CONCLUSION AND SUGGESTIONS

Conclusion

- Local governments do play an important part in the development of cities. Despite handicaps - population growth, inflation, and resource constraint - real per capita expenditure of local governments and autonomous agencies increased during the 1960s and the first half of the 1970s. In the 1980s, however, many cities saw real expenditure levels decline signifying fiscal problems and a deterioration of civic services.

In general, city governments meet about 70 percent of their expenditure out of locally raised revenues. There has however been a decline in the share of local revenues in the 1980s reflecting greater dependence on external sources usually controlled by higher level governments.

Average based on available data show that about 50 percent of the local revenues is derived from taxes, the rest from self-financing services but again the pattern in far from uniform. A variety of taxes are drawn upon by local governments the property tax being the most common and often the dominant tax source.

Property tax and octroi are the most important components of the tax income of the selected municipal bodies and together account for nearly 90 percent of such income. Although octroi has been an elastic and buoyant source of revenue its future is clouded by uncertainty. Octroi has not been considered as a source of further tax income owing to the central govern-
ments commitment to do away with it. In this context, we have to basically rely on property taxes for mobilising the existing resources within the framework of the Municipal Acts.

At least 70 percent of the income of the municipalities comes from taxes, i.e., tax on property, house tax, water tax, lighting tax, drainage and conservancy tax, etc. Property tax is not as important in small municipalities as in big ones due to a variety of factors. Whatever may be the policy impasse, it is sheer incompetence in the system that the per capita property tax is no more than Rs. 2.60 per capita per month even in million plus cities. This is in cities where even one room apartment in an ordinary localities can cost up to Rs. 1000 per month. In smaller municipalities per capita per month property tax is just one quarter of a rupee.

Though the property tax is one of the major sources in the municipal revenue. The share of property tax in the total municipal revenue is on decline.

There has been a very increasing evidence over recent years that the property tax has not been a buoyant source of revenue. Growth in property tax revenue has not been commensurated with the potential that it has, keeping in mind the increases in market values of property over the same period. Further, the tax is not elastic to increasing service costs and is not related to demand for services emanating from different land uses.

Other criticisms of the existing system of property tax are based on broader issues of rising land values which it is unable to keep pace with and
serve any urban development objectives. Thus, it is neither serving as a tool of resources mobilisation for meeting the increasing demand for services nor as an instrument for promoting the urban development objectives with the result the property tax has become an inefficient and inequitous tax instrument.

Thus, increasing dormant fiscal role of property tax apart, it is no longer an elastic source of revenue. Whereas the elasticity of property tax at constant price to population is weak in the case of Bombay, Delhi and Madrass, it is inelastic in Ahmedabad and negative in Calcutta. In Calcutta, it was found inelastic to capital investment at the city level and the number of holdings. A recent study of property tax in per capita terms has fallen behind that of land prices, rents and general cost of construction. The buoyancy of property tax per capita with respect to average land price was around 0.5, with respect to cost of construction it was around 0.8. It was about 0.7 with respect to rents (Delhi Administration 1990: 22-23).

In addition to declining revenue performance and inelasticity and disparities, serious inequities have come to characterise the property tax system in India. These shortcomings of the present property tax system are the result of a combination of inherent infirmities in the system itself. These infirmities as also the evolution of declining role of property tax, its inelasticity, disparities and inequities can be better understood and appreciated by looking at the basic feature of property tax system in India.
There exists four types of rate structure as provided for in the various statutes. These are (1) flat rate system, (2) slab system, (3) graduated slab system, and (4) straight line system.

The corporations of Delhi and Calcutta practice discriminating tax rates between residential and non-residential properties. In Delhi, the marginal rates of general tax for these two types of properties vary from 10 and 15 percent respectively on the lowest slab to 20 to 25 percent respectively in the slab of Rs. 10-20 thousand. The Corporation of Calcutta imposes surcharge on non-residential properties to the extent of 50 percent of the consolidated rate. It gives tax concession upto 45 percent of the consolidated rate to the newly constructed properties for a period of three years.

Relatively high tax rate in Bombay and Ahmedabad (including service taxes) has been brought about by the compulsions of a depressed base. Ever increasing local public expenditure commitments and the depressed tax base are compelling factors for the enhancement of tax rate. However, the corporations of Madras and Trivandrum seem oblivious to such a situation. In the latter, the rate structure has not been revised since 1967. In the former, it is still pegged at 1972 levels.

A great deal of variation is found in the tax rates not only between different states but also amongst the various municipalities of same state. Thus, there is inter-state variation as well as intra-state variation in rate structure. The consolidated rate (consisting of property tax and other
service taxes) varies from a minimum of 6.25 percent of the ARV in Alwar in Rajasthan to a maximum of 20 percent in Ghaziabad in U.P. It thus, indicates interstate variations.

In Haryana all the municipal bodies levy the tax at a uniform rate of 12.5 percent of the ARV except for the municipal bodies at Faridabad and Rohtak. These towns apply a lower rate of 10 percent of ARV. The reason for such a lower rate is attributed to the fact that in Rohtak the rates have not been revised since 1935 whereas in Faridabad the existing rates are the same as in the years prior to 1971.

In U.P., there exist variations in the general house tax rates as well. These vary from a minimum of the 5 percent in Hapur to 10-12.5 percent in Meerut. There are two reasons for such variations in the property tax rates in Uttar Pradesh. Firstly, the U.P. Municipality Act does not provide for a fixed limit of property taxes. Secondly the revisions have not been made in an uniform manner. Except for Ghazibad all other towns belonging to U.P. have not revised their rates for several years.

It is equally important to note that there is a positive relationship between the property tax rates and the per capita yield. Ghaziabad which has the highest rate of this tax (24%) also happens to be the town with the highest per capita yield. As against this, in Alwar the yield is the lowest as the prevailing tax rate happens to be only five percent of the ARV. Hence there is scope to rationalise the rate structure of property taxes.

In certain cases, there appears to be a variation in the rate structure
of property taxes. For instance, the rate structure in U.P. towns varies substantially from one town to other. Similarly from among the Haryana towns, Faridabad and Rohtak apply a rate lower (10% of rateable value) than all other towns (12% of rateable value). The main reason for such variation has been the inability of the municipal bodies to pass a resolution and request the state government to issue a notification for modifying their rate structure in accordance with their eligibility.

Though rental value of land and building constitutes the base of property tax, the enabling legislations in all the states have only vaguely defined the base. Lack of clarity in the definition of property tax base has led to considerable erosion in the base with all its accompanying consequences for elasticity and buoyancy of property tax. Almost all the enactments for constituting the municipal authorities in various Indian states define the base as the "gross annual rent of land and building at which they may reasonably be expected to let from year to year". Deductions varying from 10 to 15 percent of the gross annual rental value are provided for in various enactments towards repairs and maintenance so that the properties could be in a state to command that rent.

Only in Gujarat, the Municipal Acts and Rules provide for the "rent actually realised" as the basis for levying of property tax. But it also lays down that if the rent realised is a collusive rent, the tax is to be assessed on the basis of "reasonable rent". Some of the Acts provide for determination of annual rental value by taking some proportion of the capital value of land
and buildings. The enactments in the states of Tamil Nadu and Kerala provide that for government and railway properties are any other type of property which are not rented and therefore the rent can not be estimated, rental value is to be computed at 6 percent of the price of land and the estimated cost of construction at the time of assessment. The law provides for depreciation on construction cost varying from 10 to 15 percent.

The Calcutta Corporation Act provides for 5 percent of the capital value of properties used as hospitals, educational institutions, places of worship etc. as the gross rental value. However this is 7.5 percent for other types of properties for which rental value can not be estimated. The Act has an innovative provision in so far as it has included also "service charges" within the purview of rentals.

Property tax apparently, consists of rentals which a property could be" reasonably expected" to fetch in the market. Application of such an abstract concept in a real live situation has been one of the major problems afflicting the property tax in India.

There is found to be an erosion in the property tax base owing to the operation of rent control laws. The operation of rent control laws has considerably depressed the base of this tax. The "reasonable annuals gross value" is not the market value but the standard rent as determined according to the provisions of the rental laws.

The determination of the base of this tax, that is, the gross annual value at which the property is" reasonably let from year to year" is a highly
subjective exercise and hence is riddled with corrupt practices. This could be minimised by making the valuation objective and explicit. This requires the standardisation of rents on a per sq. ft. basis by taking into account some of the attributes of the property such as location, quality and type of construction, land use, age of building and so on which are instrumental in raising property values. The municipal corporation of Delhi already follows this method in a crude manner by evolving what they call the "rental data". Further sophistication has been brought into it in Bombay, Bangalore and in all the Urban areas in Kerala. The Ahmedabad Municipal Corporation has introduced valuation on the basis of carpet area which takes into account attributes such as location access to infrastructure, use and structure of the properties concerned.

Proposals have been made to replace the base of ARV by alternatives like capital value, or site value, or composite bases determined by the summation of a number of selected variables, (e.g, location, type of building, age of structure, etc.) each with a predetermined weight. It is necessary to mention that several countries including Canada, U.S.A. some Latin American countries and a few other, have the capital value base. In U.K., from which our system was borrowed, the Layfield Committee of 1976 recommended a change over from ARV to capital value, but this recommendation has not been accepted by the British Government.

Although capital value base has advantages like easy determination than ARV; flexibility in adjusting rates; inducing better land use by bringing
unimproved land under taxation; attaining the desired allocative effects in
regard to the use of land; and becoming more responsive to the economic
changes and have an objective valuation of property; in Indian situation
because of the imperfect property market, the system cannot work. Unlike
Europe and America where CV system is in vogue, we do not have a well
developed real estate market in our country, where properties could be sold
frequently. Even when the properties are sold, the amount mentioned in the
sale deed is understated. The valuation exercise in the absence of a well
developed real estate market will prove to be highly subjective. Local
Finance Enquiry Committee 1951 and Taxation Enquiry Commission 1953-
54 were all against the CV system.

Will it then be worthwhile to switch over to Site Value (SV) system
? The SV system of property taxation besides serving as an instrument of
revenue mobilisation, also serves the urban development objectives. Under
this system the tax is imposed only on the value of the site, leaving out all
structures. It is, argued that if building are 'derated' then building activity
will be encouraged and unutilised areas fully utilised.

However, the basic problem of valuation, still remains intact. If there
is no open and free land market, the determination of site value presents the
same difficulty as that of capital value. Leaving the buildings out will mean
serious discrimination against the owners of residential accommodation or
small structures.

This then leaves the scope for reforming the property tax limited to
a system of imposing the tax on the basis of certain area details. Suggestions have been made for the replacement of all direct valuation whether of rental, or of capital worth, or of site, by some objective criteria, like the area of land, the plinth area, the floor area and so on. A more developed variant of this 'composite base' or the 'points system' under which the tax is payable is determined by the summation of a number of selected weighed variables. In fact, the single criterion schemes also include weightage for a few other variables and therefore, all this can be discussed together.

One suggestion has been to levy a land tax and also a building tax, both on the basis of area measurement. The rates would vary according to zones and there would be additional charges for non-residential use and also to meet development cost where applicable.

A second suggestion is that in addition to land and plinth areas, other factors like location, type of construction, nature of use and age should be compounded into a standardised formula.

The system adopted in Orissa had come somewhat nearer to this system. However if the property tax is continued with the system of area characteristics and valuation of assessment is formalised on the basis of the few most important factors giving rise to property values, it may not withstand scrutiny by the courts of law after the enactment of new rent control law, if it does not delink the property valuation from the provision of rent control law. The fair rent or the hypothetical rent to be fetched by a property has been interpreted by the Supreme Court as the standard rent
determined according to the Rent Control Act.

The alternatives suggested reveal that there hardly exists any scope for changing base. The remedy lies in improving the ARV system within the existing system itself, by either computing the rateable value on the basis of area of land and built-up value there on or with the application of appropriate factors taking into account the location and standard of construction.

A workable suggestion towards reform in specifying the basis of the levy of property tax would be to substitute the Municipal Act, the term "standard rent" for "reasonable rent". The following factors are to be taken in the calculation of standard rent - the user, percentage of cost of land and cost of construction. The system of assessment on the basis of actual rent should be abandoned and the rates as per the PWD schedule be revised according to a new base year.

Yet another constraint is the valuation and assessment procedure. Firstly, a substantial proportion of additions and alterations brought about in the properties are not properly reported. Secondly, the distortion of the rental market because of underhand practices of pugree (Key money) and advances does not allow an assessment of the real rental values of properties. The base of this tax thus gets depressed further. Thirdly, the valuation and assessment of the property tax is not revised as stipulated in the relevant acts and by-laws.

The crux of the problem in resource mobilisation from this tax lies in
capturing, as far as possible, the market value of the land and building so that increases in property values are constantly mopped up. This calls for periodical valuation and assessment as provided for in the relevant laws and bye-laws.

In view of the fact that it is politically as well as administratively difficult to revise the property tax demand in retrospect, it is better if the selected municipal bodies exercise their powers of quinquennial assessment of property tax demand well in time. This has substantial potential for the mobilisation of municipal resources.

The attempt to improve the buoyancy of the property tax collection through a better method of valuation of the properties can be seen in the suggestions of CVB. The method suggested by CVB and immediately accepted by some of the municipalities indicates that the rateable value of properties has increased substantially. In contrast, the property tax of the other municipalities, which continue with the old method of valuation, remains at a much lower level. It will be useful to point out that the difference in the property tax yield between these two groups of municipalities is statistically significant.

There exists a host of administrative deficiencies in the management of financial resources. These deficiencies are:

1. There is virtually no management information system for an effective and efficient tax administration. For example, information on the
various property attributes which are very important for property tax administration does not exist even in rudimentary form. This makes it difficult to identify the problem areas.

2. The current accounting and budgeting practices do not include the factual and actual resource position.

3. The collection machinery has been lethargic and inefficient with the result that the tax arrears have been mounting year after year.

Further, delay and backlog in finalisation of valuation is on rise. There are about 6 lakh properties within the jurisdiction of the MCD and this number is increasing every year due to the process of suburbanisation and urban growth. The assessment department, however, is not able to cope with this magnitude. Thus valuation and assessment is not finalised for a very large number of properties. According to a recent study of procedures relating to fixation of reteable value of property in MCD, the backlog of properties is increasing year after year.

Non-availability of data on the extent of current demand, arrears and collection of current demand as well as arrears do not permit an objective analysis of tax collection.

There has been a progressive increase in the arrars. Hence, much is desired to tone up the collection of property tax.

Thus, yet another factor adversely affecting revenue performance of property tax in India is poor collection efficiency of the property tax administration. Whatever tax is assessed on a deficient and depressed base
by applying the rate structure which itself is not rationalised and reviewed frequently, is not collected effectively. The ratio of collection of total tax demand in the case of Ahmedabad has declined from around 40 in 1980-81 to about 18 in 1990-91. During the same period, its accumulated arrear demand has increased from about two-third of the total tax demand. Trivandrum municipal corporation is able to collect less than one-third of the total property tax demand. Only the municipal corporation of Madras is able to collect around 70 percent of the total tax demand. But the arrears to be collected have mounted to about one fourth of the total demand.

No amount of perfection in the base, VAP and rate structure will increase the yield from property tax unless the increased demand arising out of these packages of reforms are collected (Dillinger 1988). Collection efficiency presently is very low. Enhancing of efficiency in tax collection will call for application of ABC analysis for concentrating the collection efforts on the high value properties which involve very high demand. Generally, such properties are less in number but account for a high proportion of the total demand. Exempting the low value properties will also go a long way in enhancing administrative efficiency as it will save the frittering away of energies in realising a small proportion of total demand from a very large number of such properties. Other areas of reform pertain to penalties to be inflicted for non-compliance and incentives for prompt payment. in all the enactments, there is a provision to collect property tax as arrears of land revenue, if the assessess default in payment of tax. This
provision culminates in attachment of immovable properties. The municipal authorities hardly take recourse to this provision. MCD has, however, innovated an interesting practice of attachment of bank accounts. This has proved much more effective in promoting tax collection than the complicated procedures involved in attachment of immovable property. Charging a penal rate of interest is yet another strategy which could be profitably used for ensuring tax compliance.

Raising of exemption limit to Rs. 1000 per annum and a package of incentives given in Delhi by MCD led to doubling of property tax collection from Rs. 180.96 million in 1978-79 to Rs. 379.52 million in 1983-84 (Sharma 1991: 34-68). Incentives included a rebate of 25 percent in tax for SOPs and properties constructed after 31 March, 1985 if the tax was paid within the due date. This for the partially self-occupied properties was 15 per cent. The municipal staff engaged in collection work were given cash awards for enhancing the collection ratio. This provided a built-in incentive for the employee to be motivated. If these incentives did not work, the penalty included attachment of bank account as also the immovable property. Litigation is minimised by providing for in the law itself for payment of tax before moving a court for legal intervention.

**Generalization About Property Tax Policy**

1. The property tax should be kept as simple as possible. Exemptions should be kept to a minimum and rate structure kept as uncomplicated
as possible. Reform should emphasize improving the general property
tax administration rather than adding special features to affect resource
allocation or income distribution.

2. The property tax needs to be viewed as a system, and reforms need to
be coordinated by all parties involved in structuring and administering
the property tax. Decisions about assessment and collection practices,
exemption policy, and rate structure design may be the responsibility
of different offices but must not be made independently.

3. In general, a flat rate property tax on all real estate is not likely to be
regressive in either the short or long run.

4. The distribution of property tax burdens will be more progressive if the
preferential treatment granted to owner-occupants is eliminated.

5. The exemption of low-value properties or, better yet, granting all
taxpayers a deduction from assessed value will make the property tax
more progressive, favour low-income housing development, and ease
property tax collection problems. The revenue costs will be small.

6. On balance, it is preferable to tax land more heavily than improve­
ments. Therefore, if increased revenues are to be raised from an
existing capital value tax, it is worth considering raising the tax rate
only for land, rather than for land and buildings alike.

7. If a special tax is to be levied on vacant urban land to speed up its
development, this tax instrument should be explicitly linked to a land
use development plan rather than applied indiscriminately to all vacant
property in the metropolitan area.

8. A property transfer tax is likely to interfere with the efficient operation of urban land markets and should be replaced by more effective administration, and possibly a higher rate, for the general property tax.

9. A land value increment tax is not likely to be effectively administrated in developing countries. Efforts to raise property tax revenues would do better to focus on improving the administration of existing property tax systems.

10. The four facets of property tax administration - identification of properties, record keeping, assessment, and collection - must all be improved to make the property tax more productive. Improving collection efficiency alone will increase revenues in the short run but will not provide the broader base necessary for long-run growth.

**Suggestions for Reconstruction of Property Taxation in India**

As the constraints in the existing practices inhibit the optimum utilisation of the property tax base, the resources from this source can not be substantially mobilised unless these constraints are removed. In view of this a set of measures is suggested which can help in removing these constraints.

**Nature of Base**

a) Buoyancy of property tax could be restored by restoring the competitiveness of the rental market by, among other things, explicitly
defining the base and delinking the dampening effects of RCLs on property valuation.

b) The abstract concept of 'reasonable rent' needs to be explicitly defined in terms of "rent actually received" or "the prevailing rent" so that there does not exist any amendment about it. It will have to be accompanied by amendment in the RCLs.

c) Sustainable reform for refurbishing of the base requires to amend the RCLs in one of the three ways viz. (i) complete delinking of provisions of the RCLs from municipal assessment; (ii) restructuring the scope of the RCLs for providing protection to the target group for which these laws were enacted; and (iii) indexing of Standard Rent.

Valuation and Assessment Practices

Timely Revisions

d) With a view to exploit fully the revenue raising potential of property taxes, an attempt should be made to capture the rising market values of urban properties by a regular and timely review of property tax assessment. In other words, efforts should be made to have a timely revision of assessment of urban properties.

e) To dispense with the existing favourable and liberal assessment of SOPs; to review the exemption of Union properties which are not let and hence for which there does not exist a rental evidence, by applying certain ratio on the market value of land and buildings.
f) Collusive rent and concealing of rent could be dealt with by restoration of market rent as the norm for assessment of RV. If, however, it is not effective, Rent Standarisation could be put in to the law itself so that the rent per unit of floor area could be related to the prevailing rent.

g) With a view to enable the municipal authorities to have services of qualified valuers as also to insulate property valuation from local politics, it would be advisable to set up CVO at the state level.

**Rate Structure**

h) The existing diverse type of rate structure (step system, graduated slab system, and straight line system) need to be reviewed. Equity consideration and the ability to pay principle of taxation do not have much of relevance at the local level. Hence, the progressive rates' need to be replaced by a differentiated flat rate for residential and non-residential properties.

i) Increases in the costs of services calls for charging separately for financing of specific services. Charging through service taxes is simple to administer as they are levied along with property tax on the same base. However, as the base of property tax is depressed due to a host of administrative and legal factors, service taxes have to be delinked from the property tax base.

**Tax Collection**

j) Collection efficiency needs to be improved by using punitive mea-
sures like charging a penal rate of interest and attachment of bank account and also by taking recourse to the existing punitive measure like attachment of immovable properties.

k) A package of incentives has been found to be much more effective in promoting tax compliance. Hence, the incentives as tried recently in Delhi by the MCD need to be emulated by other municipal authorities. Thus special drives to improve the collection efficiency is warranted which will include variety of steps: (i) Introducing the collection through identified banks. This include issuing a passbook, giving the detailed breakup of tax demand and collection; (ii) attractive rebates and incentives for prompt payment; (iii) penalising the defaulters by a penal rate of interest on arrears; (iv) solving the huge accumulated arrears on the basis of informal discussions with property holders rather than taking the matter to court.

Rationalisation of Property Tax Administration

Information System for Revenue mobilisation

l) A comprehensive information system needs to be developed as a management aid for mobilisation of resources and management and financing of civic services. Details of properties in terms of their number, use, assessed value, location, type of construction, tax demand, tax collected and arrears, and so on need to be brought into the ambit of such an information system.
Mid-Career Training to the Municipal Staff

m) Improvement in the tax administration (as mentioned earlier under mobilisation from property taxes) as also in the information system will require a multi-level orientation/training for the municipal staff employed in the financial management wing. This training should cover methods of building a strong information base, techniques for proper budgeting and performance evaluation and launching effective collection drives.

Computerisation

n) One of the modern means to handle tax collection system is to undertake its computerisation. In the case of metropolitan centres and large cities it would be advantageous to resort to it, thereby saving time and labour required for handling the various procedures involved as well as for providing varied data quickly for policy formulation with a view to augmenting tax collection. The experiences gained by some municipalities in the proper use of computers should be shared by other to augment financial resources.

Improving Taxpayer’s Perceptions and Relations Between the Taxpayer and the Administration

o) This important step will include:

The political dimension;
Avoiding complexity;
Improved communication with the taxpayer;
Contact points and contact staff;
Improving taxpayers rights;
Decentralising the administration of property taxes;
The introduction of new information technology.

In the end it is to be stressed that property tax structure and administration go together and must be viewed as such while undertaking reform and administration of property tax has four critical aspects, viz, property identification, record keeping, assessment, and collection. Attention must be paid to all of them if the taxation of property is to show better results. Thus, there is need to view property tax as a system and not merely as a set of independent activities. There is no doubt a lot of merit in approaching property tax administration as a system with four interrelated dimensions call for concerted attention.