IPTI Xtracts

Property Tax and Assessment News from Around the World

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### *Tel Aviv subway tax sets a dangerous precedent*

Half the cost of the Tel Aviv subway will be financed by taxing owners of property within 800 meters of a station.

'How do you make a small fortune in Israel? Come with a big fortune." In the 40 or so years since its heyday, the joke has all but been forgotten. Capitalism and an open market have brought phenomenal wealth creation. However, the joke is being dusted off and is set for a comeback.

Half of the cost of the Tel Aviv underground subway system is going to be financed by a tax on owners of properties situated within 800 meters of a station. A bill going through the Knesset orders they pay 75% of the increase in the value of their property. The government's justification is the generous building and betterment rights that will be granted near subway lines.

The unique nature of the tax is that it is not on income or realized capital gains, rather on unrealized capital gains. A person pays tax not on money received, but because the paper value of their assets has increased.

Even in the US, Democrats have only discussed, but not introduced, a so-called billionaires tax on unrealized assets to help fund trillions of dollars in new spending. Opponents of the tax claim it will damage economic growth. It will be a disincentive for people to build wealth when they will have to hand over cash based on the paper value of their assets before they have any money in their hands.

There is also a fundamental difference between the proposed billionaires' tax and the bill going through the Knesset. Proponents of the billionaires tax point out that the people it targets have massive fortunes in shares, which are highly liquid. In contrast, the subway tax is targeting property, a non-liquid asset. And the billionaires' tax, if it indeed ever happens, will target the unrealized assets of those with massive wealth, as opposed to the subway tax, which is going after normal working people.

Owners of properties hit by the subway tax will have to take hundreds of thousands of shekels from their savings or pension funds. If those are not options, they will have to borrow the money and pay interest on the loan or sell their property. The latter will mean moving away from their friends and communities they may have lived in for several decades.

The tax is brutally unfair. Increases in the value of a property are already taxed by higher local property taxes and higher capital gains when the property is sold.

Many residents will never use the subway, be it because of age, disability, comfort or lifestyle but will have to pay the bill. Those who will benefit most will be from out of town, coming for shopping, business, medical appointments and leisure. All they will have to pay will be the fare, possibly covered anyway by an existing travel pass.

Apartments within 800 meters of a station will be hit by the tax while neighboring units outside will be completely exempt. Presumably, the tax will apply straight away, or be staggered over many years, even though the subway will not be ready for over a decade. During this time, there will be massive disruption, dirt, building works, traffic and noise.

Local authorities, who will determine how much property values will rise, are obviously biased, as they have a vested interest to raise as much money as possible. The market value is the only true metric. The 75% rate is ridiculously high compared with tax rates in the Western world. And there is nothing to stop the government from changing the rate, or indeed the 800-meter rule when the project inevitably goes over time and budget.

It is also conceivable that, as people sell to avoid the tax, they will have to do so at a steep discount. The market could be flooded by sellers, and potential buyers will be put off by the tax, especially as they cannot know what their eventual exposure will be.

The underground subways in London and New York, both built in the late 1800s, were financed initially by private companies. Each had a viable business model. If the government thinks that the subway cannot be financed by projected income from rail tickets, and revenue from other indirect taxes due to increased business, it places a serious question mark on the whole project.

The bigger issue, however, is that once a tax on unrealized income is introduced, no one with assets will be safe. This applies whether those assets are properties, shares or private business. There will be nothing to stop a finance minister marketing themselves as a modern-day Robin Hood and introducing unrealized capital gains taxes anywhere and everywhere in order to finance budget deficits or projects that will never pay for themselves.

Residents in Tel Aviv may turn to the Supreme Court, which struck down the third apartment tax. The tax had ordered those with three or more properties to pay NIS 1,500 per month for each, regardless of the level of any rent, in addition to other taxes.

In personal relationships, trust is essential. Destroy trust and the relationship is gone. Likewise, if trust in the tax system and the government is eroded by new, novel and unforeseeable taxes, and by taxes on unrealized profits, the consequences for Israel could be catastrophic. People will have no security about their financial future. Aliyah will be impacted, investment scaled back, and people's ideas and inventions taken elsewhere.
The fact that the Tel Aviv subway tax is being pushed through the Knesset without any real public debate or opposition is a serious warning sign as to what could lie ahead.