

Report Part Title: South Africa

Report Title: Land Value Taxation:

Report Subtitle: A Case Study Approach

Report Author(s): William J. McCluskey and Riel C.D. Franzsen

Lincoln Institute of Land Policy (2001)

Stable URL: <http://www.jstor.com/stable/resrep18161.6>

JSTOR is a not-for-profit service that helps scholars, researchers, and students discover, use, and build upon a wide range of content in a trusted digital archive. We use information technology and tools to increase productivity and facilitate new forms of scholarship. For more information about JSTOR, please contact support@jstor.org.

Your use of the JSTOR archive indicates your acceptance of the Terms & Conditions of Use, available at <https://about.jstor.org/terms>



Lincoln Institute of Land Policy is collaborating with JSTOR to digitize, preserve and extend access to this content.

JSTOR

PART II: The Land Value Tax Systems in the Five Countries

In this part an overview of the property tax system(s) within each of the five countries is given, with specific emphasis on land-value tax systems. The applicable system(s) is (are) then evaluated against the following criteria (Kelly, 1998):

- *Coverage ratio*, i.e. the amount of taxable land actually captured in the fiscal cadastre, divided by the total taxable land in the taxing jurisdiction (measuring the completeness and accuracy of the property information in the valuation roll);
- *Assessment (valuation) ratio*, i.e. the value on the valuation roll divided by the real market value of the properties on the valuation roll (measuring the accuracy of the overall valuation level);
- *Tax rate ratio*, i.e. the average tax rate used in the taxing jurisdiction (measuring the amount of tax per value of property);
- *Collection ratio*, i.e. the tax revenue collected over the total expected tax liability budgeted for the financial year (measuring the efficiency of the revenue collection).

Finally, some important policy and practical issues, as well as the future prospects are discussed in relation to each of the countries (or states) discussed.

South Africa

Origin and Historic Development

South Africa is a large and diverse country. Although major constitutional, economic and social changes have taken place since the first democratic elections were held in April 1994, the country will be burdened by its apartheid and colonial legacy for generations to come.

Land-related taxes date back to 1677. Transfer duty, which is still levied today, was introduced in 1686. In its modern guise property tax (referred to as 'rates on property') has been levied since 1836 in the former British colony of the Cape of Good Hope (Franzsen, 1999). It is levied in terms of provincial legislation (dating from the pre-1994 constitutional dispensation) in each of South Africa's nine provinces. After the establishment of the Union of South Africa in 1910, the principal form of municipal rating used was based on capital improved value (Dunkley, 1997). In 1912 a Provincial Commission was set up in the Transvaal to investigate rating. The recommendation of this Commission was that rates should be levied on the site value of land. In 1916 land value taxation was introduced in the old Transvaal province, apparently to stimulate property development and to counter land speculation. The Transvaal Ordinance was to act as the model or template for much of the rest of the country. Differentiation in the levying of rates between land and buildings became possible in the former Cape of Good

Hope and Natal provinces in 1917 and 1925 respectively (*Durban Corporation and Another v Lincoln* 1940 AD 36).

Local Government Structure

Local government in South Africa has undergone dramatic changes since 1994 and is presently still in a transitional phase. From a property tax perspective it is important to draw a distinction between metropolitan and non-metropolitan areas. In metropolitan areas so-called metropolitan local councils (the primary tier of a two-tier metropolitan government structure) levy and collect 'rates on property' (i.e. property tax). In non-metropolitan areas only urban municipalities (i.e. secondary cities, towns and villages) presently levy rates on property. Rural land is not taxed.

After the December 2000 local government elections, the present 843 municipalities in South Africa will be replaced by 284 newly-demarcated municipalities. Within metropolitan areas the two-tier structure will be replaced by single metropolitan municipalities (so-called 'uni-cities' - Cape Town, Pretoria, Johannesburg, Durban, East Rand and Port Elizabeth). A two-tier structure will be retained in non-metropolitan areas. However, the secondary-tier district municipalities will be the only form of local government in sparsely-populated rural areas demarcated as 'district management areas' (Franzsen and McCluskey, 2000). Within each district municipality will be one or more 'local municipalities'. A local municipality will typically consist of one or more towns with its/their surrounding hinterland, i.e. consisting of urban and rural properties. The property tax base will therefore extend to rural properties.

Present Status of Land Value Taxation

Property tax is the most important own source of tax revenue (representing approximately 60%). With municipal income from traditional trading services (especially the provision of electricity) set to become less important, and property tax being a constitutionally guaranteed source of own revenue, the importance of property tax is on the increase. In the former Cape Province a form of rural property taxation was abolished at the end of the 1980s (when so-called regional services councils were established country-wide).

There are three property tax systems presently in South Africa. Generally municipalities are free to choose from:

- Site rating (i.e. a property tax with its base, the unimproved value of land);
- Flat rating (i.e. a property tax with its base, the capital improved value); or
- Composite rating (i.e. a property tax taxing the unimproved value of the land at one (higher) rate and the improvements at another (lower) rate).

Of the some 500 urban municipalities about one third utilise site rating (Bell and Bowman, 1998). Site rating is predominant in Gauteng, Mpumalanga, the Northern

Province and North West, flat rating in the Eastern Cape, Northern Cape and Western Cape and composite rating in the Free State. In KwaZulu-Natal both site rating and composite rating are used extensively (in comparison to flat rating)(Bell and Bowman, 1998).

Nature of the Property Tax

Table 7: Synopsis of the local government property tax legislation

Taxable object	All urban land, irrespective of zoning
Tax Base	Municipalities can generally decide on any one of 3 options: site rating (land value only); flat rating improved value); or composite rating (land and also improvements, but at separate tax rates)
Taxpayer	Owner of rateable land
Method(s) of Assessment	Land: Comparable sales, or other suitable method(s) Improvements: residual value (i.e. capital value minus site value) in most provinces
Assessment	Only registered values (in-house or outsourced); no overarching quality control 3 values for each property required (except in the Western Cape and KwaZulu-Natal)
Valuation cycles	4-5 years
Objections and Appeal Procedures	Appeal procedures vary among provinces; no legislative scope for informal dispute resolution (before a formal objection)
Tax Rates	Uniform tax rates set annually, with almost no 'direct' differentiation
Exemptions	Very few, e.g. state-owned land is rateable
Rebates	Rebates for residential properties ('indirect' differentiation) apply in most jurisdictions; Additional relief for hardship cases (e.g. low income, pensioners, etc.)
Collection	Lump some or monthly instalments (for residential properties)
Enforcement Procedures	Interest payable on arrears Clearance certificate required before any formal transfer Seizure and public sale (after 3 years)

Valuation Issues

Valuations for rating purposes can presently only be undertaken by valuers registered in terms of the Valuers' Act of 1982. Before the Local Government: Municipal Structures Act was amended in October 2000 (as an interim measure until the Local Government: Property Rates Bill is passed into law), legislation effectively ruled out the use of computer assisted mass appraisal - as a physical inspection of each individual rateable property was required under provincial legislation.

The larger metropolitan local councils (e.g. in Cape Town, Johannesburg, Durban and Pretoria) and some of the secondary cities (e.g. Port Elizabeth, East London and Potchefstroom) have their own in-house valuation departments responsible for the

preparation of general and supplementary valuation rolls. The remainder of the urban municipalities use private sector valuers to prepare their valuation rolls. Rural properties are not presently assessed.

In August 1999 there were approximately 2,000 registered valuers, associate valuers and valuers in training (Franzsen and McCluskey, 2000). Only a small percentage of these valuers actually do municipal valuations for rating purposes. Apart from the formal objection and appeal procedures, there are no legislative quality control measures in place to monitor and report on the quality of valuation rolls generally and to ensure equity and consistency in municipal valuation across the country (Franzsen and McCluskey, 2000).

In terms of the former Transvaal Local Authorities Rating Ordinance (1977), applicable in four provinces, 'improved value of land' is defined as 'the amount which such land... would have realised if sold on the date of valuation in the open market by a willing seller to a willing buyer'. The 'site value of land' is arrived at in a similar manner, 'but on the assumption that the improvements, if any, had not been made'. The value of improvements is the residual value, i.e. what remains when the site value is deducted from the improved value.

In most provinces the valuation roll has to reflect all three values (i.e. site, improvements and improved value), irrespective of the value(s) used as the tax base.

Overall Performance (Coverage, Assessment, Tax and Collection Ratios)

Coverage ratio: Where property tax is levied, the coverage ratio is generally excellent. However, presently only urban land is rated. Some urban municipalities are still struggling with the extension of the property tax to black townships.

Assessment ratio: Only a few municipalities are not keeping to the statutory valuation cycles. Cape Town, for example, is still using the 1979 valuation roll. The accuracy and quality of valuation rolls are not at present independently monitored and evaluated.

Tax ratio: Tax rates are set annually by the municipalities, and may vary dramatically (depending on the base utilised, the expenditure needs and the date of the last revaluation). No research to date has been done on the range of effective tax rates between municipalities. It is generally accepted, however, that tax rates could still be increased in some jurisdictions.

Collection ratio: On average collection levels are high. However, as part of the legacy of the racially segregated municipal dispensation operative during the apartheid era, it may vary substantially within some jurisdictions. In certain former black townships, collection levels are extremely low (less than 40%). Improper billing, lack of administrative capacity, a persistent culture of non-payment (used as an effective political tool between 1986 and 1994), a lack of services, a lack in political will to

enforce, and the inability to pay, are just some of the reasons given for low collection levels.

Revenue and Non-Revenue Policy Issues

The importance of property tax as a revenue source for the four largest metropolitan local government areas is illustrated in the Table 8.

Table 8: Importance of property tax as a revenue source for metropolitan local government (in millions of Rand)

	Property tax	RSC levies	Income from bulk services	Grants and subsidies	Other	Total
Johannesburg	1,539	645	3,959	430	353	6,926
Cape Town	1,258	299	2,592	157	1,264	5,570
Durban	1,013	247	2,493	128	1,246	5,127
Pretoria	906	266	2,978	257	474	4,881

Source: Budget Review, 1999

It is debatable whether the present number of registered valuers in South Africa will be able to cope with the extension of the tax base to rural land, the demarcation of new municipal boundaries and the resultant need for new valuation rolls, and the use of new valuation techniques (e.g. CAMA) and methodologies (Marten, 1999; Franzsen and McCluskey, 2000). The Property Rates Bill clearly states that only persons registered as valuers in terms of South African legislation may prepare municipal valuation rolls.

The Future of Land Value Taxation in South Africa

Government seems ambivalent as far as the preferred tax base is concerned. Although the current wording of clause 5 of the Property Rates Bill suggests that capital improved value is the preferred choice, the Bill still provides for the retention of the current three tax bases (as well as local government choice in this regard). Various interest groups, amongst these the South African Council of Valuers, are in favour of taxing improvements. It is argued that a system, which also taxes improvements, relates better to a taxpayer's ability to pay, and is perceived to be more equitable.

The Bill (clause 33(1)(b)) presently states that:

‘the site value of property must be determined as an amount equal to what the property would have realised if sold on the date of valuation in the open market by a willing seller to a willing buyer, but on the assumption that:

- (i) there are no improvements on the property; and

- (ii) only the existing improvements may be erected on the property.’

This implies that the principle of ‘highest and best use’ is not embraced in the context of site value. What is being assessed is current use. Should it be enacted without amendment, this limitation of the tax base will probably play a significant role in a municipal council’s decision regarding a proper tax base. It must therefore be concluded that the future of site rating is not absolutely secure. However, the Bill is still to be debated in Parliament and discussed at public hearings before the Portfolio Committee on Local Government.

Kenya

Origin and Historic Development

Kenya’s population is 21 million people of which approximately three million live in the capital city, Nairobi. Kenya has a three-level system of government (central, provincial and local), although the eight provinces have very few powers and functions. Like many other developing countries, Kenya has a highly centralised economy (Omamo, 1995).

The property tax (rating) system in Kenya was introduced early in the 20th century. It spread from South Africa to Rhodesia and from there to the three British East African colonies of Kenya, Uganda and Tanganyika (now Tanzania). Mombasa (in 1900) and Nairobi (in 1901) introduced a rating system based on annual rental value (Ayiecho, 1996; Konyimbih, 1995; Syagga, 1994). In 1908 all townships in Kenya were empowered to introduce a rating system. However, annual rental value was found to be inadequate and inappropriate and replaced (in 1908) by flat rating. A lack of rental evidence and vast tracts of undeveloped land necessitated a change. The English system was ‘unsuitable for introduction in the new growing townships’ and therefore, in the early 1920s, site rating was introduced - following the example of Australia and New Zealand (Syagga and Olima, 1996). The early Kenyan legislation was based on the 1916 rating ordinance of the former Transvaal province of South Africa (Olima, 1999). In 1920 unimproved site value (USV) was recommended and subsequently introduced (Konyimbih, 1995).

In 1921 it was decided to use unimproved site rating in Nairobi (Rating of Unimproved Site Value Ordinance 1921). This Ordinance became operative in 1923 when the first valuation roll for Nairobi was prepared. The Ordinance was repealed in 1956 with the passing of the Local Government (Valuation and Rating) Ordinance, whose aim was to establish a uniform rating system for all municipalities established under the Municipalities’ Ordinance of 1955 (Ayiecho, 1996). The 1956 ordinance set out the basic procedures for a site value rating system and eventually resulted in the promulgation of the Valuation for Rating Act 1956 (Cap 266) and the Rating Act 1963 (Cap 267). In 1956 a single rating law was promulgated for the whole country. Unimproved site value was introduced for the following reasons (Gachuru and Olima, 1998):