

**Property Taxation in a Global Economy:
Is a Capital Gains Tax on Real Property a Good Idea?**

Sally Wallace

© 2007 Lincoln Institute of Land Policy

**Lincoln Institute of Land Policy
Working Paper**

This paper was prepared for the conference, “Toward a 2015 Vision of Land – A Celebration of ICLPST’s 100 Regular Sessions,” held October 24-25, 2007, at the International Center for Land Policy Studies and Training in Taiwan. This paper will be included in a book of conference proceedings to be published by the Lincoln Institute in 2008.

The findings and conclusions of this paper are not subject to detailed review and do not necessarily reflect the official views and policies of the Lincoln Institute of Land Policy.

Please do not photocopy without permission of the Institute. Contact the Institute directly with all questions or requests for permission. (help@lincolninst.edu)

Lincoln Institute Product Code: WP07SW1

Abstract

The concept of globalization has become an increasing concern of public finance scholars around the globe. As capital becomes more mobile and barriers to the entry and exit of capital fall, we expect capital to migrate among sectors of the economy and among countries seeking out the highest return. Competition for capital may be affecting tax policies from corporate income taxes to property taxes. Some believe that ultimately, tax policy is in a race to the bottom, where systems will become more and more homogenous among countries.

The property tax is viewed as a “good” tax for local governments around the world. Many local governments are given the right to tax property, but the level of usage, tax bases, and nuisances of the property tax systems around the world vary greatly. With few exceptions, however, the tax is not heavily used. In the context of the globalization debate, the property tax is a bit unique in terms of its role. On one hand, as a benefits-tax, the tax should only be partially affected by the pressures of worldwide competition for capital. The new view of the property tax holds that the tax is a distortionary tax on capital and that differentials in property tax can affect the migration of capital among jurisdictions. In that world, with the increased ease of capital migration due to globalization, the property tax might be viewed as an endangered species.

In this paper, we take a look at an alternative tax on real property—a tax on capital gains. We introduce a linkage between globalization and the growth in the value of real property, and then focus on whether or not a tax on capital gains is appropriate for many countries. We conclude that there are some merits to such a tax, but the administrative complexities may make it beyond the reach of some developing nations.

About the Author

Sally Wallace
Professor of Economics
Andrew Young School of Policy Studies
Georgia State University
Atlanta, GA

Contact information:

swallace@gsu.edu
404-651-1912
404-651-0416 (fax)
14 Marietta St., NW
AYSPS, Room 434
Atlanta, GA 30303-3992

Table of Contents

Introduction	1
Globalization and Property Values	2
Capital Gains Tax on Real Property	6
Arguments in Favor	7
Arguments Against	9
Do Capital Gains Taxes on Real Property Exist?	10
Design and Administrative Issues: Can They Be Overcome?	15
Conclusions	16
References	17

Property Taxation in a Global Economy: Is a Capital Gains Tax on Real Property a Good Idea?

Introduction

The concept of globalization has become an increasing concern of public finance scholars around the globe. As capital becomes more mobile and barriers to the entry and exit of capital fall, we expect capital to migrate among sectors of the economy and among countries seeking out the highest rate of return. Competition for capital may therefore be affecting tax policies from corporate income taxes to property taxes. Some believe that ultimately, tax policy is in a race to the bottom, where systems will become more and more homogenous among countries—developed and developing alike.

There continues to be much debate about the globalization of tax bases. Aizenman and Jinjark test the hypothesis that globalization forces countries to move from easy to tax bases (trade taxes, seigniorage) to bases that are more difficult to tax (VAT and income tax for example). They find evidence of this type of change as countries increased their share of hard to tax bases from the early 1980s to the late 1990s. Other studies have not found as much evidence. For example, Alm et al. (2002) analyzed the composition of taxes in the U.S. under the hypothesis that mobile taxes such as state and local taxes on capital would decline. They could not find conclusive evidence of this trend.

The relative mix of taxes among countries and differences in tax administration may be reasons for the lack of consensus regarding the empirical impact of globalization on taxes. Developed countries tend to have better funded tax administrations, which may make them more able to adapt to changes in the tax base due to globalization. Countries with a large use of trade taxes may be particularly vulnerable to the impact of globalization. The type of central-state-local revenue assignment used in various countries may also increase the impact of globalization. We might think that in cases of significant decentralization of revenue authority, there would be more pressure to integrate tax bases due to competitive pressures associated with globalization.

The property tax is a bit unique in terms of its role in the globalization debate. On one hand, as a benefits-tax, the tax should only be partially affected by the pressures of worldwide competition for capital. In a world where individuals are mobile and can vote with their feet, the property tax is akin to a lump sum tax and is non-distortionary in terms of its impact on the allocation of capital. However, there is another side to the story. The new view of the property tax holds that the tax is a distortionary tax on capital and that differentials in the effective property tax rate can affect the migration of capital among jurisdictions. In that world, with the increased ease of capital migration due to globalization, the property tax might be viewed as an endangered species.¹

¹ There are many good discussions of the benefits view versus capital tax view of the property tax, but these are not presented in detail here. See for example, Zodrow (2001) and Fischel (2001).

The property tax has a number of dimensions. In this paper, we focus on the growth in the value of real property—itsself a product of globalization, and the possibility of integrating a tax on capital gains on real property into the tax mix. While some countries tax capital gains in real property, few do it well, and others rely on other taxes to do the job of a capital gains tax. We suggest that these are not good imposters and there may be room to integrate a real capital gains tax in some developing countries.

In the next section, we make the case for just beginning this story of considering a tax on the increased value of real property. If the potential tax base of a capital gains tax has grown, now may be the time to consider a capital gains tax on real property. In the third section, we ask the question “should we have a capital gains tax on real property?” The fourth section summarizes the taxes that are currently used that effectively tax capital gains on real property. Finally, we take a look how a tax on real property might be imposed by presenting some issues related to design and actual implementation. There are many important and difficult issues surrounding the taxation of real property and as such, this paper touches the surface of a number of them, but more work is to be done.

Globalization and Real Property Values

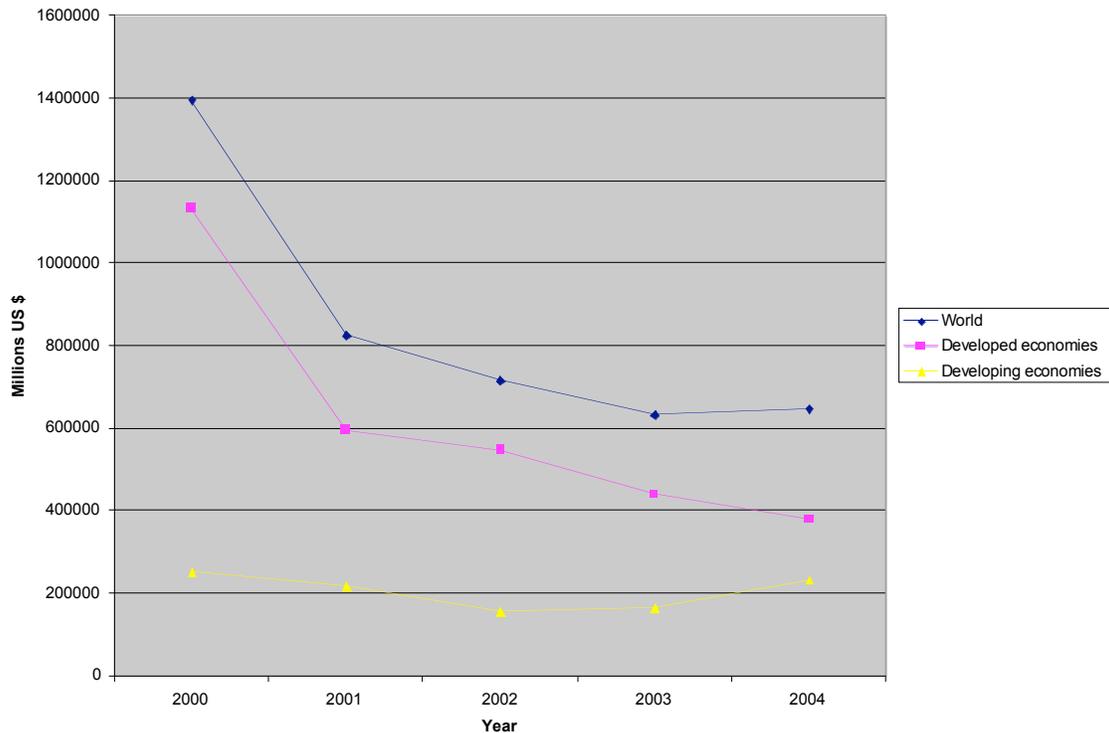
Globalization continues to be difficult to define, but easy to point out. Increased access to international markets, outsourcing of work, internet communication and sales, and more are evidence of globalization. The economics of globalization and its impact on property is, in theory, fairly clear cut. Mobile capital will seek the highest rate of return. As the barriers to mobility fall (for example, financial markets open up, transportation becomes cheaper, tariffs and other taxes fall), capital moves more easily among countries. This mobility of capital has been hailed as one the driving factors in the potential “race to the bottom” of taxes worldwide since, under certain conditions, taxes will lower the rate of return to capital.² Countries with high taxes on capital will be at a competitive disadvantage vis-à-vis other countries, so there is pressure to bring tax rates on mobile capital down to match those of other countries.

Increased capital flows can increase productivity, leading to higher levels of economic growth. Increased investment, expanding businesses, and increased employment will increase the demand for real property thereby putting pressure on the prices of land and structure. So, we might expect that the march of globalization would yield significant gains in property values.

Some evidence on the progress of globalization and investment can be found by studying the flow of foreign direct investment around the world. The United Nations Conference on Trade and Development (UNCTAD, 2006) produces FDI flows for most countries in the world. In Figure 1, we see that in the post-2000 boom-to-bust, FDI dropped substantially between 2000 and 2001. By 2004, we see some recovery of investment—with most of the growth occurring in the developing countries. As a frame of reference, in 2004, FDI in-flows worldwide were over 3 times what they were in 1990. In developing economies, they were over 6 times as great at 1990 levels.

² See, for example, Alm, Chen, and Wallace (2002) and Neumann et. al. (2002).

Figure 1: FDI Inflows, 2000-2004



Source: UNCTAD database, 2006.

Has the flow of capital had an impact on the price of real property?³ There is much anecdotal evidence that property values have increased in many parts of the world. It is more difficult to find comparable empirical evidence regarding the value of real property. Gravelle (1994) reports that in the U.S. net gains on personal residences accounted for 25.3 percent of all capital gains in the early 1980s, putting the total gain on residences at approximately \$27 billion. That amount has increased over time and by 1990, the total level of capital gains was \$145 billion. If housing retained its 25.3 percent share, then in a matter of eight years, the level of capital gains in real property increased more than 30 percent.

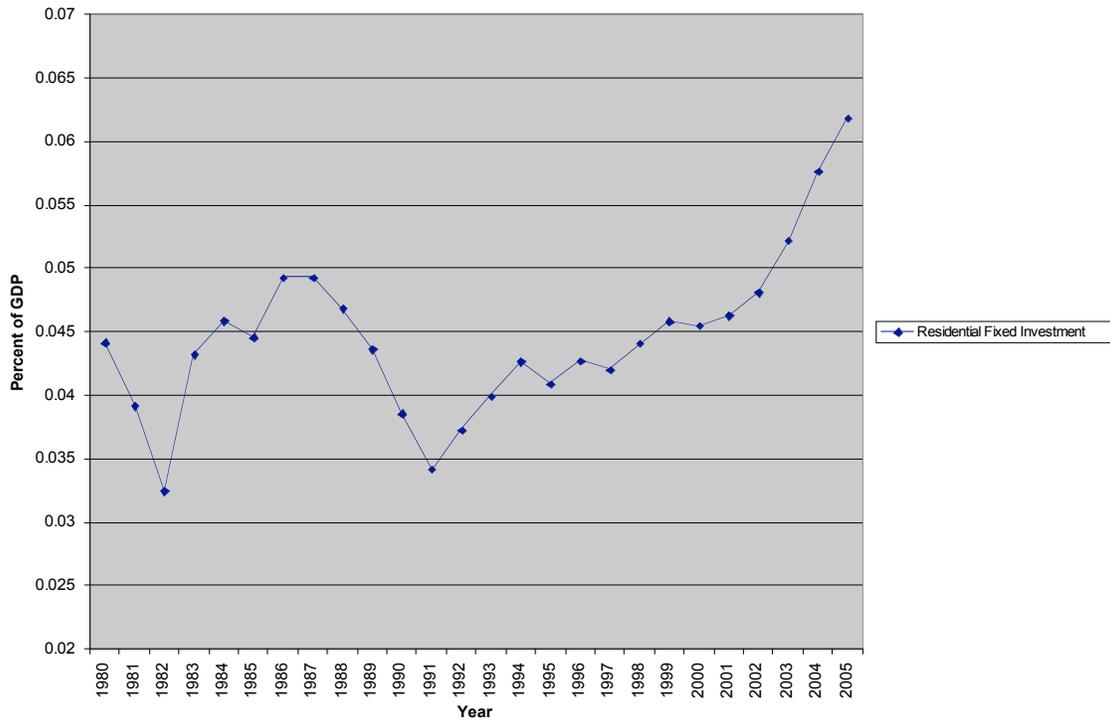
In 2004-05 there were concerns over the potential bursting of the “housing bubbles” in the U.S. and the U.K., providing some evidence that there are significant gains on real property.⁴ The U.N. (2005) reports that rising housing prices in developing economies may lead to risky housing price bubbles in those countries as well.

³ It would be interesting to test this proposition empirically by estimating whether or not urbanization, for example, is affected by flows of foreign direct investment. A positive correlation between FDI and urbanization would suggest that increased FDI would increase the demand for housing and land. In turn, there may also be a longer-term impact whereby increases in the value of real property reduced the growth of further FDI. If that were the case, property values may naturally stabilize or even fall after a big run up in gains fueled by FDI. This analysis is not done here.

⁴ Many popular outlets have published “bubble” stories. Businessweek (June 2005) reported that the chief economists for Freddie Mac found rational reasoning (job and income growth) behind the double digit

In the U.S., we can identify more specific data to analyze the trend in gains to real property. We use the ratio of residential fixed investment as a share of GDP and the stock of residential property as a share of GDP as rough measures of evidence of capital gains. Figures 2 and 3 demonstrate the growth in both of these indicators. In the case of Figure 2, we see that as a share of GDP, residential fixed investment has grown quite steadily since 1991. The values of capital stock of all residential property and owner occupied property as a share of GDP (Figure 3) have also shown consistent growth since 1991-92. Neither of these ratios is a perfect measure of the growth of net capital gains in real property, but they provide some evidence of growth in capital gains on real property.⁵

Figure 2: Residential Fixed Investment as a share of GDP, US (1980-2005)

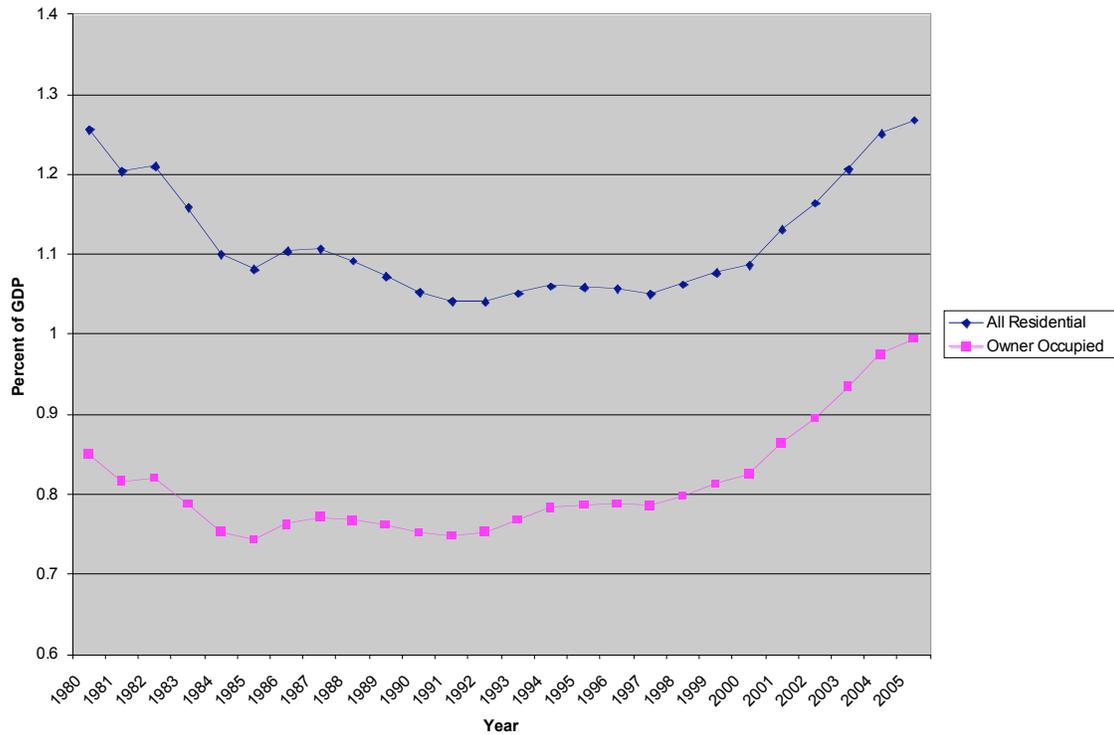


Source: U.S. Bureau of Economic Analysis (2006).

growth in home values in some large US markets. The BBC (May 2006) reports strong gains for housing in the U.K. over the last several years.

⁵ The national income accounts do not include capital gains because it is not the addition of a net investment in the economy. In the U.S. the near elimination of capital gains on owner occupied housing reduces the usefulness of the IRS data on capital gains on real property.

Figure 3: Private Residential Fixed Assets (Current Cost of Net Stock) as a share of GDP, US 1980-2005



Source: U.S. Bureau of Economic Analysis, 2006.

At the very least, these data provide some circumstantial evidence on the globalization-FDI-property value link. A structural model of globalization, investment, and property values could be developed and tested if data were available. However, the pattern of strong FDI (with expected downturns during recessionary periods) and evidence of housing price increases provide some support for the intuitive notion that globalization, increased flows of investment, and housing prices are related.

Box 1

Globalization in Ghana

There are many specific examples of globalization around the world. In Ghana, recent interviews with industry officials provide some insight into the impact of globalization in a developing economy. In the cigarette industry, the only domestic producer has recently decided to close its production line in the country and become an importer of cigarettes. Economics were the driving reason—the marginal cost of production including transportation costs were significantly lower in other countries in Africa.

Another example comes in the case of a local alcohol producer. Facing very large costs of importing new machinery to replace antiquated capital, the company had been searching for alternatives in Europe and felt the costs were too high. They instead looked to China, which they claim has become an even easier exporter, and are in the process of finalizing their deal to bring the machinery in from China.

Capital Gains Tax on Real Property

As a tax on real property, a capital gains tax on land and structures is related in some ways to “traditional” property taxes. The property tax itself, despite its merits as a local tax, is not heavily used in many developing and transition countries. Table 1 demonstrates the recent trends in property tax relative to GDP. Our data for developing countries is too sparse in 2002-2004 to provide a meaningful comparison, so we compare 2000 and 2001 among countries. In OECD countries, the average is just slightly over 2 percent, while in developing and transition countries, it is much lower and averages around 0.59 percent of GDP. Earlier estimates from Bahl (2001) suggest that these ratios have increased only gradually since the 1980s for a variety of reasons including valuation, pressure to keep rates low, collection, and compliance.

Table 1
Property Tax as a Percent of GDP

	2000	2001	2002	2003	2004
OECD					
Number of obs.	18	18	17	16	12
AVERAGE	2.17	2.06	2.10	2.01	2.16
Developing Countries					
Number of obs.	40	30	4	2	1
AVERAGE	0.57	0.54	0.62	1.14	1.63
Transition Countries					
Number of obs.	20	18	11	14	10
AVERAGE	0.65	0.64	0.79	0.77	0.79

Source: IMF, Government Finance Statistics, 2006, also reported in Bahl and Martinez-Vazquez (2006).

A capital gains tax on real property could increase the effective rate of taxation on property in developed and developing and transition countries. A real capital gains tax would tax the change in *real* value of the property. The tax base is the sales price minus the real purchase price minus the real value of improvements.⁶ For our analysis in this paper, we focus on taxing realized capital gains. While a tax on unrealized gains may be preferable from a Haig-Simons perspective, the administration of an annual tax on unrealized gains could be unwieldy.

Arguments in Favor

There are numerous arguments in support of a capital gains tax on real property and they focus on equity and efficiency issues. First is the issue that many countries tax a variety of assets, but relatively few tax real capital gains on real property. There are situations as in the case of the U.S. where nominal gain on corporate stocks is taxed, but the gain to residential property is effectively exempt.⁷ This difference in treatment of assets may redirect investment in ways that are not anticipated—potentially lowering the price of real assets relative to other capital assets and fueling increased prices in housing. This may not be as much an issue in developing countries as it may be in developed countries. Or—it may be an issue for urban areas in developing countries but not so much an issue in rural areas.

⁶ To be consistent, real losses on property should be deductible under an integrated income tax system. For purposes of this paper, we can implicitly assume the symmetric treatment of gains and losses.

⁷ In the U.S., an individual can exempt up to \$250,000 of gains and a married couple can exempt up to \$500,000 in capital gains on the sale of their primary residence.

Secondly, the issue of vertical equity is an important consideration. The distribution of wealth in countries around the world continues to show patterns of heavy concentration in the upper income deciles in all countries. The World Bank (2005) reports that the level of poverty and distribution of income or consumption has shown improvement in some countries, but it has changed very little, or even gotten worse, in other countries (countries of sub-Saharan Africa having some of the most disparate distributions). While data on the distribution of capital assets are not readily available for most countries, we expect that the ownership of real assets is concentrated in higher income groups. On grounds of vertical equity, a capital gains tax on real property could therefore rate quite high.

Third, the revenue from a real capital gains tax could be significant. Of course, this is a big “could.” Tax administration would play a critical role in instituting a tax on capital gains. Lax enforcement of taxes in many countries calls into question the ability of a tax on capital gains to yield significant revenue.

How much revenue is possible? In the U.S., for example, the estimate of the tax expenditure associated with the exclusion of capital gains on housing is upwards of \$40 billion. This means that, based on available data, if residential properties were subject to the capital gains tax, receipts would be \$40 billion higher. In Jamaica, which has no tax on capital gains, it was estimated that a tax on real property and financial assets could raise as much as \$1 billion (Wallace and Alm, 2004). Bahl (2004) estimates that the real property portion of a capital gains tax in Jamaica could be \$200 million.

Increased property values may be viewed as a monetary gain that property owners get from general government expenditures on infrastructure and other general public goods. From this perspective, it is only fair that government should receive a share of this benefit via a capital gains tax (Bahl, 2004).

The imposition of a property tax and a capital gains tax does not mean that real assets are the subject of “double taxation.” Under the benefits view of tax incidence, the property tax is a payment for local government services. If the tax is fully capitalized, then property values decrease to the extent of the tax. If benefits are also capitalized, property values may increase due to the value of the benefits. The property tax/benefits impact could net out so that there would be no change in the value of property (or even a reduction in the value of property if tax capitalization were more than capitalization of the benefits). A capital gains tax would tax real *appreciation* in the value of real property—which comes due to increased demand for housing, better living conditions in a particular area to externalities associated with the specific benefits, etc. If there were no appreciation in assets, there would be no capital gains tax to levy.

From the new view, or capital tax view, differentials in property tax rates leads to migration of capital to lower taxed jurisdictions. Globalization may enhance this movement. For jurisdictions with higher than average property taxes, the gross price of property increases, but the net price in the entire market (province, state, country,

worldwide market) would fall. A capital gains tax in this world would be based on a higher gross price in the higher taxed jurisdiction. In all other jurisdictions, once again, only if there is an appreciation in the value of property, would a capital gains tax be due. The potential argument of double taxation becomes even less of an issue if a national capital gains tax were proposed (although there is room for international mobility of capital) and/or if the gain to the value of land alone were the subject of taxation.

A tax on real capital gains could discourage speculation by reducing the after tax rate of return on real property. This could have the effect of smoothing the returns to real property and reducing the chance for bubble phenomena. However, if the capital gains tax allowed full loss offset in the case of real losses on property, the government would share both the risk and the yield of the assets, which may in fact increase individuals to take on a slightly riskier set of real estate investments.

Finally, there is a possible self-policing aspect of a capital gains tax that could be attractive to the tax administrations of developing countries. Currently, in the case of most property transfer tax systems, both seller and buyer have an incentive to underreport the value of the transaction. In the case of a capital gains tax, the seller might want to underreport the value of the sale (to reduce his capital gain) but the buyer wants her basis to be as high as possible—so she would want the sale reported at the highest possible price (barring any other taxes or fees). Self-interest of both parties is likely to push the parties toward reporting a transaction value that is more in line with the actual value of the transaction than is currently the practice in many countries.

Arguments Against

Just as there are proponents of taxing real gains to real property, there are solid arguments against such taxation. The lock-in effect of capital gains taxation is one problem that has received much attention in the literature, which covers real property as well as other capital assets like corporate stocks. The lock-in effect in the case of real property means that imposition of a capital gains tax (or an increase in the tax rate) increases the cost of selling a house. If, in the absence of the tax, an individual would have sold the house and moved, then the lock-in effect reduces utility. The economy as a whole suffers an efficiency loss as capital may be misallocated and thus not be put into its most productive use. This is similar to the lock-in effect attributed to acquisition-value property taxes where houses are revalued for property tax purposes only when sold (O’Sullivan, et. al., 1995).⁸

Administration of a capital gains tax is difficult. To be true to the base of “real capital gains” the administration must have documented evidence of the sales/purchase price as well as the timing and cost of improvements. This type of documentation is standard in some countries, but not in most developing nations. Indexation is less of a problem. Although not perfect, an annual inflation adjustment could be used that is based on the

⁸ The lock-in effect for capital assets such as stocks has been very heavily researched, without a definitive answer regarding the impact of capital gains taxes on the long run lock-in effect. See for example, Gravelle (1994), Burman and Randolph (1994), and Auerbach (1989).

consumer price index over a calendar year period. Another administrative issue is the treatment of inter-family transactions. There is a tendency to allow these types of transfers tax-free, but the potential for tax evasion through this avenue is significant. For example, an unrelated individual may want to buy a property, but instead, bankrolls another person to purchase the property from a family member. The financier then could rent back the property for no cost. This is risky for the financier, but in certain markets, escalating rental prices could make the risk worth it.

A capital gains tax, even if it is a substitute for another tax, is likely to be politically unpopular. A capital gains tax would be very transparent as it is a “big ticket” item when real property is sold.

In addition, capital gains tax revenue flows can be erratic, although most empirical evidence on the stability of capital gains covers the capital gains taxes on financial assets (Sjoquist and Wallace, 2004). Housing values have grown in many countries over the last decade, but there are areas that have not experienced growth and in the case of developed nations, documented evidence of real declines in the value of real property.

There are also arguments that preferential treatment for capital (in the form of lower or no tax on capital gains) is needed to encourage investment and entrepreneurship and in the case of housing, to increase the ability of individuals to own their own homes. Higher capital gains taxes increase the price of home ownership and may therefore reduce the ability of potential homeowners to purchase a home.

To summarize, there are good and bad points to a capital gains tax. A proponent of a tax on real capital gains would highlight that such a tax could raise significant amounts of revenue, that the tax reduces disparities among treatment of capital assets, that the tax is a way to enhance vertical equity, and that the tax could be self-policing thus reducing evasion. Opponents of such a tax might highlight that it could be difficult to administer especially for local governments, the tax could create a lock-in affect and reduce the mobility of individuals and companies, and that the tax might be too burdensome. Both sides would have valid arguments, as is true in most of our tax policy debates. In the next section, we turn to reviewing capital gains-like taxes that already exist and rate them and a tax on real capital gains on a number of economic and administrative issues.

Do Capital Gains Taxes on Real Property Exist?

There are taxes that may look like capital gains taxes but fall short of taxing capital gains on real property for a variety of reasons. There are other taxes that may in fact look quite like a capital gains tax. These include stamp duties, property transfer taxes, gift taxes, betterment levies, and land value increment taxes. The value added tax might also be considered a capital gains-type tax.⁹ And, there are some examples of real capital gains taxes. Recall that we define a capital gains tax as one that taxes real returns to real

⁹ The VAT typically taxes the value of the transaction so the VAT is not a tax on real capital gains in most countries.

property. We might evaluate potential capital gains tax “imposters” relative to a capital gains tax by considering the following issues:

- Does it tax real capital gains?
- Are improvements accounted for?
- Does it raise significant revenue?
- What is the distributional impact?
- Does it induce “bad” behavior, e.g. evasion, lock-in effects?
- Is the administration clear or arbitrary?

We first take a look at the types of capital gains (or other) taxes used in a small sample of countries. The experiences of various countries are summarized by the information in Table 2 and then, in Table 3, we evaluate these examples according to the criteria listed above. The purpose of this exercise is to evaluate whether there are many true capital gains taxes on real property out there. Of course, the countries listed in Tables 2 and 3 are only illustrative. More detailed summaries of property taxes, other taxes on property, and capital gains taxes are reported by Bird and Slack (2004), Youngman and Malme (1994), Almy (2001), and Franzsen and McCluskey (2005).

Jamaica imposes a property transfer tax and a stamp duty tax. Bahl (2004) evaluates both taxes and finds them to not be convincing capital gains-like taxes. The stamp duty is charged on transactions and a few types of sales (airline tickets, for example). The property transfer tax is levied on the transaction value of real property. As noted by Bahl (2004), there is an incentive to underreport the value of transactions in Jamaica’s property transfer tax system. Little effort is expended in the administration of these taxes, so the undervaluation problem has been an issue for much of their history.

The property transfer tax in Jamaica is sometimes referred to a substitute for a capital gains tax, but it is not a good substitute. The base of the property transfer tax is not the real capital gain. There is no inflation adjustment, no accounting for original sales price or improvements, and the reported transactions value is universally below the actual sales price. The tax does not reach the realized value of real property in Jamaica.

There are numerous other examples of capital gains type taxes levied on real property. Youngman and Malme (1994) summarize the state of other taxes on immovable property in the early 1990s. At that time, of the 14 surveyed countries for which information is reported (largely OECD countries with the addition of South Korea, Chile, Israel, and Indonesia), all but one report some type of tax on the gain to immovable property. Most often the tax on capital gains is a combination of transfer tax and capital gains tax.

Franzsen and McCluskey (2005) provide a comprehensive list of countries with property transfer taxes and capital gains taxes. Almy (2001) also surveys a number of countries and reports “other property-related taxes” for transition countries. These are mostly transfer, gift and inheritance types of taxes with the exception of Estonia’s land use fees.

There are nuances about the capital gains taxes and other property related taxes that are reported in the studies of Youngman and Malme (1994), Franzsen and McCluskey (2005)

and Almy (2001). Looking at the detail for a handful of countries suggests that these taxes are not taxes on real capital gains nor are the property related taxes good approximations to a capital gains tax. For example, we find that in Malaysia, the capital gains tax on real property for individuals falls to 0 when assets are held for five or more years. There is in fact a sliding scale rate for all property owners where the tax rate falls as the holding period increases. This may be done as a rough adjustment for inflation (which is not explicitly accounted for in the definition of the tax base).

In Ghana, the capital gains tax base is basically on transactions and not on the increase in value of real property. In the U.K., realized capital gains on residential property are exempt. These cases are some evidence that countries that impose capital gains taxes may not be imposing what we have been calling a real capital gains tax.

Another example of incomplete capital gains taxation is the case of the Russian Federation. The tax base of the gift and transfer taxes is based on the self-reported value of the transaction and not the appreciation in the value of the asset (Rider, Martinez-Vazquez, and Wallace, 2006). It is likely that similar treatment is found in other transition countries as well. The capital gains tax in Russia exempts residential property, but transfers of real property are subject to the VAT.

Korea and Taiwan provide examples of a tax that is more like a real capital gains tax on real property. Taiwan's Land Value Increment Tax (LVIT) taxes the real return to land and makes allowances for inflation and the costs of improvements and fees ("costs" of owning land). The tax is levied using a progressive rate structure. There are some exemptions including transfers that occur as inheritances (Tsui, 1998, Ministry of Economic Affairs, 2006).

Korea's LVIT is a tax on unrealized capital gains on unimproved land held by companies and excess residential land (Lee, 2000). The definition of "idle land" lead to a means for tax evasion. Lee (2000) points out that property owners could construct cheap improvements to the land to avoid taxes. Challenges to the tax in 1995 reduced its usefulness as a tax on capital gains from real property.

This brief survey of taxes on property is summarized by the information in Table 2. Taiwan and Korea's land value increment taxes come closest to a tax on real capital gains. However, Korea's LVIT was probably one of the closest approximations to the type of capital gains tax we have raised in this paper, and Korea's tax faced stiff resistance by taxpayers.

The information in Table 3 highlights the similarities and differences between the taxes listed in Table 2 and a real capital gains tax (on real property). A capital gains tax, with a strong tax administration component, could be a significant revenue producer, as noted earlier. It could induce some "bad behavior" via the lock-in effect. Of the small sample of other taxes that are listed in Table 2 and 3, the LVIT of Taiwan and Korea come closest to the capital gains tax in terms of impacts and revenue potential—at least in theory. Korea's LVIT is a good case study in the politics of this type of tax. However, in

Korea, the tax rate on gains was 50 percent—high by most standards for any tax. An additional lesson that could be taken from Korea’s case is that the tax rate matters to the taxpayer. Introducing a new capital gains tax at a relatively low rate probably has a better chance of success than one that is enacted with a high tax rate.

Table 2
Examples of Property-Related Taxes in Select Countries

Country	Tax	Base	Rate	Other issues
Jamaica	Property transfer	Nominal transaction value	7.5 percent	Rate is coupled with a stamp duty of 5.5 percent
Taiwan	Land value increment tax	“total increment amount of land value”	Progressive rates from 20 to 40%	Adjusts for improvements and inflation
Korea	Land Value Increment Tax (1990s)	Unrealized gains	50% of excess profits	Basic value increase is exempt, not all property is taxed
Russian Federation	Estate and gift, capital gains	Self-reported nominal value of transfer	Individual income tax rate (13% flat rate)	Russia’s system of a market-based property tax is in development
U.S.	Capital gains	Nominal capital gain	Individual income tax rate	\$500,000 exemption for married filers, \$250,00 for single

Table 3
Survey of Capital Gains-Like Taxes

Country	Tax	Are Capital Gains Taxed?	Inflation Adjustment?	Revenue?	“Bad Behavior” and Economic Costs
“Ideal Case”	Capital Gains on Real Property	Yes, on land and structures	Yes	Can be significant	Self-policing (“good behavioral effect”) Lock-in possible
Jamaica	Property Transfer Stamp Duty	No	No	Small	Under declaration
Taiwan	LVIT	Yes, on land, realized	Yes	Substantial amount for subnational government	Lock-in effect Local governments must revalue the tax base regularly
Korea	LVIT	Yes, on land, unrealized	No	Small due to political pressures and definition of taxable property	Avoidance by constructing “improvements”
Russian Federation	Capital Gains tax	Residential property largely exempt	No	Small	If the tax were enforced, it could induce a lock-in effect
U.S.	Capital Gains Tax	Residential property largely exempt	No	Relatively small	The tax has become non-binding for most homeowners, so it has little impact.

Design and Administrative Issues: Can They Be Overcome?

The administration of capital gains taxes is difficult. The demands for information, reporting, record-keeping, and the like could prevent any developing nation (or developed country) from seriously considering a significant capital gains tax on real property. However, there are cases where there is a basis for implementing a real, live capital gains tax on real property. Das-Gupta (2002) reports the administrative structure of for transfer and property taxes in Uttar Pradesh, a state in India. Much effort has been put into developing a baseline value for properties. Cost-based norms are used to regularly adjust the values for buildings. These adjusted baselines can be used to compare against self-reported values. If an inflation adjustment were included, this type of valuation could be used to implement a capital gains tax on real property.

Bahl (2004, p. 53) sets out an approach to levy a land-based capital gains tax in Jamaica. The estimation of liability is carried out in six steps:

1. Land value at time of sale
2. minus land value at purchase, net of costs of improvements, adjusted for inflation over the period;
3. minus allowable exemption status;
4. equals taxable realized capital gain;
5. times tax rate;
6. equals tax due.

A method similar to that used in Uttar Pradesh could be used to estimate 1. and 2. Exemption status is specified in law (exemptions may include low valued homes, for example). The greater administrative costs and difficulties come from the inclusion of improvements.

If a capital gains tax were feasible, should a capital gains tax and property tax co-exist in our globalized world? Property taxes vary among countries due to their structure and administration. This makes it difficult to make general statements about the potential for co-existence of a capital gains tax and a property tax. However, as explained earlier, a real capital gains tax is not a double tax in the sense of a “tax on tax.” Capital gains taxes may be a better way to address vertical equity and to repay government for the general benefits of increased infrastructure and an atmosphere that promotes foreign direct investment and growth in the real estate markets. With the pressures of increased capital mobility within and among countries, a capital gains tax on all real property (even properly administered) could exacerbate capital outflows. A more reasonable alternative may be to focus on the development of a capital gains tax on land. With some work on developing a baseline that could take advantage of tax administration infrastructure of the property tax, a real capital gains tax on land may be a viable alternative in countries where it is not yet utilized.

Conclusions

Globalization is changing the structure of the worldwide economy. The easing of the flow of capital, labor, and goods among countries produces changes in the distribution of resources among countries, but also possibly within countries. In this paper, we have appealed to the notion that globalization has increased the movement of capital and that the increase in investment across the globe has produced upward pressure in the value of real property. Of course, not all countries are necessarily winners in the capital mobility game—and even within countries, urbanized areas may see large increases in real values of property while rural areas may actually witness a decline.

The growth in the value of real property may be an important tax base for developing countries. A brief survey of tax treatment of property suggests that while a number of countries report taxes on capital gains or capital gains-like taxes, the reality is that real capital gains are probably not taxed in many countries. Issues of equity (both vertical equity as well as reasonable contributions for general benefits from public goods), potential revenue generation, and the possible tie-in with property tax administration may be intriguing enough to countries to further explore a capital gains tax on real property. Since globalization makes the taxation of capital more difficult, a capital gains tax on real increases in the value of land may be a more appropriate concept to explore in more detail.

References

- Aizenman, Joshua and Yothin Jinjark (2006), "Globalization and Developing Countries—A Shrinking Tax Base?" National Bureau of Economic Research Working Paper 11933, Cambridge, MA.
- Alm, James, Shiyuan Chen, and Sally Wallace (2002), "Globalization and State-Local Finances," in *Proceedings of the 95th Annual National Tax Association Conference, Orlando, Florida* pp. 155-164.
- Almy, Richard (2001), "A Survey of Property Tax Systems in Europe," prepared for Department of Taxes and Customs, the Ministry of Finance, Republic of Slovenia, accessed on August 28, 2006: <http://www.agjd.com/EuropeanPropertyTaxSystems.pdf>.
- Auerbach, Alan (1989), "Capital Gains Taxation and Tax Reform," *National Tax Journal*, Vol. 42, 1-36.
- Bahl, Roy (2001), "The Property Tax in Developing Countries: Where are we in 2002?" lecture at the Lincoln Institute of Land Policy, Cambridge, MA, October 23, 2001.
- Bahl, Roy (2004), "Property Transfer Tax and Stamp Duty," International Studies Program Working Paper, Andrew Young School of Policy Studies, Georgia State University, Atlanta, GA.
- Bahl, Roy and Jorge Martinez-Vazquez (2006), "Property Taxation," prepared for the conference, Lincoln Institute of Land Policy and International Studies Program, Andrew Young School of Policy Studies, Georgia State University, Atlanta, GA, October 2006.
- Bird, Richard and Enid Slack (2002), "Land and Property Tax: A Review," *Journal of Property Tax Assessment and Administration*, 7 (3, 2002), 31-89.
- British Broadcasting Company (2006), "Will House Prices Boom Again?" BBC News, accessed on October 1, 2006: <http://news.bbc.co.uk/1/hi/business/4972220.stm>.
- Burman, Leonard and William Randolph (1994), "Measuring Permanent Responses to Capital Gains Tax Changes in Panel Data," *American Economic Review*, Vol. 84, no. 4, 794-809.
- Businessweek Online (2005), "Housing Bubble or Bunk?" accessed on September 19, 2006: http://www.businessweek.com/bwdaily/dnflash/jun2005/nf20050622_9404_db008.htm.
- DasGupta, A. (2002), "India: Uttar Pradesh Policy Notes—UP's Own Revenue System: Assessment and Reform Suggestions," The World Bank, Washington, D.C.

Franzsen, Riel C. D. and William J. McCluskey (2005), "An Exploratory Overview of Property Taxation in the Commonwealth of Nations," Lincoln Institute of Land Policy Working Paper, WP05RF1.

Globe Africa, Namibia Investment Policy, accessed on Oct. 7, 2006:
<http://www.globeafrica.com/Namibia/namibia2.htm>.

Gravelle, Jane (1994), *The Economic Effects of Taxing Capital Income*, Cambridge: MIT Press.

Grubert, Harry (1998), "Has Globalization Transformed the Behavior of Governments and Taxpayers?" *Proceedings of the Ninetieth Annual Conference on Taxation, National Tax Association*, pp. 237-239.

International Monetary Fund (2006), *Government Finance Statistics* cd-rom, Washington, D.C.

Kelly, Roy (2002), "Designing a Property Tax Reform Strategy for Sub-Saharan Africa: An Analytical Framework Applied to Kenya," *Public Budgeting and Finance*, Vol. 20, pp. 36.

Lee, Tai-Il (2000), "Republic of Korea (South Korea)," in *Land Value Taxation Around the World*, Robert V. Andelson, ed., Malden, M.A.: Blackwell Publishers.

Martinez-Vazquez, Mark Rider and Sally Wallace (2006), *Russia's Tax Reform*, draft manuscript, Andrew Young School of Policy Studies, Georgia State University, Atlanta, GA.

McCluskey, William J. and Riel C.D. Franzsen (2001), "Land Value Taxation: A Case Study Approach," Lincoln Institute of Land Policy Working Paper, WP01WM1.

National Government of Taiwan, Ministry of Economic Affairs (2006), "Real Property Taxes: Land Value Increment Tax (LVIT)," accessed on September 28, 2006:
http://investintaiwan.nat.gov.tw/en/env/guide/tax/land_value.html.

Neumann, Rebecca, Jill Holman, and James Alm (2002), "Globalization and Tax Policy," University of Wisconsin Working Paper, Madison, WI.

Office of Management and Budget (U.S.) (2006), "Analytical Perspectives," in Budget of the United States Government, Washington, D.C., accessed on September 15, 2006:
<http://www.whitehouse.gov/omb/budget/fy2006/pdf/spec.pdf#search=%22tax%20expenditures%20in%20US%20budget%22>.

O'Sullivan, Arthur, Terri A. Sexton, and Steven M. Sheffrin (1995), *Property Taxes and Tax Revolts: the Legacy of Proposition 13*, Cambridge, U.K.: Cambridge University Press.

Sjoquist, David and Sally Wallace (2003), "Capital Gains: Its Recent, Varied, and Growing (?) Impact On State Revenues" for the conference, *State Fiscal Crises: Causes, Consequences, and Solutions*, Urban Institute web-based distribution 2003 (also reprinted in *State Tax Notes*, August 2003).

Tanzania Government website, accessed October 1, 2006:
<http://www.tanzania.go.tz/commerce.html>.

Tanzi, Vito (1995), *Taxation in an Integrating World* (Washington, D.C.: The Brookings Institute).

Tsui, Steven (1998), "Land Value Increment Tax for Redistribution and Efficiency in Taiwan, ROC," in Proceedings from the International Seminar on Land Policy and Economic Development, November 16-17, 1998, Taipei, Taiwan, Republic of China.

United Nations Conference on Trade and Development (2006), "Foreign Direct Investment Database," accessed on September 15, 2006:
<http://www.unctad.org/Templates/Page.asp?intItemID=3199&lang=1>.

United Nations (2005), "Sustained Economic Growth in Developing Regions Opens Window of Opportunity for Development Goals," Press release , accessed on September 21, 2006: <http://www.un.org/News/Press/docs/2005/eco90.doc.htm>.

U.S. Bureau of Economic Analysis (2006), National Income Accounts database, accessed on September 15, 2006: www.bea.gov.

Wallace, Sally and James Alm (2004), "The Jamaican Individual Income Tax," International Studies Program Working Paper, Andrew Young School of Policy Studies, Georgia State University, Atlanta, GA.

The World Bank (2005), *World Development Indicators*, Washington, D.C.

Youngman, Joan and Jane Malme (1994), *An International Survey of Taxes on Land and Buildings*, Netherlands: Kluwer Law and Taxation Publishers.