International Property Tax Institute

PRESIDENT'S MESSAGE

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As usual, the coronavirus, COVID-19, continues to dominate the headlines, but more countries are now easing some of the restrictions imposed to deal with the pandemic, although concerns remain over the possibility of a second wave of the virus.

Anyway, I thought I would move on to a rather different topic as the main feature of this month's newsletter; that is, the property tax system in Armenia. I have to admit that, until recently, this topic had not been the centre of my attention, but a recent article about proposed changes in the system caught my eye, partly because it provided some useful information about property tax in Armenia, but also because it raised a number of the issues that affect many other property tax systems around the world.

The headline read: "In Armenia, a new property tax prompts debate about social justice" which, as regular readers of this newsletter will be aware, is a topic which has been considered in many other jurisdictions, particularly in the light of the impact of the pandemic.

The article went on to state that, after introducing a flat income tax in 2019, the Armenian government now plans to levy an increased property tax with the aim of bolstering local budgets. Critics warn that this increased tax could become a social burden for people on low incomes, and that the gentrification of the Armenian capital Yerevan might accelerate - and poorer residents could move away.

The Armenian parliament gave the green light to the government project to increase property taxes and the Prime Minister characterised the introduction of a progressive property tax as one of the most important economic reforms in Armenia. "Last year we were criticised for violating the principles of social justice by introducing a flat income tax. We then said that we would solve the issue with reforms and with a progressive property tax," he said.

While many inside government and the ruling coalition MPs see these tax changes as a social justice reform - their emphasis being on taxing visible wealth - the project has sparked another wave of criticism towards the government's economic policies. These planned tax amendments come a year after the Armenian government introduced a controversial flat income tax, which was criticised by various groups at the time as being unfair.

Much of the current criticism about the planned amendments has focused on how people on low incomes who live in downtown Yerevan and other expensive neighbourhoods will pay increased property tax - an annual tax on property owners. Many of these people either inherited their apartments or received them through state programmes during the Soviet era, and some fear the new property tax will result in severe gentrification of the Armenian capital.

In an interview, the head of economic research at Armenian Revolutionary Federation Bureau commented that the proposed property tax cannot be considered as a social justice reform as it could impact poverty-stricken communities in Armenia. “The poor receive welfare payments from the government and taxing them more during a pandemic is unreasonable,” he said. “It is like giving them help and then taking it back.”

According to official data, the average monthly salary in Armenia is 135,000 drams (US$280), while the median salary is even lower. Those same statistics state that 23.5% of the population live below the national poverty line. Responding to the risk of low-income households not being able to pay the property tax, the Deputy Finance Minister said that paying the taxes will be manageable for the majority of people on low incomes, mentioning that a gradual four-year implementation plan had been designed.

An MP in Armenia’s ruling coalition justified the government’s rationale saying that “when we introduced the flat income tax, it was already announced that the logic of our tax policy would not be taxing income, but taxing property and expenses”. Another MP from the ruling coalition said in an interview he thinks people living in downtown Yerevan who are unable to pay the property tax should sell their apartments and “move to more humble apartments somewhere else and enjoy the saved money”.

In Armenia, a lot of real estate is not taxed at all and most is under-taxed. The reason is that property tax is collected according to the land registry value of real estate which is, as a rule, much lower than its market value. To counter this and, in its words, bolster local budgets, the Armenian government is planning to introduce a six-step tax system, under which the greater a property’s land registry value, the more the tax that has to be paid. The tax rates will be different for apartments and houses.

In 2019, Armenia’s State Committee of Real Estate initiated a process of reassessment (the last time land registry values were assessed was in 2002), with the goal of equalising registry and market values of real estate. The process is ongoing. The committee sets land registry values according to a special zoning system. Recent updates introduced 20 new zones (instead of the previous 17), 10 of which are in Yerevan.

In order to make the change as smooth as possible, the Armenian government says the changes will be introduced gradually, starting from December 2021. The four-year plan implies levying only 25% of the tax for the first year, 50% for the second, 75% for the third and 100% for the fourth year.

The government is also planning to remove a 3,000,000 dram (US$7,000) non-taxable threshold - properties valued under this amount are currently exempt from property tax. In a recent cabinet meeting, the Prime Minister said the non-taxable threshold should be cancelled, partly because there is a need to change public attitudes towards the state budget.

"We should care about our state budget the same way we care about our family budget," he said. "The non-taxable threshold should be eliminated. If a person's yearly property tax is as low as 100 drams (US$0.20), and our calculations show there will be such cases, let them pay it anyway. Fiscally, this means nothing, but psychologically, politically and in terms of civic attitude, this is of great importance."

According to figures recently presented by the Ministry of Finance, there are roughly 432,000 apartments in Armenia. Sixty three percent of these apartments (275,000) fall under the current non-taxable threshold, with 107,000 of these apartments located in Yerevan.

Under current land registry values, most apartments are undertaxed. For instance, the annual property tax for around 135,000 apartments is 1,800 drams only (US$3.73) and there are just 6,000 apartments which generate a property tax of around 42,000 drams (US$87).

The Finance Ministry says it has conducted research on international practices of applying property tax, comparing Armenia to countries with similar economies. For Armenia, the annual property tax revenue comes to 0.2% of GDP, while for Georgia it is 1% and Russia it is 1.2%.

Local municipalities are responsible for tax collection and all of the collected money will go to local budgets. The government says, so far, it has no plans to cut funding to local municipalities and sees property tax as an investment in improving public services.

An ARF Bureau economist said that local municipalities will likely have trouble collecting the new property tax because of bad management practices. He suspects the government could decide to cut funds to municipalities in the future, likely by claiming that local budgets will receive increased property tax revenues instead. He said the government should not have eliminated non-taxable thresholds both for income and property tax.

A former Prime Minister recently criticised the proposed reform calling claims that the new property tax is a social justice reform "nonsense" after the government "abandoned the rich should pay more" approach by introducing a flat income tax last year. The leader of an opposition party called on his followers to hold an online protest against the property tax changes.

Despite criticism, it is likely that Armenia's ruling alliance is eventually going to pass the proposed amendments in the second sitting - a move that will provoke further discussions about social justice and criticism of new economic policies in Armenia.

I have provided extended coverage of this topic partly because it is interesting to see that property tax is high on the political agenda in a country that many people know little about, but also because it will be seen that the arguments - for and against the proposed new system - are very similar to the debates concerning property tax, wealth tax, income tax, etc., in almost every country around the world. As far as I am aware, no country has so far found the "ideal" system to balance all aspects of their tax systems with taxpayers' needs and ability/willingness to pay, but the search continues!

Moving on, although IPTI has had to postpone all planned face-to-face events for the remainder of this year, we are continuing to provide significantly more online events, including a variety of webinars and workshops.

One of our most recent webinars, presented in partnership with the Institute of Municipal Assessors (IMA), was a panel discussion on the tax and assessment policy implications of the COVID-19 pandemic. We were pleased to bring together a distinguished panel of speakers to debate the issues and we had a large number of interested participants who were able to ask questions and provide comment. The second of this two-part webinar, being held on 7 July, will look at some of the valuation and other issues resulting from the impact of the restrictions imposed to limit the spread of the coronavirus.

Towards the end of June, I was involved in an interesting "online interview" which formed the focus of a webinar relating to a recent IPTI Research Paper entitled "Redefining Property Tax Management". I was interviewed live by Mordechai Katzman, President of Rethink Solutions, who asked questions about the way in which IPTI had undertaken its research along with our findings and conclusions. Anyone who is interested in finding out more about the issue can obtain a copy of the Research Paper from our website.

We are also continuing to provide a number of online events relating to various aspects of mass appraisal. In addition to webinars dealing with the topic, IPTI has started to deliver online workshops which take a more detailed - and practical - look at mass appraisal valuation modelling. The latest of these workshops involved three very experienced practitioners taking participants through the sales comparison approach. It provided hands-on analytical skills by guiding attendees through the model-building process from start to finish. The scope included mass appraisal model building, ratio studies and model performance review, relative to SPSS, including: a brief overview of the mass appraisal process, highlighting model specification/calibration as well as MRA and a high-level review of SPSS; a case study with a sample dataset using additive regression including exploratory data analysis, model specification and calibration; and finally a review of the quality of the model, application of the equation to the population and identification of properties for further review. It was well-received by participants.

Looking ahead, we will be providing more of these events which will enable participants to gain hands-on experience in developing models for different types of valuation. Full details of these online workshops, along with all other webinars we will be offering over the coming months, are available on our website: www.ipti.org

I should add that the latest edition of the "Journal of Property Tax Assessment & Administration" - Volume 17, Issue 1, 2020 - was published in June. The Journal is a joint publication between IPTI and the International Association of Assessing Officers (IAAO) and contains, as usual, many papers of interest to those practicing in the world of mass appraisal.

I am also pleased to report that IPTI is currently busier than ever with a number of projects, many of which are directly, or indirectly, related to the pandemic. A significant number of assessing jurisdictions have sought IPTI's advice on how they might respond to the impact of the pandemic on property markets, property values, assessed values and property tax legislation concerning appeals and revaluations. These projects involve lots of interesting issues and we are pleased to share our expertise in this way.

Now, it's time for a quick look at what is making headlines concerning property taxes in selected jurisdictions and countries around the world.

In Canada, it is reported that municipalities could face a $20B budget shortfall from three months of COVID-related property tax deferrals and pandemic closures. Cities across the country are facing a growing fiscal crisis, triggered at least in part by the COVID-19 pandemic. Many people are choosing to defer paying their property taxes, not taking public transit and not paying the user fees for public facilities (because they aren't using them), all of which can burn a hole in any municipal pocket. "About a third of municipal government revenue nationally comes from property taxes," said an associate professor of economics at the University of Calgary. "The rest comes from provincial transfers and user fees, such as subway or bus tickets." He went on to say, "During a pandemic in particular, you not only have households being strained to the max because of displacement from employment and income, and that creates challenges for paying property taxes, but you also see a huge drop in transit ridership and therefore a huge drop in transit revenue." Unlike the other two levels of government, municipalities cannot run a deficit budget by law. Many cities and towns have already passed bylaws to give local businesses some financial slack during the pandemic. But cities are responsible for providing some of the most essential services to Canadians: roads, fire fighting, police services or public transportation are just a few from a lengthy list. Mayors across the country say this leaves them with few choices. Without a rescue package from other levels of government, cities would likely have few options: raise taxes, cut spending, or some combination of the two. While the Prime Minister recently announced funding of $2.2 billion in annual infrastructure funding for municipalities, it isn't new funding. It will be paid out of the existing gas tax fund and will be delivered in one payment. It gives municipalities earlier access to previously allotted money, but it may not resolve looming financial woes. It is argued that the provincial government is able to borrow money at lower rates than cities can, and the federal government can borrow money at lower interest rates than the provinces. An expert said, "The federal government is better able to carry the load, to carry that debt and to borrow in a much cheaper way than individual cities or individual provinces can."

In Australia, New South Wales is missing out on more than $8 billion a year in revenue because of a tax system that fails to adequately capture value from land rezoning and new infrastructure, the Productivity Commission has been told. The calculation, based on NSW adopting a "betterment levy" on rezoned land similar to the ACT's, will put pressure on the commission amid its review of infrastructure contributions in NSW - and on the government as it looks for ways to fix the state's post-pandemic finances. The Chair of an inquiry into fast rail financing said the pandemic's impact on public coffers made it imperative for politicians to sit up and take notice. "For decades, all sides at all levels, governments have either been negligent or incompetent in not seizing this opportunity," he said. "Because we've been warned, we're entering the area of gross negligence." The submission to the NSW Productivity Commission from a Sydney University academic, backed by the university's research unit, recommends scrapping the current system of ad hoc infrastructure contributions in favour of a 75 per cent "betterment levy". The levy would be applied on the increase in land value when it is rezoned for more lucrative use or benefits from new public infrastructure, such as a metro train line or airport. It was said that a 75 per cent levy, which is the ACT model, would have raised about $8.2 billion in 2018-19 in NSW, and $18 billion nationally, but a levy as low as 30 per cent would still be useful. Economists, planners and academics have long argued for better value capture mechanisms to fund public infrastructure and ensure the value generated by taxpayer-funded projects is not privatised by landowners. The NSW Treasurer has laid out a plan to abolish stamp duty in favour of a broad-based land tax, itself a form of value capture. But some experts argue a separate levy on the uplift caused by one-off infrastructure projects or rezoning is preferable.

A disappointing story from the UK. At a time of global pandemic, most people and business are trying to help each other to deal with the crisis. However, some are seeking to take advantage of it. A company in the UK is trying to enforce payment of fees from business clients that it represents in challenging their valuations for business rates (property tax for non-residential properties). The UK government have given a large number of companies a 12-month "holiday" from payment of business rates for the fiscal year 2020-21 to reflect the financial problems they are facing. Some less reputable firms are charging their clients for the "saving" they are getting from this relief scheme as if they had negotiated a reduction on their behalf. One disgruntled client said, "They achieved nothing, the only rates reduction has been entirely due to the Government." He went on to say, "I have a witness to my meeting with their representative at which he categorically stated that I would not have to pay anything unless their company achieved a reduction." The agents are threatening clients with court action if they don't pay the fee. Another client said, "They are threatening me that if I don't pay this plus a £200 administration fee I will have to pay a termination fee £995 plus VAT and court fees which could end up between £5,000 and £6,000." Another describes the agents as bullies after being billed for a supposed rates reduction. Let's hope that if these bogus demands end up in court, the fee claims are rejected.

And finally, I have two stories to share. The first, which is a source of some sadness to me, concerns the well-known movie "The Blues Brothers". One of the questions I have often asked at various events over many years was "Do you know which film was based on a true story concerning the payment of property tax?". Most people don't know the answer so I would explain that it was this movie which purported to be about an church-owned orphanage in Chicago which faced closure if it could not raise the funds to pay the property taxes that were due. The Blues Brothers - supposedly former pupils at the orphanage - decided to bring together their blues band to raise the money required to pay the bill and save the orphanage. Sadly, it is now reported that the entire story was (perhaps predictably) untrue! I always had a sneaking suspicion that the basic premise of the film may have been flawed because church-owned property is generally exempt from property tax. However, to find the whole story is a complete fabrication is very sad and has destroyed my cherished illusions! Still, the movie does have some great music.

The next one that caught my eye concerned a residential property in British Columbia, Canada where the property taxpayers argued that the value of their property was adversely impacted by the presence of an eagle's nest in a tree which, they said, was a hazard. Perhaps unsurprisingly, the B.C. Property Assessment Appeal Board did not agree and, instead of reducing the value, increased the assessment of the property! In fairness, the increase was based on evidence put forward at the hearing, presumably from an "eagle-eyed" assessor who spotted the property was under-assessed!

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