IPTI Xtracts

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URBAN DUMP LAND: AN UNTAXED HEAVEN

Investing in piece of land considered one of safest options of money dumping

A World Bank review of nine cases of vacant land taxation from around the world in 2016 found that different governments define, identify, prioritise, and ultimately tax vacant land in different ways.

This includes deciding how to structure vacant land taxes, who benefits from the tax and how, and what penalties will be imposed if the required payment is not made.

It’s a clear myth in Pakistan that if you don’t have any active successful business to sink in your investments, you either buy commodities, equities or assets, ie, a piece of land with hope that you will sell it once the price increases.

It is considered as one of the safest options of money dumping. Travel across metropolitan cities and you’ll notice junk of private societies luring potential buyers. Icing on the cake is that you can dump in hard cash. Being banked and taxed can be taken care of via different ways.

Pakistan, a country already reeling from mounting debt, always looks for different options to tax its citizens but the most handy taxation option seems to be of no interest to policymakers.

Land value taxation includes an instantaneous, albeit stashed, mechanism that imposes a significantly higher tax on vacant land. This is because land value taxation does not account for improvements in valuation, so landowners with large houses or other large fixed assets pay the same tax as an owner of an empty plot.

Tax can be levied based on the estimated fair market value of land and improvements. Cities are increasingly enacting new rules and taking measures to levy additional taxes on owners of vacant land and properties.

Property market values are best verified through sales transactions or assessments by banks or insurers, who have a vested interest in estimating a fair market value for risk management purposes. But again, payment infrastructure is not formal at all.

It leaves with very less options to bring people to tax net who are dumping their money in empty plots.

Split rate property taxation can be a way forward, which refers to the application of tax on all properties as well as tax on improvements to built-up properties. But how to figure out the landowners who are supposed to be taxed is a difficult task when the process of transfer is very informal, ie stamp vs registry vs file vs possession.

Policymakers rather seem to incline towards surtax on urban dumps, where land that has been vacant for at least x number of years is subject to a higher tax than the x% property tax on improved plots.

There can be other way forward as well. Government can impose extra levy on dump plots based on the World Bank pilot model in the Philippines and Washington.

In Philippines, the tax is levied on landmass greater than 1,000 square metres, regardless of one half which is an unimproved residential lot and regardless of land area, one half of which is unutilised or unimproved residential lot at 2.5% per year of the assessed value of property.

In Washington, an extra levy is imposed on regular properties at 0.83% of the assessed market value, 5% on vacant land property based on the assessed market value, or 10% on blighted/ ruined property based on the assessed market value.

But how to assess the market value of a dump plot is a serious issue. There are three different market value benchmarks – DC rate, FBR valuation and market value.

How can a dump plot valuation be figured out minus development is another problem. To estimate the valuation of a dump plot, it is important to separate the value of land from its improvements.

There are also instances where tax credits are used to protect vacant land. These have been used primarily in Pakistan, where urban growth is outpacing agricultural land and forests.

There is a desire to safeguard these lands because they provide other public benefits, particularly agricultural land used for food production. However, as cities grow, the value of land rises, and the idea is that without tax credit, the landowners would be incentivised to sell it for construction.

Tax relief prevents them from doing so, instead incentivising the owners to keep their land. However, just as in previous cases where taxing vacant land was an ineffective tool for encouraging densification, efforts have been ineffective.

It is important to note how many private societies emerged in metropolitans in Pakistan and out of those how much proportion is dump land.

Showing green land as part of brown land for NOC purposes to build fancy societies is grave corruption, which needs to be stopped via a proper framework and dump urban plots need to be taxed.