corporations was 37%. Poor collection efficiency represents inadequate efforts at collecting the tax or alternatively lack of acceptability of the tax and the amount disputed.

3.4.4 Reform Initiatives on Property Tax in India

The discussion in the previous section shows that municipal governments in India have failed to mobilize significant revenues from property tax to finance local public services with adverse effects on public service delivery. The HPEC has estimated the investment requirement for urban infrastructure and services for the next 20 years at Rs. 39000 billion at FY 2009-10 prices which is equivalent to USD. 780 and some proportion of this will have to be generated by reforming the property tax. If the cities have to function as leading edge of economic dynamism as has been the case in many countries, they will have to substantially augment local infrastructure and services for which, the municipal governments will have to undertake reforms in their property tax systems.

Although the general situation in regard to property tax, as analyzed in the previous section is far from being satisfactory, there have been interesting initiatives at reforms in recent years and it is important to review some of these initiatives. In this section, important reform initiatives are discussed. These, in the main include, more scientific/objective methods of determining the tax base, introduction of self-reporting/self-assessment system, ensuring ease of tax payment including on-line payment of the tax to significantly reduce the compliance cost. Successes of these reforms have not been even. Among the larger municipal corporations, Bangalore Municipal Corporation has been successful in substantially increasing the revenues from the tax in recent years and these experiences offer hope for others to adopt these reforms.

There has been a significant increase in both the number of properties assessed leading to increase in the demand and percentage of actual collection from demand or increase in collection efficiency. However, reform in Municipal Corporation of Delhi has not been very successful in increasing revenues. In fact, there was a decline in the revenues after the introduction of reforms. Understanding the lessons from these reforms is necessary to avoid the shortcomings in the future.

Historically, property tax was levied on the rental values of properties. The method of valuation goes back to the Valuation (Metropolis) Act of 1869 in which, the 'annual vale' or 'ratable value' is determined on the basis of actual or presumptive rent or capital value³⁶. In Independent India, as mentioned earlier, Entry 49 in the State List specifies the 'taxes on lands and buildings" and the municipal governments are authorized to levy the tax as laid down in the respective State Acts. These Acts list out the exemptions, indicate the floor and ceiling rates and lay down the procedure for administration and enforcement. Not surprisingly, there are wide variations in the determination of the base, structure of rates as well as administration of the tax. Although the base was supposed to be rental value, the way it was determined hardly reflected the rental value and there were no attempts to make periodic revisions and not surprisingly, the tax bases hardly reflected the true market rents.

³⁶ For a historical account of the developments in property tax, see (Rao, 2008).

A major constraint in the determination of the 'true' tax base was the interpretation of the Courts that for determining the base of property tax, it is not the actual or presumptive rent, but the 'fair' rent as laid down in the Rent Control Acts of the respective State governments should form the basis of determining the annual rental value. A number of studies have analyzed the adverse revenue implications arising from this decision (Pethe and Karnik, 2003). However, in later judgments, the Supreme Court interpreted the *nonobstante* clause in the statutes and delinked the presumed rent for property tax purposes from the Rent Control Acts (Rao, 2008).

The most important development, however, was the reform initiated by Patna Municipal Corporation which moved over to a completely presumptive area-based valuation taking into account the location, usage, built –up area and the type of construction. There were 3 norms for location (principal main roads, main roads and others), 3 construction types (*pucca* with reinforced concrete roof, *pucca* with asbestos or corrugated sheet and others) and three usage categories (commercial/industrial, residential and others), thus making 27 combinations. By fixing the annual rental value per m² for each of the categories, the tax base was determined. The result of this reform was that the tax rate was reduced from the prevailing 43.75% to 9%. Interestingly, the Supreme Court upheld the new method of valuation on the grounds that it eliminated arbitrariness and discretion (and corruption). Subsequently, a number of cities adopted the reform with varied degrees of success.

The more recent initiative for reforming the property taxation was mandated as a part of the conditionality in the central government's assistance program for the municipal corporations for up-grading of their infrastructure and services. Named after the First Prime Minister, the Jawaharlal Nehru National Urban Renewal Mission (JNNURM) mandated the reform of property tax systems. In addition, the standardized service levels stipulated for municipalities by the Ministry of Urban Development also mandate the on-line system for payment of property tax and the use of GIS system for the mapping of properties to ensure comprehensive coverage.

Subsequently, there have been reform initiatives in a number of cities, though the results of these reforms have been varied. Furthermore, many of the reform initiatives have been recent and the revenue implications of these reforms are yet to be ascertained. The most reform attempts are to bring about clarity and

transparency in the determination of tax base, reduce cost of collection, improve the ease of tax collection and reduce the compliance cost. The important measures in this direction include switching over to the area based valuation to determine the tax base, introduction of self-assessment (declaration) scheme, building a comprehensive data base containing the registry of the taxable properties, transparency and attempts at taking the taxpayer into confidence in the reform attempts, on-line payment of the tax and other measures to ensure ease of payments and better coverage of the tax by using GIS mapping.

A detailed study of the reforms in 10 cities by the National Institute of Urban Affairs (NIUA) brings out some interesting findings (NIUA, 2010). The study shows that the trend has been to move away from the annual rental value based system to area based system, though some of the municipalities continue with the old system but determine the rental values in a presumptive manner and many of them determine the values based on the recommendations of the Municipal Valuation Committees comprising of experts in urban administration, taxation, and representatives from the local body.

In places where area based taxation is followed, properties are classified in terms of factors such as location, usage, type of construction and age of the building. Most of the municipal corporations follow a progressive rate structure, but some of the municipal corporations like Bangalore and Ludhiana levy a flat rate of tax with rates differentiated between residential and non-residential dwellings and lower rates for owner occupied as compared to rented houses. Some of the municipal corporations levy the tax on vacant lands though while determining the total area. However, the plot size is not taken into account while determining the value in the case of independent houses/villas and this tends to reduce the progressivity in case of rich owners building houses in large plots of land.

On the tax administration, some have computerized and adopted the property identification code, many still to act on this front. On using the GIS to identify the missing properties from the tax register, Bangalore has completed the exercise and the effort is going on in Ahmedabad. In most others, the initiative is yet to be taken. Many of the corporations have introduced the self-assessment scheme and a few like Bangalore have introduced on-line payment of the tax.

As mentioned earlier the successes of reforms have been uneven. While the revenue productivity in Bangalore has shown a sharp increase, in many others including Delhi, the revenues have continued to be stagnant. Unfortunately, Patna, the first municipal corporation to introduce area based taxation has the lowest and most stagnant per capita collections. In most cases, while the initial effort yielded good results in terms of increasing revenues, over the years, stagnancy crept in as they were not able to undertake periodic revaluations. Bangalore is an exception even here as the municipal corporation undertook a revaluation exercise in 2008 to maintain the high buoyancy of the tax.

An important feature of the reforms is the replacement of annual rental value with values determined on the basis of floor area for the purpose of taxation. Even in the case of the area based value, imputed values will have to be based on either the market rents or the capital values. Bangalore Municipal Corporation has moved over to the capital value basis to determine the values of property within the area based taxation. As mentioned earlier, any presumptive taxation can succeed only when the actual base chosen is substantially lower than the market value not only because, the market value is not a realized value and there are limits to increase the tax payments on a property when the reform is done³⁷.

The advantages of the area based taxation are stated as its objectivity, transparency, fairness and lower compliance cost. However, there is a major challenge in designing the tax that can fulfill all these qualities. Whichever method is taken it is necessary to initially determine the guidance values and it is not clear or transparent how these are determined. Taking the values of the properties transacted may not be realistic partly because, in most developing countries, the registered values of the properties transacted is substantially higher than the actual values at which these are transacted. Then fairness in taxation demands that several considerations that must be taken account of in determining the tax base. These relate to the location, age, type of construction, usage (residential, commercial/industrial), the type of residents (owner occupied versus tenants). More the categorization, better the differential values are captured, but more complex and non-transparent the tax base determination will be. Thus, there is a clear trade-

³⁷ The Bangalore Municipal Corporation limited it to two and a half times when it switched over to the area based taxation to ensure acceptability.

off between fairness and complexity³⁸. Too much of differentiation may defeat the cannon of simplicity.

Another major challenge of the area based system is the need to make the revision in the values from time to time to keep up with the changes in value to make the tax responsive to changes in nominal incomes. Changes in the value may be due to increase in the prices of property values (including capital gains), or additions/improvements done to properties. In the absence of periodic revisions, the revenue productivity of the tax will be low. At the same time, as mentioned earlier, there can be severe political opposition to periodic revisions and more importantly, capturing the unrealized capital gains in the base can pose severe problems in its acceptability.

3.4.5 Towards Reforming the Property Tax System in India

Reforming the property tax system is critical to making the cities the leading edges of economic dynamism. This is particularly true of India where the backlog in urban infrastructure is large and the standards of urban services, poor. There is no doubt that contrary to the experience of many cities across the globe where the tax played an important role in financing urban services, property tax revenues have been inconsequential and have not played any significant role in financing urban services.

The challenge of reforming property taxes in urban areas in India is, however, daunting. With the urban property owners having used to enjoying exemptions and concessions or paying very low levels of the tax, the revenues have been low and stagnant in absolute terms and declining as a ratio of GDP, ensuring larger payments from and imparting greater buoyancy to the tax is bound to be very challenging. Exploiting the large revenue potential of this tax should be an important agenda to facilitate urban renewal, but the challenge is formidable.

The reform of the property tax system should begin with having a separate tax powers to urban local bodies. As mentioned earlier, placing the local tax powers in the State List has denied them the power to determine the base, the rate structure and administrative and enforcement mechanism. Further more, it has given the State governments to abolish the property tax altogether for populist reasons

³⁸ Rao (2008; p. 251) shows that when all these factors are considered, there may be 240 different categories.

without providing any alternative revenue source, thus denying them an important revenue source and leaving them with large unfunded mandates. While the state governments should provide autonomy to the local bodies to levy, collect and appropriate the revenues from property tax, it is important to undertake measures to build their capacity to design implement and enforce the tax. The handholding is particularly important for smaller municipalities. It would be useful to create an advisory cell in the Urban Development department of each of the state governments to undertake this task.

Wide ranging exemptions and concessions tend to erode the tax base significantly. It is therefore, necessary to have a relook at the exemptions. Furthermore, from the viewpoint of both equity and revenue, it is important to include the plot area along with the built up area in the tax base, though the tax rate on the latter may be lower. At present, the floor area of a bungalow and an apartment is treated alike. There should be an intelligence cell in every property tax department to focus on the additions and improvements to properties and getting information on the changes in property values.

The experience of reform with the property tax shows that transition from the annual rental value to area based taxation holds a lot of promise and if properly done, can bring in significant additional revenues. However, care should be taken while designing the tax base and assigning presumptive values. The first important precondition is the transparency to ensure acceptability of the tax. After making the categorizations in terms of different zones (zones need not be geographically contiguous but should reflect similar land values), type of construction and age, the presumptive values for each category must be published and the people should be made to walk through the calculations to work out their tax liability. Fairness requires that the people should see transparently the way in which tax has been designed. Besides wide publicity and taxpayer education, there should be a public relations cell that should deal satisfactorily with all questions and confusions relating to the tax in a clear manner.

The transition to area based valuation does that necessarily mean it will reflect market values and therefore, an end in itself. This should be construed only as a transitional measure. This is a presumptive base; it will be accepted only when the base quantified is substantially lower than the actual market value. In other words, even after significant differentiation in terms of location, types of use, type of

construction, age of buildings etc., and the quantified base could have only a distant relationship with the Market values of the property. In the ultimate analysis, presumptive values can have stronger relationship with the market values only when the urban property market is well developed and organized.

This would require other important policy interventions including the abolition of legislations constraining the markets such as rent control acts, urban land ceiling acts as well as reforming the provisions relating to the taxation of capital gains and registration fees. At present, there is disincentive for both the seller and buyer to declare the true value of the properties transacted which is often used in formulating the guidance value. The seller would like to under report the value to evade capital gains taxation and the buyer would like to under report the purchase price to evade registration fees. Taxing the capital gains at a lower rate and having a lower rate of stamp registration fees could help to develop organized markets for immovable properties.

The area based property tax tends to be relatively stagnant as it is unresponsive to changes in the prices of properties pending revaluations. The only source of increase in property tax is the increase in the number of properties. While there are inherent difficulties in imputing the capital gains over times as these gains are not realized until they are sold in the market, as increase in prices affects the cost of providing public services, it is necessary to introduce an element of indexation of the values. The estimate of property prices is made by the National Housing Bank at present for some major cities. If the guidance cell in each of the State Urban Development department works out the trends in property prices in different municipal areas using similar methodology, the municipal bodies can automatically adjust the values of the tax bases to these indexes for the purpose of property taxation.

A major requirement for the tax reform is the ownership of the reform by the tax administration. It is important that the tax officials should not only understand the reform well, but also be prepared to undertake advocacy. Equally important is the need to have a high degree of coordination and exchange of information between the connected departments. Much can be gained by having information exchange between the property tax department and various departments that undertake valuation, public works and registration of property transactions.

An important problem constraining the reform is the absence of a comprehensive cadaster of properties in urban areas which should be computerized. Clear assignment of ownership or tenancy rights is extremely important to levy the tax. Most municipal governments do not have up to date register of property ownership and in many cases, there are ownership disputes. In many cases, due to rigid tenancy laws, the tenants have lived in the properties for long and the owners do not find it worthwhile paying the tax. In many case the enforcements have been ineffective. These can be remedied only when there is a strong leadership and political willingness at the municipal level. Comprehensiveness also requires mapping the taxpaying properties with the information contained in the GIS. In addition, the department can also resort to third party information. A mechanism should be found to incorporate the value of additions and improvements to the original buildings by having an intelligence network.

Computerized register of properties and taxpayer education helps to introduce on-line payment of the tax. This is extremely important to avoid a constant interface between the taxpayer and collector. This will improve tax compliance and significantly reduce the compliance cost. While some of the municipal corporations like Bangalore have facilitated the tax payments by having online payment tax, many others, including Delhi have not. It is important to ensure ease of tax payments including the online payments.

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3.5 INDONESIA : Challenges to Collect Property Taxes in Surabaya City, Indonesia

(Tri Rismaharini , Suhartoyo)

3.5.1 Introduction

The enactment of Law No. 32 year 2004 on Subnational Government as was amended by Law No. 12 year 2008, provides local administration with broader authority with aiming to increase the efficiency and effectiveness of subnational government functions. The decentralization of functions required a substantial source of revenues. There fore, the decentralization policies were accompanied by the enactment of Law No. 33 Year 2004 to govern financial balance between Central Government and Subnational Governments.

Based on Law No. 33 Year 2004, it was regulated that to finance their functions and undertake development programs at the local level, local governments obtain income from:

- a. Local owned revenues, consisting of:
 - 1) Local taxes and charges revenues
 - 2) Revenue from local owned companies
 - 3) Other legitimate revenues
- b. Balanced Fund, consisting of:
 - 1) Revenue Sharing Fund (natural resources and taxes)
 - 2) General Allocation Fund
 - 3) Specific Allocation Fund
- c. Other revenues

Local governments are encouraged to raise local revenues especially local taxes and levies as an important source of revenue to finance the local government administration. In order to improve the provision of public services and local independency, it is necessary to expand the objects of local taxes and charges, providing the local governments with full discretion of setting tax rates. The imposition of local taxes and charges should be based on the principles of democracy, equality and justice, community participation, and tax potentials.

Law No. 28 FY 2009 on Subnational Taxes and Charges, became effective in January 2010 adopts the principle of a 'closed-list' system where the kind of subnational taxes and charges are listed. Local governments are allowed to collect 11 types of taxes and 30 types of local charges. They are not allowed to collect taxes and charges other than those that are stated in the law. Among the 11 types of local taxes, two of them were devolved from central government, namely '*land and building transfer tax*' (BPHTB) and '*rural and urban land and building tax*' (PBB-P2).

Before the enactment of the Law No. 28 Year 2009, BPHTB and PBB-P2 were levied and administered by the central government, and the revenues were transferred to local governments as shared revenue. The devolution of PBB-P2 and BPHTB are expected to increase the fiscal capacity of local governments, especially local own revenues.

Property is one of the investment instruments for the societies, especially in the urban areas. The growing economy will bring the increase of BPHTB revenue as the transaction frequency and the land and building values will increase. In Surabaya City, PBB-P2 and BPHTB contribute significantly to its local own revenues. Therefore, the city government quickly sought to take the collection of the said taxes.

3.5.2 Preparation for PBB-P2 and BPHTB Collections

Since January 1, 2011, the government of Surabaya City has started collecting PBB-P2 and BPHTB simultaneously. As a matter of fact, Surabaya City was the first local government in Indonesia that took over the collection and administration of PBB-P2 by issuing local regulation and investing quite a number of funds on the development of systems and infrastructures as well as human capacities.

In the preparation of PBB-P2 and BPHTB collections, Surabaya City has taken some strategic measures as following:

Legal Framework

Legal basis for the collection of PBB-P2 is local rregulation No. 10 Year 2010, while for BPHTB is local regulation No. 11 Year 2010. Some important stipulations in the regulations are as following:

a- Tax rates

For PBB-P2, tax rate is set at 0.1% of the tax object sales value (NJOP) for properties that worth IDR 1 billion or less and 0.2% for properties that worth more than IDR 1 billion. The effective rates are the same as the rates that were applied by central government previously and less than the maximum rate stated in the law, 0.3%.

Tax reduction of 50% is provided for the utilization of land and buildings that are environmentally friendly or cultural heritage. On the other hand, disincentives are given to the utilization of land and buildings that may distract the environment by charging additional tax of 50%.

For BPHTB, tax rate is set at 5% of the tax object transaction value (NPOP) or the tax object sales value (NJOP) whichever is higher.

b- Non-Taxable PBB-P2

Every taxpayer is given a non-taxable PBB-P2 up to IDR 15 million.

c- Non-Taxable BPHTB

Every taxpayer is given a non-taxable BPHTB up to IDR 75 million.

In the case of the acquisition of rights by inheritance or testamentary grant received by an individual who is still in the family relationship by blood lineage straight one degree up or down by one degree, including husband/wife, non-taxable BPHTB is IDR 400 million.

d- Tax Object Sales Value (NJOP)

A variable that is directly controlled by the government for tax calculation is the determination of the Tax Object Object Sales Value (NPOP). The value is published by the head of local government regulation. Surabaya City Government has issued by Mayor Regulations No. 73 Year 2010 governing the NJOP and its classification as the tax base for PBB-P2 calculation. Under these provisions, land is divided into 100 classes while building divided into 40 classes.

In practice, during the first year of devolution period, the city government used the data submitted by the Directorate General of Taxation as a basis for establishing the PBB-P2. In the second year, some adjustments were made based on the indicated transaction value and field surveys.

Infrastructures and Facilities

Preparation for property taxes collection is done by developing infrastructures and providing facilities, include:

- (a) Reviewing and adding tasks and duties of each division and section in the organization that deals with local taxation.
- (b) Forming additional Office Technical Units, from 5 units to 8 units, to intensify the coverage area of UPTD from initially 1 unit serving 6 sub-districts into 1 unit serving 4 sub-districts.
- (c) Procuring of equipment for operations such as servers, computers and printing equipment, and other documents.

Human Capacities

Preparation is done by sending staffs to educational institutions and training programs to provide adequate personal staffs.

Financing

Funding is budgeted gradually through annual budget to finance the preparation of regulations such as socialization, provision of infrastructures and facilities and the education and training of managers.

3.5.3 The Achievement of the PBB-P2 and BPHTB Devolution

Local Revenues

The revenue of Surabaya City increased annually, from IDR 2,675 billion in 2009 to IDR 4,605 billion in 2012, with an average annual increase of IDR 571 billion.

Surabaya City Target and Realization of Local Revenues, Year 2009 – 2012, (in IDR)

No.	Types of Revenues	2009	2010	2011	2012
1	Local Own Revenue	809,795,526,042	908,647,775,730	1,886,514,301,581	2,353,324,920,469
2	Balance Fund	1,448,259,536,803	1,445,414,314,692	963,419,947,354	1,404,313,958,313
3	Others	417,324,931,829	689,962,701,335	909,100,178,376	848,061,858,369
	Total	2,675,379,994,674	3,044,024,791,757	3,759,034,427,311	4,605,700,737,151

Surabaya City Increase of Local Revenues, Year 2009 – 2012, (in IDR)

No.	Types of Revenues	2009	2010	2011	2012
1	Local Own Revenue	80,582,206,698	98,852,249,688	977,866,525,851	466,810,618,888
2	Balance Fund	159,048,005,987	2,845,222,111	481,994,367,338	440,894,010,959
3	Others	116,987,012,380	272,637,769,506	219,137,477,041	61,038,320,007
	Total	356,617,225,065	368,644,797,083	715,009,635,554	846,666,309,840

Revenue growth on average per year is 18.79%, with the highest average local own revenue by 38.91% followed by miscellaneous revenue amounted to 32.33% and by 6.14% Balance Fund.

Surabaya City, Local Revenue Growth, Year 2009 – 2012, (in %)

No.	Types of Revenues	2009	2010	2011	2012	Average
1	Local Own Revenue	11.05	12.21	107.62	24.74	38.91
2	Balance Fund	12.34	0.20	33.35	45.76	6.14
3	Others	38.95	65.33	31.76	6.71	32.33
	Total	15.38	13.78	23.49	22.52	18.79

Local revenue contribution given the highest average of Revenue at 40.35% and the contribution in year 2009 amounted to 30.27%, increase to 51.10% of the value indicated Revenue provide information local financial capacity continues to increase.

Surabaya City, Local Revenue Contributors, Year 2009 – 2012, (in %)

No.	Types of Revenues	2009	2010	2011	2012	Average
1	Local Own Revenue	30.27	29.85	50.19	51.10	40.35
2	Balance Fund	54.13	47.48	25.63	30.49	39.43
3	Others	15.60	22.67	24.18	18.41	20.22
	Total	100.00	100.00	100.00	100.00	100.00

Local Own Revenues

Local own revenue consists of local taxes, local charges, and dividends from local owned companies. In 2009, local tax realization amounted to IDR 442 billion while the set target was to IDR 1,909 billion in 2012 or an average annual increase of IDR 377 billion.

Surabaya City, Target and Realization of Local Own Revenues, Year 2009 – 2012, (in IDR)

No.	Types of Local Own Revenues	2009	2010	2011	2012
1	Local Taxes	442,852,257,428	525,403,484,538	1,488,358,147,753	1,909,562,850,00
2	Local Charges	164,247,724,956	183,312,246,927	209,834,317,888	251,896,629,645
3	Dividends	43,324,809,294	63,304,547,606	75,962,115,306	82,515,616,099
4	Others	159,370,734,364	136,627,496,659	105,259,156,201	109,349,824,725
	Total	809,795,526,042	908,647,775,730	1,879,413,737,148	2,353.324.920,469

A big jump of local taxes revenue took place in 2011 that reached IDR 1,488 billion or increased by IDR 962 billion compared to the local taxes realization in 2010 which was only IDR 525 billion.

Surabaya City, Increase of Local Own Revenues, Year 2009 – 2012, (in IDR)

No.	Types of Local Own Revenues	2009	2010	2011	2012
1	Local Taxes	44,862,061,822	82,551,227,110	962,954,663,215	421,204,702,247
2	Local Charges	5,310,641,501	19,064,521,971	26,522,070,961	42,062,311,757
3	Dividends	804,780,802	19,979,738,312	12,667,567,700	6,553,500,793
4	Others	40,226,005,576	22,743,237,705	31,368,340,458	4,090,668,524
	Total	80,582,206,699	98,852,249,688	970,765,961,418	473,911,183,321

Local own revenue grow with the average of 38.83% per year. The highest average growth is in the Local Taxes at 60.37%. The dividends from local owned companies grew by 19:16%, local charges by 10.75%, and other legitimate revenue by 0.10%.

Surabaya City, Local Own Revenue Growth, Year 2009 – 2012, (in %)

No.	Types of Local Own Revenues	2009	2010	2011	2012	Average
1	Local Taxes	11.27	18.64	183.28	28.30	60.37
2	Local Charges	3.13	11.61	14.47	20.05	10.75
3	Dividends	1.89	46.12	19.99	8.63	19.16
4	Others	33.76	14.27	22.96	3.89	0.10
	Total	11.05	12.21	106.84	25.22	38.83

Local taxes is the main contribution to the local own revenues. Its shares increase annually, from 54.69% in 2009, 52.82% in 2010, 79.19% in 2011 and 81.14% in 2012. Average, the local taxes contributed 68.2% to local own revenues during 2009 – 2012. It shows that the devolution of PBB-P2 and BPHTB has provided significant revenue source to local government.

Surabaya City, Local Own Revenue Contributors, Year 2009 – 2012, (in %)

No.	Types of Local Own Revenues	2009	2010	2011	2012	Average
1	Local Taxes	54.69	57.82	79.19	81.14	68.21
2	Local Charges	20.28	20.17	11.16	10.70	15.58
3	Dividends	5.35	6.97	4.04	3.51	4.97
4	Others	19.68	15.04	5.60	4.65	11.24
	Total	100.00	100.00	100.00	100.00	100.00

3.5.4 PBB-P2 and PBHTB Revenues

Surabaya City received the last revenue sharing of PBB-P2 and BPHTB from central government in 2010 with the total amount of IDR 577.1 billion or IDR 341.7 billion and 235.4 billion respectively. When the two taxes were fully collected and administered by Surabaya City in 2011, the revenue increased dramatically to the total of IDR 956.7 billion or IDR 540.4 billion and IDR 416.3 billion respectively.

In 2012, PBB-P2 revenue was targeted to IDR 790 billion and BPHTB IDR 419 billion. The revenue realization up to the third quarter of 2012 (September), PBB-P2 is IDR 517 billion and BPHTB is IDR 370 billion. It indicates that Surabaya City can manage the collection of property taxes well.

Surabaya City, Target and Realization of PBB and BPHTB Revenues, Year 2009 – 2012, (in IDR)

No.	Types of Taxes	2009	2010	2011	2012
1	PBB	308,143,066,275	341,759,567,832	540,428,563,239	790,613,785,000
2	BPHTB	208,617,149,054	235,436,405,701	416,314,633,814	419,270,247,000
	PBB + BPHTB	516,760,215,329	577,195,973,533	956,743,197,053	1,209,884,032,000

3.5.5 Challenges to collect PBB-P2 and BPHTB

The main challenges faced by Surabaya City in collecting PBB-P2 and BPHTB are related with data availability and administration as following:

PBB-P2

The problems of collecting PBB-P2 are mainly in the quality of data with the following characteristics:

- The amount of tax arrears received from the DG of Taxation in early 2011 was about IDR.619 billion. The settlement is done by charging and re-evaluating the data receivables.
- The existence of an object that has a tax marking more than one. The process of settlement by way of checking the location if proven it would be cancelled upon marking incorrect.
- There are a number of imaginary tax objectsthat remains unknown. The settlement is done by redoing the data collection of the existing tax object.

BPHTB

Certain taxpayers' behaviour and administration problems have been constraints to the collection of BPHTB, such as:

- A taxpayer used the tax object number of other people in property transaction.

To settle the problem, Surabaya City has examined the location of the tax object in the map, whether it is in accordance with the transaction or not.

- Unable to link the tax object number and the Land Use Permit (SIPT) in the monthly report.
The resolution was made by requesting list of transactions that have been executed by the notary.

3.5.6 Conclusion and Recommendation

1. As stipulated in the Law No. 28 Year 2009 on Sub-National Taxes and Charges, local governments can collect 11 types of local taxes and 30 types of local charges. Two of the 11 local taxes are 'land and building transfer tax' or BPHTB and 'rural and urban land and building tax' or PBB-P2 that were devolved from central government.
2. Surabaya City Government acted quickly enough to implement Law No. 28 Year 2009 by collecting BPHTB and PBB-P2 in the first year of the transition period (2011). A strategy that was adopted by Surabaya City was to take over the collection of PBB-P2 and BPHTB as quickly as possible by preparing legal bases, infrastructures and facilities, and human resource before January 2011.
3. The government of Surabaya City has been able to manage the collection of PBB-P2 and BPHTB simultaneously since 2011. Some challenges that were faced during the devolution process could be solved by applying certain strategies and methodologies.
4. The devolution of PBB-P2 and PBHTB to local governments have resulted the increased revenue of Surabaya City. The revenue of both types of taxes contributes to around 51% of Surabaya City revenue or 81% of its local own revenue.

3.6 INDONESIA : Challenges to Devolve Property Tax in Indonesia

(Adijanto)

3.6.1 Introduction

Indonesia has issued Law No. 28/2009 on Subnational Taxes and Charges to replace Law No. 34/2000. The new law established a closed list of subnational taxes which includes the 'rural and urban land and building tax (*Pajak Bumi dan Bangunan Perdesaan dan Perkotaan* or PBB-P2) and the 'land and building transfer tax' (*Bea Perolehan Hak atas Tanah dan Bangunan* or BPHTB) available for local governments.

The PBB-P2 and BPHTB are now devolved to the local governments (districts and municipalities) levels. Both PBB-P2 and BPHTB were previously designated as central taxes with the revenues shared with provincial and local governments. The PBB levied on the plantation, forestry and mining sectors remain to be administered as central shared taxes.

Under Law No. 28/2009, Local governments are given broad authority to determine the tax rates (with a maximum rate set by the law), the exemptions, the due date of payments, number of installments, and the tax administration systems to apply. The Law also provides flexibility for the local governments as to whether to implement or not to implement any subnational tax, depending on its potential revenue. For example a local government may decide not to implement it, because the administrative costs are higher than revenues collected.

The BPHTB was adopted simultaneously by all districts and municipalities in Indonesia by January 1, 2011. In terms of revenue, the devolution of BPHTB to local level has shown a successful one as the total revenue collected for the first year of devolution was not less than the previous year. However, there are few local governments that have not implemented the said tax due to the low tax potentials.

The PBB-P2 is expected to be transferred to local governments gradually but concluding no later than January 1, 2014. The 4 years transition periods are considered to be short, given the amount of work to be prepared and given the potential magnitude of revenue loss if local governments fail to prepare their systems and procedures on time. If, local governments are not ready to levy PBB-P2

by January 2014, for instance, then there is no other level of government currently authorized to collect the tax.

3.6.2 The Property Taxes as Local Taxes

In accordance with Law No. 28/2009, local governments are authorized to determine the tariff rates and exemption levels within the following parameters:

BPHTB

- a maximum rate of 5%;
- a minimum exemption level (NPOPTKP) of IDR 60,000,000 for most transactions;
- a minimum exemption level (NPOPTKP) of IDR 300,000,000 for heir transactions.

As with other local taxes, BPHTB is a self-assessment form of tax. In addition, Public Notaries and the National Land Agency (BPN) are two important institutions that support administrative processes of BPHTB collections. With its relatively high value of valuation exemption (IDR60,000,000) it is estimated that there will not be too many BPHTB's transactions in many LGs in Indonesia, with the exception of the large cities.

For the implementation of BPHTB systems, local governments do not really require any sophisticated information technology software / applications as long as they are able to develop an adequate data communication systems with Public Notaries and National Land Agency.

PBB-P2

- a maximum rate of 0.3%;
- valuation exemption (NJOPTKP), with a minimum threshold value of Rp 10,000,000;
- due dates and the number of payment installments;
- tax administration systems.

Devolving the PBB-P2 will be more complicated. There are many administrative functions related to PBB-P2 processes, such as property information data collection; property valuation; tax assessment and distribution of tax bills;

revenue collection; enforcement; appeals; arrears management; and taxpayer services.

3.6.3 The Challenges and Strategic Options

The main challenges for devolving PBB-P2 is a wide difference in revenue and administrative capacity among the 491 local governments in Indonesia (January 2012). For this reason, it is useful to classify local governments into several groups/clusters. The groupings can be related to asymmetric approaches and strategies which could be undertaken for each group/cluster to smooth out the devolution process.

***Clustering of Local Governments (Districts and Municipalities)
By PBB-P2 Revenue Capacities***

ID	Clusters	Local Governments	% of total LGs	% of National PBB-P2 Revenues
1	Cluster 1	30	6%	70%
2	Cluster 2	100	20%	20%
3	Cluster 3	361	74%	10%
	Total	491	100%	100%

In the transition period (between 2011 to the end of 2013), all local governments in all clusters should implement the collection of PBB-P2 by issuing local regulations. The high tax potential local governments (cluster 1 and some of cluster 2) are expected to adopt full PBB-P2 administration and carry out all administrative functions, such as: data collection; valuations; distribution; billing; and the provision of services to taxpayers. Some of cluster 2 and cluster 3 may not be able to carry out all functions of PBB-P2 collections at once.

Due to the different revenue capacities, our experiences showed that the high tax potential local governments (big cities and some districts) quickly and actively responded to the PBB-P2 devolution policy by issuing local regulations, developing IT systems, preparing infrastructures and facilities, and training staffs to be able to collect property taxes as soon as possible. They viewed that the investment costs for these preparations will be paid off by the increased revenue of property taxes. On the other hand, the local governments view that the investment costs will be

much higher than the revenues that may be obtained from the collection of property taxes. These local governments slowly adopted the new policies and expected bigger supports from the central government.

The strategy to support the transfer of PBB-P2 for each cluster therefore should be different.

The specific forms of assistance that need to be provided by central government are:

- Central policy and technical support as guidelines for local governments in preparing local regulations and the transfer of an appropriate IT systems, property information and related procedures;
- Technical and capacity building support related to the migration of SISMIOP, property information, and procedures, with some training, internships, assistance for at least two cycles of PBB administrative devolution, provided mainly by KPP;
- Information technology systems provide technical support and development to implementation of IT systems. There are several possible IT options that can be applied to support local administration and joint administration, with the following criteria:
 - The high tax potential local governments are expected to copy the existing IT systems (SISMIOP Oracle based system) by making minor changes to suit the local governments' conditions. Since the information technology will not change much, then, the business process system will also only need minor changes.
 - For local governments with limited funding capacity to purchase an Oracle license, central government (DG Tax) prepares a simple technical application that allows local governments using remote access to access the existing application and database in the local tax office during the transition period until 2014. With this option, these local governments do not need to purchase a license for Oracle so that cost shifting becomes more affordable.
- In medium and longer term, the government needs to support capacity building of technical expertise in the field of data collection and assessment and

prepare a systematic capacity development plan for building tax policy awareness. Furthermore, local tax office can also conduct capacity building to local governments' staff by providing opportunities for local governments' staff to participate with KPP as they perform their routine data collections and assessments (*extensification*). Capacity development is also needed to improve the ability of local government staff in other administrative functions, such as the distribution of tax bill, payment, billing, handling complaints, lawsuits; and other taxpayer services.

Specifically for low tax potential local governments (LGs in cluster 3), the administration functions to these local governments should be provided in stages. After issuing local regulations, administration functions that should be carried out by these local governments are the preparation of tax billing and collection of the tax. Other functions can be supported by other parties (such as local tax office or other parties) to work on the valuation and systems development.

There are several types of third-party agencies that could be participating to support local governments in carrying out some of PBB-P2 administration functions, namely:

- 1) Local tax office support local governments for having the trained, experienced human resources, management capacity and adequate equipment for PBB-P2 collections.
- 2) Joint ventures between regions, where local governments could work out arrangements to pool administrative responsibilities with cost-sharing in order to take advantage of administrative economies of scale.
- 3) Outsourcing to third parties for example, to local companies that could provide these services at reasonable cost (eg, billing and data maintenance functions).

3.6.4 The Progress of Property Taxes Devolution Process

The devolution of BPHTB to local governments has been successfully implemented in 2011 where the total revenue collected during this year was not less than the BPHTB revenue of 2010 when the tax was collected by central government. However, there were several local governments that had not collected BPHTB for efficiency reason, mainly the regions in the remote areas in the eastern part of

Indonesia. The improvement for BPHTB administration at the local level has been done gradually by providing technical guidance, training, and policy adjustments. PBB-P2 was collected at the first time by Surabaya City of East Java in 2011. In 2011 and 2012, this city had been able to collect PBB-P2 much more than it was in 2010. Other 17 local governments collected PBB-P2 in 2012. It is expected that another 100 local governments will collect PBB-P2 in 2013, and the rest will collect PBB-P2 in 2014, the latest transition period.

With strategic measures as outlined in the road-map for PBB-P2 devolution and better coordination between central and local governments, it is expected that the devolution process of PBB-P2 will be successfully implemented in time. Beside encouraging local governments to make better preparation for the collection of PBB-P2, a number of policy and technical issues encountered during the process will be tackled and improved.

3.6.5 Conclusion

In 2010, Indonesia decided to transfer property taxes (BPHTB and PBB-P2) from central government to local governments (districts and municipalities). The transition period for the devolution is 4 years. In 2014, all local governments are expected to collect property taxes or no level of government will collect the tax as of FY 2014.

There are a number of challenges faced in the devolution process, among others: the wide diversity of tax potentials over regions that brings about different responses to the devolution policy. To solve this condition, different strategy should be applied to different clusters of local governments. High tax potential of local governments may not need support from central government as much as the low tax potential the local governments do. IT and data management systems as well as valuation are the PBB-P2 administration functions that need most attention to make the devolution process a successful one. Local capacity development and policy adjustment are other issues that need to be reviewed and improved.

3.7 INDONESIA : Property Tax Reform

(Hartoyo)

3.7.1 Introduction

Indonesia has undergone a series of property tax reforms. In the colonial era, there were a number of taxes on properties such as: land tax, landrente, and land rent. After proclamation of Indonesian independence and until 1985, the government introduced 'contribution to regional development' (IPEDA) as a revenue source for development.

A major reform on property tax was done in 1985 when a 'land and building tax' was introduced by issuing Law 12/1985. This tax was administered by the central government and collected by the Directorate General of Taxes. The objective of the enactment of Law 12/1985 are:

- for the effectiveness of tax collection
- for equity and fairness
- to increase national revenue
- to establish equality and uniformity

Property tax improvement was applied in 1994 by issuing Law 12/1994. With this law, property tax is determined as a central tax. The strategies for reform are as follows:

- Amending Law 12/1985
- Establish Data Base of Property Information Management Systems (PIMS/SSISMIOP)
- Improve Assessment System
- Improve Human Resources through education, training and implementing valuation standard.

As part of property taxation, in 1997 Indonesia introduced Law 21/1997 on land and building transfer tax, which is also a central tax. By this law, individuals or entities that obtain right on land and/or building are subject to land and building transfer tax with a single rate of 5%. The tax base is the transaction value of the properties or the sales price of tax objects (NJOP) which is decided by the Minister of Finance.

A major reform took place in 2009 by issuing Law 28/2009 on subnational taxes and charges. By this law, two types of property taxes (rural & urban land and building tax, land and building transfer tax) were devolved to local governments (districts and municipalities). The strategies for this reform are to:

- establish better collection systems
- Improve local taxing power
- improve the effectiveness of monitoring systems of tax collections
- broaden tax base of local taxes
- improve the PIMS (SISMIOP) for local governments

3.7.2 Comparisons of Property Taxes (as Central Taxes versus Local Taxes)

In general, property taxes policies under the new law and the previous one have no significant differences. The main change is the level of government which has the authority to collect the afore mentioned taxes. However, there are several distinctions of property taxes treatment between central and local taxes, as following :

Land and Bulding Transfer Tax

	As Central Tax	As Local Tax
Subject	Individual or an entity that obtains right on land and/or building	Individual or an entity that obtains right on land and/or building
Object	Acquisition right on land and or building	Acquisition right on land and or building
Tax Rate	5%	Maximum 5%
Non-Taxable	Maximum IDR300 Millionforinheritance or will grant	Minimum IDR300 Millionforinheritance or will grant
Acquisition Value	Maximum IDR 60 Million except inheritance or will grant	Minimum IDR 60 Million except inheritance or will grant
Tax Payable	5%x (NPOP – NPOPTKP)	5% (maximum) x (NPOP-NPOPTKP)

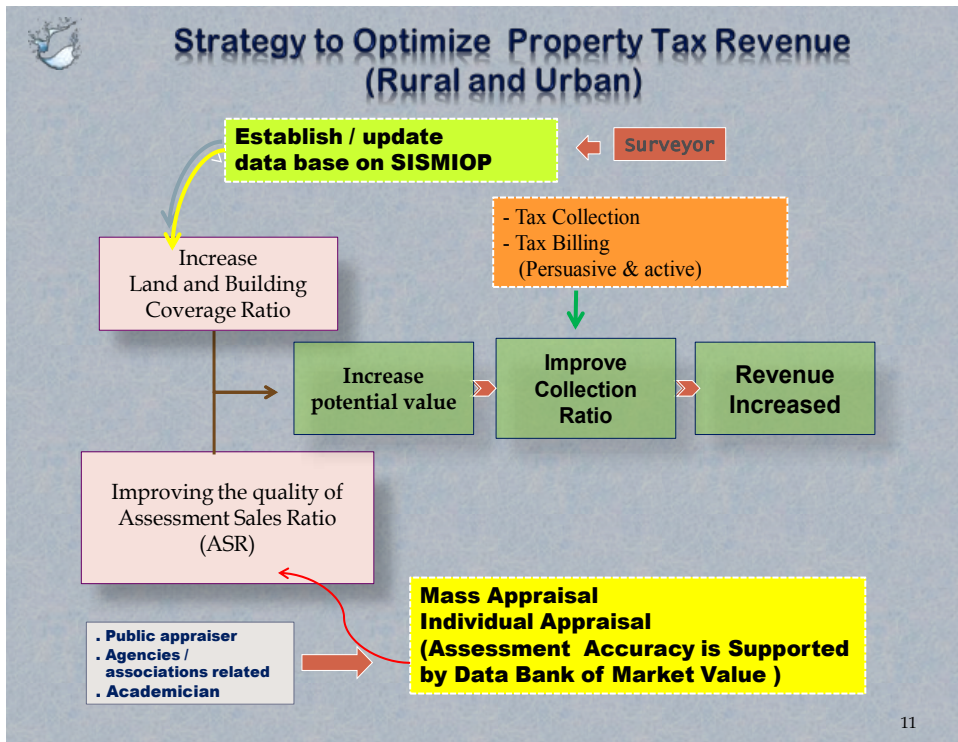
Rural & Urban Land and Bulding Tax :

	As Central Tax	As Local Tax
Tax Subject	Individuals or organization that actually have certain rights over land, and/or obtain benefits from land, and/or possess, control, and/or obtain benefits from buildings	Individuals or organization that actually have certain rights over land, and/or obtain benefits from land, and/or possess, control, and/or obtain benefits from buildings
Tax Object	Land and building	Land and/or Building, except areas that are used for the business activities of plantation, forestry and mining
Tax rate	0.5%	Maximum 0.3%
The Taxable Sales Value	Minimum 20% (twenty percent) and maximum 100% (one hundred percent) of the sales value of the tax object.	Not applicable
The Sales Value of Non-taxable Tax Objects	Maximum Rp24 Million	Minimum IDR 10 Million
Tax Payable	Tax Rate x NJKP x (NJOP-NJOPTKP): 0,5% x 20% x (NJOP-NJOPTKP) or 0,5% x 40% x (NJOP-NJOPTKP)	Tax Rate x (NJOP-NJOPTKP): (max0,3%) x (NJOP-NJOPTKP)

3.7.3 Strategy to optimize property tax revenue

The process of devoluting property taxes from central government to local governments took a significant amount of time due to different views and concerns of various stakeholders. One of the common concern was whether or not the property tax revenue can be collected optimally. If it could be granted, then the property tax was appropriately devolved to local governments.

There are two main components that play important role in the optimization of property tax revenue i.e. data management and valuation. The strategy that can be adopted is depicted as follows in the table below:



3.7.4 Decentralization of Property Tax as Local Tax

The decentralization of property taxes from central government to local governments began with the development of legal basis. Law 28 Year 2009 was the basic regulation for the devolution process and it was followed by a series of implementing regulations such as joint regulation of Minister of Finance and Minister of Home Affairs No. 213/PMK.07/2010 and No. 58 Year 2010 concerning preparation of property tax devolution as local taxes. The joint regulation was also followed by the Director General regulation No. PER-61/PJ/2010 concerning the procedures for preparation of property tax devolution as local taxes. As part of the preparation process, the government has conducted several activities to prepare local governments to be ready to collect property taxes, such as:

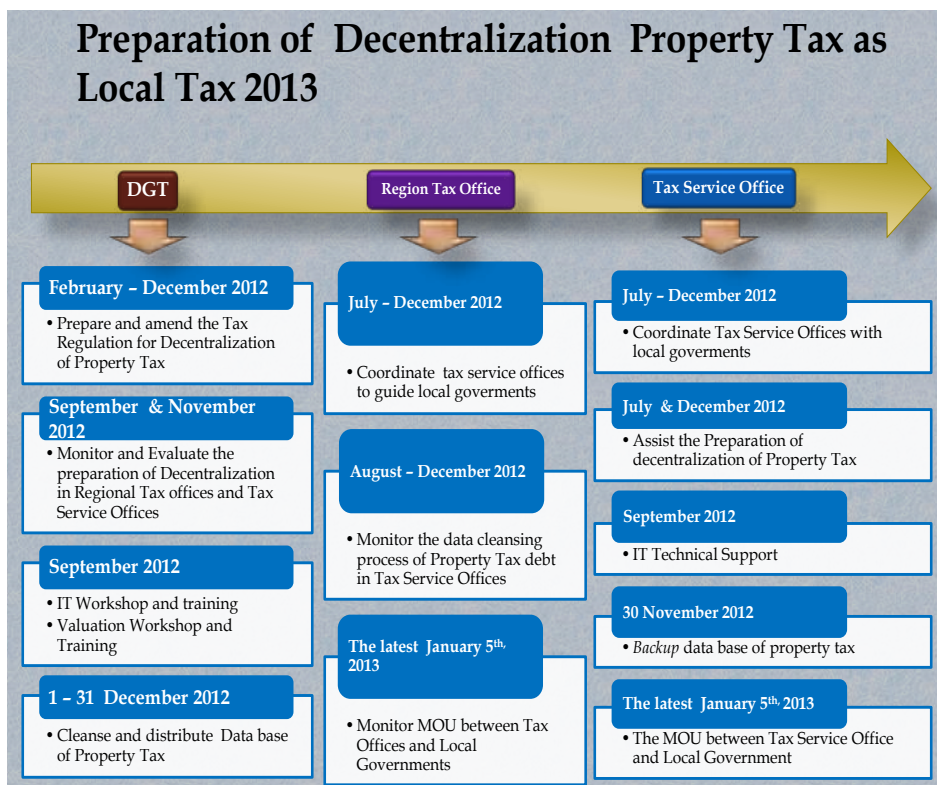
- coordination between local governments and regional tax offices/tax service offices (kpp)
- monitor and evaluate decentralization stages for each region
- IT workshop and training

- Cleanse and prepare the data base for each local government
- distribute the database of property tax to local governments
- valuation workshop and training

The table below describes the summary of activity plan of the Directorate General of Taxes, Regional Tax Offices, and Tax Service Offices in relation to the preparation of property tax devolution to local governments.

The result of the activities can be seen from the number of cities/districts that are ready to implement the collection of PBB-P2, as follows:

2011	1 city (Surabaya City)
2012	17 cities/districts
2013	105 cities/districts
2014	369 cities/districts



3.7.5 Conclusions

Indonesia has continuously reformed its property tax systems to increase the efficiency, accountability, and revenue optimality. At the beginning, property tax was determined as a central shared tax. The systems were improved gradually by making use of the development of information technology (IT).

To support the decentralization policies and adopt the international good practices, Indonesia conducted a major reform on property taxes in 2010. Two types of property taxes were devolved to local governments namely 'property transfer tax' (BPHTB) and 'rural and urban property tax' (PBB-P2). The two types of taxes contribute a significant source of revenue to local governments especially in more developed regions.

The devolution process is still on going. The Directorate General of Taxation and the Directorate General of Fiscal Balance together with the Ministry of Home Affairs hand in hand supported local governments to implement the collection of property taxes.



4. ANNEXES

Annex 1 Seminar Agenda

FIRST DAY / November 27, 2012	
08.00 – 09.00	Registration
09.00 – 09.30	Opening Ceremony / Keynote Speech: <input type="checkbox"/> Georg Witschel, Ambassador of FRG to Indonesia
09.30 – 10.00	<input type="checkbox"/> Agus D.W. Martowardojo, Minister of Finance of the Republic of Indonesia
10.00 – 10.30	Coffee / Tea break
10.30 – 11.15	Country paper presentations: <input type="checkbox"/> Ram Bahadur Aryal Chhetri: Challenges to Collect Property Tax in Nepal <input type="checkbox"/> M. A. Quader Sarker: Challenges to Collect Property Tax in Bangladesh
11.15 – 12.15	Panel discussion: <input type="checkbox"/> Rajendra Prasad Pokharel (Nepal) <input type="checkbox"/> Humaira Sayeeda (Bangladesh) <input type="checkbox"/> MachfudSidik (Indonesia)
12.15 – 13.15	Lunch
13.15 – 14.00	Country paper presentations: <input type="checkbox"/> MilwidaM. Guevara: Getting the right mix in property tax policies and administration <input type="checkbox"/> GovindaRao: Property Tax Reform in India
14.00 – 14.30	Coffee / Tea break
14.30 – 15.30	Panel discussion: <input type="checkbox"/> Anna Marie L. Fortuito (Philippines) <input type="checkbox"/> Pethe Abhay Moreshwar (India) <input type="checkbox"/> Chandra Fajri Ananda (Indonesia)
15.30 – 16.30	Plenary: <input type="checkbox"/> Lessons learned from country cases <input type="checkbox"/> Suggestions to address current challenges
19.00 – 21.00	Dinner & Cultural Event (Papua Traditional Dance & Accoustic): <input type="checkbox"/> Heru Subiyantoro, Secretary of <i>DG Fiscal Balance</i>

SECOND DAY / November 28, 2012	
08.00 – 09.00	Registration
09.00 – 09.30	Reflection and Summary of the first day presentations
09.30 – 10.30	Presentation and Panel Discussion on Indonesian Property Taxes: <ul style="list-style-type: none"> <input type="checkbox"/> TriRismaharini (Mayor of Surabaya City) : <i>Challenges to Collect Property Taxes in Surabaya City</i> <input type="checkbox"/> Adijanto (Director of Sub-national Taxes and Charges) : <i>Challenges to Devolve Property Taxes in Indonesia</i> <input type="checkbox"/> Hartoyo (Director of Extensification and Valuation): <i>Indonesian Property Tax Reform</i>
10.30 – 11.00	Coffee / Tea break
11.00 – 12.30	Break out sessions: Working Group 1 : <i>Data management and IT Support in property tax administration.</i> (Resource person: Anna Marie L. Fortuito) Working Group 2 : <i>The role of appraisal/valuation.</i> (Resource person: Said Rehman) Working Group 3 : <i>Tax evasion, enforcement, and accountability.</i> (Resource person: Akhmad Makhfatih)
12.30 – 13.30	Lunch
13.30 – 14.30	Cross-group sessions: (members of the working groups mix up to form new cross groups: sharing of the discussion results)
14.30 – 15.30	Plenary session: <ul style="list-style-type: none"> <input type="checkbox"/> Wrap-up and concluding remarks <input type="checkbox"/> The way forward
15.30 – 16.00	Closing Ceremony: <ul style="list-style-type: none"> <input type="checkbox"/> Ulrich Mohr, GIZ Country Director for Indonesia and Timor Leste <input type="checkbox"/> Heru Subiyantoro, Secretary of the Directorate General of Fiscal Balance, Ministry of Finance

Annex 2 List of Participants

No.	N a m e s	Countries	Position/ Organization	Role in the Seminar	Contact/ Address
1	Mr. Agus D. W. Martowardojo	Indonesia	Minister of Finance	Keynote speaker	Ministry of Finance Jl Wahidin No. 1, Jakarta, Indonesia
2	Mr. Marwanto Harjowiyono	Indonesia	Director General of Fiscal Balance, Min. of Finance	Speaker	Ministry of Finance Jl Wahidin No. 1, Jakarta, Indonesia
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10	Ms. Mahbuba Hossain	Bangladesh	Additional Com-missioner of Taxes, Tax Zone-2	Participant	
11	Mr. Mohammed Fakhruil Islam	Bangladesh	National Board of Revenue	Participant	
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25	Mr. Tulsi Ram Marasini	Nepal	Ministry of Federal Affairs & Local Govt, Municipal Management Section	Participant	
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51	Mr. Ronny A.K.	Indonesia	DG Tax, Ministry of Finance	Participant	
52	Mr. Tonny Ardianto	Indonesia	Fiscal Policy Agency, Ministry of Finance	Participant	
53	Ms. Hanifah	Indonesia	DG of Treasury, Ministry of Finance	Participant	
54	Mr. Sulaimansyah	Indonesia	DG of Treasury, Ministry of Finance	Participant	
55	Mr. Rindi Andhika Jafri	Indonesia	DG of Debt Management, Ministry of Finance	Participant	
56	Mr. Febridony M. Gultom	Indonesia	DG of Debt Management, Ministry of Finance	Participant	
57	Mr. Syamsu Syakbani	Indonesia	Financial Education and Training Agency, Ministry of Finance	Participant	
58	Mr. Budi Antoro	Indonesia	Director of Local Revenue and Investment, Ministry of Home Affairs	Participant	
59	Mr. Arsan Latif	Indonesia	Ministry of Home Affairs	Participant	
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70	Mr. Januar	Indonesia	Local Government of Batam City	Participant
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96	Ms. Ida Ayu Indira		World Bank	Participant
97	Ms. Nandya Yuwono		World Bank	Participant
98	Mr. Rabin Hattari		Asian Development Bank	Participant rhattari@adb.org
99	Ms. Deeny Simanjuntak		Asian Development Bank	Participant

Annex 3 List of Organizing Committee

No.	Name	Institutions	Status
1	Adijanto	MoF – Director of Subnational Taxes and Charges, DG Fiscal Balance	Chairman
2	Heru Subiyantoro	MoF – Secretary to the DG Fiscal Balance	Vice Chairman
3	Anwar Syahdat	MoF – Subdirector of Subnational Taxes and Charges Synchronization	Coordinator
4	Erny Murniasih	MoF – DG Fiscal Balance	Vice Coordinator
5	Anang Adik Rustandi	MoF – DG Fiscal Balance	Speech Coordinator
6	Rayi Renggani	G I Z	Invitation Handling
7	Denada Stotle Ishmi Rayi Renggani Paulita Septarini	G I Z G I Z G I Z	Contact Person Handling
8	Bhavanti Yuniawan Anik Snady Sukma Lestari Paulita Septagrini	AusAid AusAid MoF – DG Fiscal Balance G I Z	Ticketing and Hotel
9	Bonatua Mangaraja Prasetyo Wibowo	MoF – DG Fiscal Balance M oF – DG Fiscal Balance	Logistic and Equipment
10	Faisal Riva Setiara	MoF – Secretariate General MoF – DG Fiscal Balance	Press Handling
11	Teddy Rahmat Paulita Septarini Dyan Adhitya Kharismaningtyas Rahayu	MoF – DG Fiscal Balance G I Z MoF – DG Fiscal Balance MoF – DG Fiscal Balance	Transporation

12	Dian Putra Nathalia MS Denny Kurniawan Kurnia Ricka Yunita Prasetya Adrian Kusuma	MoF – DG Fiscal Balance G I Z MoF – DG Fiscal Balance MoF – DG Fiscal Balance MoF – DG Fiscal Balance MoF – DG Fiscal Balance	Protocol and Liasion Officer
13	Nyimas Herleni Haris Dwi Faisal	MoF – DG Fiscal Balance MoF – DG Fiscal Balance	Event Coordinator
14	Ayu Trisnaningtyas Perasanta S Nur Khalimah	MoF – DG Fiscal Balance MoF – DG Fiscal Balance MoF – DG Fiscal Balance	Reception Coordinator
15	Heri Sudarmantor	MoF – DG Fiscal Balance	Breakout session Coordinator
16	Hendra Gunawan Yudha Prasetyo	MoF – DG Fiscal Balance	Infocus Handling
17	Ananto Prasetyo Aji Prasetyo	MoF – DG Fiscal Balance MoF – DG Fiscal Balance	Documentation
18	Budi Sitepu	G I Z	Report Writing Coordinator



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MINISTRY OF FINANCE OF THE REPUBLIC OF INDONESIA
DIRECTORATE GENERAL OF FISCAL BALANCE