

Canada's and Russia's Experiences with Land Taxation Reform: Lessons for China

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1. Introduction

Bearing in mind China's ongoing reform of land taxation, we look to the experience of Canada and the Russian Federation in reforming their systems of taxation. The two cases capture the wide range of challenges a reformer would face. Clearly, in the grand scheme of things, Canada's property taxation functions effectively in that it supports national and regional economic development, a reasonable level of equity and social cohesion. Examination of Ontario's transition to the uniform system of current value taxation in 1998 and its outcomes gives us a sense of the modern standards in property taxation, their advantages and disadvantages when their functioning is unencumbered by the institutional upheaval so typical of economies in transition. Here we look to Canada's experience with land taxation to identify "best practices." Russia's experience with (still ongoing) land taxation reform then highlights some of the pitfalls of implementing a modern system of taxation in the context of economic transition.

Notably, in the two cases (1) tax reform was associated with a recentralization of fiscal autonomy at the provincial level in Ontario and at the national level in Russia; (2) was introduced in an opportune political moment and has required a great deal of political

will. While in Canada, the political costs of tax reform figure prominently, in Russia reforms are compounded by the economic and organizational cost of creating cadastres and developing the institution of cadastral assessment from scratch. Ontario's reform took place against the background of good overall budgetary performance and good fiscal discipline among the municipalities, while Russia's tax reform have had to be mindful of the local governments' ability to collect taxes and to finance assessments.

2. Reform of property taxation in Ontario, Canada

Land taxes¹ in Canada are levied by primarily by municipal governments, but some provincial governments levy property taxes as well. In municipalities, property taxes generate revenue for municipal services and for primary and secondary schooling (when levied by provincial governments). For instance, in 2006, 19 percent of the property tax revenue collected by the city of Kensington in Ontario was spent on education; correspondingly, 81 percent were expended on municipal needs. The main expenditure items in the municipal budget are police (16.9 %), social services (15.3%), fire and rescue (11.8%), road maintenance and construction (8.8%) and capital infrastructure investment (8.3%) (Kensington City Government, 2006).

Provincial governments regulate tax bases and rates in municipalities within their jurisdiction. Thus sub-national *regulatory* fiscal autonomy is exercised primarily at the

¹ I discuss throughout this section Ontario's land (plus improvements) value taxation and do not mention land transfer taxes. Similarly to sales tax, land transfer taxes in Canada are collected at the time of purchase of a property. In Ontario and British Columbia the sales taxes are progressive, but use different formulas for calculating the tax. In British Columbia, land transfers for a sum below \$200,000 are taxed at 1 percent, while land sales in excess of \$200,000 are taxed at 2 percent. In Ontario, a .5 percent tax is imposed on land transfers under \$55,000, a 1 percent tax is charged on transfers between \$55,000 and \$250,000, while a 1.5 and 2 percent tax rates are applied, respectively, to land transfers \$250,000-\$400,000 and in excess of \$400,000 in value.

provincial level. Municipal governments have the authority to vary tax burdens across different types of properties.

Property-related revenue accounts for a significant share of municipal budgets, around 53 percent across all provinces in 2000. Property taxation is central to the ability of the municipal governments to meet their expenditure responsibilities. In fact, the 5 percentage-point reduction in the share of intergovernmental grants between 1998 and 2000² was largely compensated by an almost equivalent increase in property taxes (Slack, 2002).

The tax base is defined as “real property,” including land and improvements to it. In some instances machinery and equipment are considered improvements. Special treatment is extended to land with mineral deposits, oil and gas wells, as well as public utilities servicing several jurisdictions, pipelines and railways.

Land and properties are assessed at the market value; the value of farmland and managed forests is established for current land use. An effort is being made to link to the assessed value of the property to the actual conditions of the property market, while avoiding excessive fluctuations. In Ontario, for instance, in 2001 the assessed “current” value was estimated with a two-year-lag; in 2005 the lag was reduced to 1 year³; in 2006, however, the current assessed value is calculated as a rolling average for the previous three years.

Public hospitals and educational institutions, churches, charities, cemeteries and Indian land are exempted from taxes. Lands and properties occupied by government

² Grants declined from 23 to 18 percent of total municipal revenue, while property tax revenue rose from 48.6 to 53.3 percent.

³ I.e. the market value as of June 30, 2004.

institutions (federal and provincial) are not subject to taxation, but pay fees at a discounted rate.

Different rates apply to residential and non-residential properties. Within non-residential properties several types are further distinguished, based on use.⁴ The province of Ontario, for instance, establishes separate rates for five types of non-residential properties: commercial, industrial, pipelines, farms, and managed forests.

To meet differential expenditure responsibilities, municipalities can vary tax rates by manipulating transition ratios.⁵ However the autonomy of the municipal governments is limited – a municipality is free to increase transition ratios up or down for only within a given range, “the range of fairness.” Yet when transition ratios exceed the upper bound of the range of fairness, municipal governments cannot further increase the transition ratio, but can only keep it at the existing level or decrease it, converging toward the range of fairness.⁶ For instance, Ontario’s 2006 transition ratio for industrial properties is 2.5, which is well beyond the range of fairness (0.6-1.1); consequently municipalities in Ontario can either maintain this ratio (2.5) in 2007 or decrease it (See Appendix 1).

In Ontario, the range of fairness for multi-residential properties is between 1.0 and 1.1, while for most non-residential property classes⁷, transition ratios were allowed to vary from 0.6 to 1.1 (Slack, 2002).

A favorable rate applies to farmland at 25 percent of the residential rate (transition ratio 0.25).

⁴ Multi-residential properties are further distinguished.

⁵ Transition ratios anchor the tax rate for each property class to the tax rate on residential properties (transition ratio is equal to 1 if it is equivalent to the residential property tax rate).

⁶ Existing municipal rates for some property classes may exceed the range of fairness for historical reasons.

⁷ The notable exceptions are professional sports facilities and pipelines, for which the ranges of transition ratio were, correspondingly, 0.001 to 1.1 and 0.6 to 0.7 (Slack, 2002).

In Ontario, reduced rates apply to vacant commercial properties (35 percent below the rate of developed commercial properties), while vacant industrial land receives a 30 percent reduction. Agricultural land pending development is taxed at a reduced rate. The tax increases on such land are introduced in stages: when the land is registered for subdivision and when a building permit has been issued.

Tax relief takes a number of forms. Tax deferral schemes are available to the seniors, widowed or disabled, in which case a portion of the land tax is converted into a lien on the property payable when the title is transferred. Property tax credits are available to homeowners and renters. The amount property tax refund is calculated as a difference between the amount of property taxes and some fraction of the taxpayer's income, to the effect that higher income taxpayers receive smaller refunds. Grants to residential taxpayers are extended in Alberta, New Brunswick, Manitoba and British Columbia. The grants and/or subsidies are paid directly to the taxpayer to reduce the payable property taxes. Tax deferrals as well as grants/subsidies are administered by either provincial or municipal governments and are funded from the corresponding budgets; while property tax refunds are administered by provincial governments.

Billing and collection of property taxes are administered by municipal governments. Municipalities collect and remit to the learning board budgets education taxes of a quarterly basis.

Property assessment is coordinated at the provincial level. Provincial governments established independent assessment bodies, such as BC Assessment in British Columbia or the Municipal Property Assessment Corporation (MPAC) in Ontario. MPAC is a non-

profit organization, its governing body, the Board of Directors, comprises taxpayers as well as municipal and provincial representatives. Every municipality in Ontario holds membership in MPAC. The list of MPAC's responsibilities includes: assessment of value of properties, classification of properties, identification of tax-exempt properties, compilation of the annual assessment roll to be submitted to municipal governments, and processing of assessment appeals.

Consideration of assessment-related disputes by MPAC creates an alternative channel of dispute resolution. MPAC facilitates resolution of disputes related to assessments by providing property owners with a opportunity : (a) to review the assessment roll available at municipal offices; (b) to review the details for their own property and basic assessment roll information for as many as twelve properties using MPAC's Internet-based service; (c) to access a MPAC's Property Profile Report showing the assessment details for their property; and (d) to access comparable Property Reports from MPAC for six comparable properties selected by the owner and six comparables selected by MPAC. If consideration of the contested assessments by MPAC fails to lead to a resolution, the tax payer can take the case to the Assessment Review Board, a quasi-judicial body, or appeal the assessment through the court. One indication of the effectiveness of the arbitration process in Canadian provinces is the relatively low rate of arrears which was equivalent to 7 percent of total property taxes in 1999 in Ontario (Slack, 2002).

Eight years ago Ontario's property tax system underwent a reform which thought to correct a number of problems: (a) lack of uniform assessment methods across municipalities, since market value taxation was introduced on a voluntary basis, not all

municipalities adopted it; (b) outdated assessment system – for instance properties in Toronto had last been assessed in 1953 based on 1940 values; (b) inequitable rates and property value assessment between and within municipalities, and between classes of properties; (c) high rate of appeals of inequitable assessments. In Toronto these distortions were politically motivated and designed to shift the tax burden away from the residential taxpayers at the expense of businesses; as a result Toronto's businesses received a substantial incentive to set up operations elsewhere.

In response to these challenges tax policy reform in Ontario undertook a number of steps. (1) A uniform system of assessment across municipalities was introduced. (2) The provincial government required municipalities to move to the single variable rate system which has been discussed above. Prior to the reform, provincial legislature mandated higher rate of taxation for non-residential properties.⁸ Prior to the reform, on average, non-residential property rate was nearly 18 percent above the residential rate; under the new system the difference could not exceed 10 percent. (3) The provincial government provided for tax deferral and gave provinces up to 8 years to phase in the new regulations. (4) The legislature prohibited subsidizing of tax increases for one class of property at the expense of other classes (most importantly, of course, subsidization of the residential class from the commercial or industrial classes).

Reforms led to the shifting of the tax burdens. Within the commercial property class, the relative burdens on small commercial properties increased by comparison with large office properties. To dampen the effect of this shift, the new tax legislature moved to introduce (1) optional property classes to allow for differential rates for subclasses of

⁸ On average, non-residential property rate was nearly 18 percent above the residential rate

commercial properties; (2) optional caps on tax rate increases; (3) provisions that increases in total expenditure be financed from property taxes.

What are the consequences of this reform? Has the goal of equitable distribution of tax burdens been achieved? And more broadly, what lessons can we draw from Ontario's experience in land taxation?

- Within the international context, despite all the inadequacies discussed here and which prompted the reform, Ontario's land taxation has performed well in that it generated adequate revenue for the government to finance maintenance of local infrastructure and to support provincial spending on education.
- Also, despite the fact that land revenue is considered a rather static tax base which cannot support sudden increases in expenditure, Ontario's land taxes made up for the reduction of government transfers to the provincial budget fairly effectively.
- The results of the reforms have been mixed. Indeed, the reform promoted greater uniformity across provinces in assessment and the structure of property taxes. However, these reforms ran up against substantial political constraints – primarily significant increases in the tax rates for certain property types and increased burden on residential tax payers due to reassessment of residential properties and limits on the increases of non-residential property classes. Political repercussions motivated introduction of caps which effectively led to new distortions in the distribution of tax burdens across property classes.
- Having said this, the practice of tying the tax rate on business property to the residential taxes in a given proportion seems like a politically savvy practice with a lot of potential to limit the tendency of the local government to over-tax businesses.

- Concerns with increasing assessed value of properties have led to freezing of the assessed value of non-residential properties at pre-reform (1997) level. Current value taxation is thus implemented fully only in the residential property class.
- The reform recentralized – in the name of fairness – to the provincial level the power to regulate taxes by limiting the ability of municipalities to manipulate the distribution of tax burdens between classes of properties.
- Current value assessment also introduced a greater degree of complexity in tax administration.
- Clearly the new system of assessment is largely trusted and has reduced the number of disputed assessments.
- What insights does Ontario’s experience offer for other reformer? Slack (2006) seems to believe that the longer one waits to reform taxes, the greater the cost of the reform will be – had Ontario introduced current value assessment in 1978 as did British Columbia, the cost of the reform would have likely been lower.
- This also implies that the initial period of reform is most costly politically, financially, and possibly socially.
- Confidence in the fairness of assessments is crucial to market value taxation and investments in “getting assessment right” will pay off.
- The political will of citizens is central to the success of the reform, especially in view of high political cost and when reforms concern such highly visible tax.

3. Reform of land taxation in Russia

Russia is undergoing a reform of its property taxation system. There has been a notable progress toward simplification and modernization of property taxation. Many changes have been introduced only recently and their effect is hard to judge, yet certain attributes of Russia's reform of the property taxation provide relevant insights for China's ongoing reform of land taxation.

Russia and China: Differences and similarities in government finance

The very fact that Russia is attempting to create a modern land and property taxation system in the midst of transition from command economy makes its experience relevant to China.

In Russia, expenditure assignments leave local governments responsible for social protection schemes, which should be financed by the federal governments to ensure proper redistribution (Martinez-Vasquez and Boex, 2001). Similarly, in China local governments are assigned a substantial role in provision of social protection. In both countries local governments face significant expenditure responsibilities and weak local revenue bases and land taxation in both cases is seen as the way to boost local revenue capacity.⁹

Central authority in Russia and China has experienced significant erosion since the beginning of market reforms. In Russia, asymmetric federalism of the early to mid 1990s

⁹ Excessive "earmarking" of central government transfers in Russia and federal limits on local revenues compounds the problem of insufficient revenue sources at the local level (Bird 2002).

was symptomatic of the weakness of the central government. On the one hand, asymmetric arrangements served to appease secessionist movements in the regions, but on the other hand, they weakened the federal government's fiscal capacity and contributed to the federal government's default on internal debt in the wake of the 1998 crisis (Martinez-Vasquez, 2002). In China local secessionist movements did not gain the same kind of momentum they did in Russia, but the inability of the central government to control local officials is symptomatic of the weakness of the central government. Notably, China and Russia both moved to recentralize their systems of government finance after the central and consolidated government revenues also declined substantially as a result of fiscal decentralization of the 1980s and early 1990s in China¹⁰ and in the early to mid nineties in Russia. In Russia, as in China, reform of land taxation is seen as a way of improving the effectiveness of the government apparatus.

The two countries face a related problem of the lack of accountability of local governments. And in Russia, as well as China, there is an expectation that the land and property tax reform must increase transparency of local governments' financing and their accountability (e.g. by eliminating the excessive reliance on extra-budgetary funds).

At a more operational level, like China, Russia has had to build its land taxation system from ground up – there was neither a cadastre of properties nor a capacity to perform cadastral assessment.

Unlike China's, Russia's reform of land and property taxation was initiated in unfavorable economic circumstances, including poor growth and economic instability, but with a renewed sense of urgency – after the default of 1998 – of transforming fiscal relations.

¹⁰ Tax Sharing System reform of 1994.

Land taxation prior to 2005

Prior to January 1, 2005¹¹, the Federal Law on Payment for Land provided the legal basis for land taxation. Land tax applied to land in ownership or use of legal entities and physical persons. Lessees of the state-owned land (federal, regional, or municipal) were subject to land lease fees.

Legislatures at the corresponding levels set the rates of land lease fees for different categories of lessees/owners and types of use. However, the federal government established the minimum and maximum caps on the tax rate, thus setting boundaries to local tax autonomy.

Different fee schedules were applied to agricultural and non-agricultural lands. The tax rate doubled if the land remained unused or if it was used for unintended purposes.

Tax rates on agricultural land vary according to the composition¹² of land, its quality, area, and location. The Federal Law on Payment for Land set the *average* tax rates for each region, while the regional legislature established the *minimum* rate for agricultural land. A different rate applied to non-agricultural use of land by individuals in rural locations. It was a fixed rate calculated on the basis of the area of the plot. Local governments had the discretion to increase the fee by up to 100 percent for plots under non-agricultural use in certain locations.

Taxation rates for urban land were established by the federal Law on Payment for Land. The rates varied by economic zone – there are eleven of them in Russia – and ten

¹¹ That is prior to the adoption of Federal Law N141-FZ from November 29, 2004.

¹² Different rates are set for different soil types of ploughed land, plantations, pastures, etc.

categories of urban settlement size. These rates represent the *average* tax rates mandated by the federal government for a town of a certain size within a given economic zone; the local governments in turn had the discretion to apply differential rates for various subdivisions as long as they could meet the revenue quotas corresponding to the average rate. In calculating specific rates, local governments factored in location, distance from the center of the city or town, the level of economic development, environmental and geological characteristics. The tax autonomy of local governments consisted in the ability to distribute the tax level differently across subdivisions within their jurisdictions, while the overall tax rate for each jurisdiction was set by the central government.

Although land tax was classified as a local tax, its revenues were nevertheless shared between the three levels of government. Tax revenues from rural land in non-agricultural use went to local budgets. Fifty percent of revenues from urban land went to the local budgets, 20 to regional, and 30 to central. The federal share in revenue from agricultural land was set annually by the laws regarding the federal budget. The decision regarding the share of federal government was informed – at least in principle – by the administrative expenses of the federal government (management of land use, operation of the tax-collecting service, monitoring and protection). The regional governments' share in agricultural land revenue was determined by the regional legislature but could not exceed 10 percent.

Land taxation system established in the Federal Law on Payment for Land has a number of problems. (1) The tax rate structure was very complex, with rates varying on the basis of economic zones, types of ownership or lease, types of land use, settlement size, etc. (2) The revenue sharing arrangements were also too complex and allowed the

federal government a substantial degree of discretion of the federal governments to determine its share in the revenue on a yearly basis, which introduced uncertainty into the budgetary process and gave the central government to expand at the expense of the lower tiers.¹³ (3) The federal government appropriated a sizable fraction of the land revenue, for instance, 30 percent of revenue from the urban land tax went to the central budget. (4) The level of taxes was tied to the land's physical attributes and did not correspond to its market value, leading to significant undervaluation of the land. (5) Although the Law granted a degree of tax autonomy to local governments, their discretion was narrowly circumscribed – they could not determine the overall level of taxes they levied in their jurisdictions, but could distributed the tax burden differently across subdivisions.

Reforms after 2005

Adoption of the Federal Law on the Payment for Land in 1992 marked the beginning of land privatization in Russia. In the absence of land markets, to enable transactions in and taxation of land, the law introduced normative land values which varied across regions. Between 1992 and 1998 approximately 129 million hectares of land had been privatized.

The land taxation based on nominal values was confounded by hyperinflation which characterized Russia's transition. Hyperinflation required radical and rapid adjustments of the tax values to maintain adequate levels of real revenue. In some cases – mostly in urban areas – adjustments were made on the basis of market values of land, although

¹³ The same holds for the regional government, but to a lesser extent, since the federal government sets a ceiling on the regional government's discretion to determine its share of revenue.

these markets were very rudimentary. Non-uniform value adjustments to land value led to sizable inequities in the distribution of taxation burden with similar properties assessed wildly differently in different jurisdictions. These inequities undermined the fiscal bases of many local governments and exacerbated substantial regional inequalities of sub-national revenues. The need for a land taxation reform became obvious, but politically challenging.

After the default of 1998, the Russian government has been gradually reforming the revenue system, including the land taxation laws. Chapter 31 of the Tax Code of Russian Federation¹⁴ replaced the Federal Law on Payment for Land.

The new Tax Code defines the land tax as a local tax in the sense that its revenues go to the municipal budgets. Local governments are also permitted to adjust the tax rate.

Between 1999 and 2006, the Russia's Land Cadastre Service, Rosnedvizhimost, prepared a cadastre of nearly all land using mass valuation methods and since January 1, 2006 cadastral value of land provides the basis for land taxation.¹⁵

Mass valuation methods were based on sale comparison, income and cost approaches. The mass valuation of land has been difficult to implement in a uniform fashion (geographically and across types of land) due to lack of reliable land market data. On the one hand, only housing markets in urban centers are adequately active enough to generate adequate market value data; and even then sales represent a minority (approximately 6 percent) of property-related transactions. On the other hand, land registration data could not be used for assessment because the prices recorded during registration are underreported by the contracting parties to reduce transfer fees.

¹⁴ Federal Law N141-FZ from November 29, 2004

¹⁵ The current estimated value of land is assessed at RUR 23600 billion, approximately USD 790 billion (Mishustin, 2006).

As an alternative to market value assessment, geo-referenced statistical models linked to cadastral maps are used to predict the value of urban land. Predictors of market land value include such factors as access to public utilities and services, transport infrastructure, as well as environmental factors.¹⁶ Fourteen types of urban land use – each associated with a certain value per square meter – are distinguished for each cadastral unit and the tax base could be calculated to reflect its current or best use.

Rural land is assessed on the basis of its income-generating capacity, since the agricultural land market is even less established than the urban market.¹⁷ A large number of plots occupied by infrastructure installations, roads, industrial sites, etc. are assessed on individual basis due to the lack of market reference points for their valuation. This introduces a substantial degree of subjectivity and opacity into their assessment.

According to articles 10 and 11 of the Law on the National Cadastre of Lands, provincial governments (subjects of the federation) carry the primary responsibility for conducting cadastral assessment of lands, while collection of additional information regarding the land remains the responsibility of local governments.

The Tax Code significantly simplifies the tax rate schedule. It sets the maximum rate of 0.3 percent of the cadastral value of land for agricultural land, residential land (including land under residential construction), and land under personal use as garden plots. For all other land, the maximum tax rate is 1.5 percent. However, regional governments can set their own rates within the federal limits. For instance, the city of Moscow set the rate on the residential land at 0.1 percent. The Tax Code (article 394)

¹⁶ According to Mr. Overchuk, for areas where reasonably reliable market data are available, the correlation coefficients between predicted and actual market values are on the order of .6-.7 (Overchuk, 2004).

¹⁷ While private ownership of land was allowed in 1992, the sale and purchase of land were permitted since 2002 only.

provides for the possibility of introduction of differentiated rates for different categories of land and land use¹⁸. In Kazan, for examples, the municipal government imposed taxes in the range between 0.1 and 0.4 percent of the cadastral value of land, depending on the category of land.¹⁹ Notably the Tax Code applies uniform rates to different categories of taxpayers. The tax rate is no longer doubled for unused land.

For land in joint shared ownership, the amount of tax is calculated based on the size of each share in terms of the land area. The tax on land in collective ownership is divided equally between the members of the collective.

It is expected that the new cadastral value-based land tax will increase the level of taxes for densely populated urban areas where the value of land is high, while the level of taxes in smaller settlements (less than 50 thousand) will decrease.

Other property taxes

In addition to the land tax, there two more taxes on property: individual property tax and enterprise property tax. Inheritance and gift tax was recently abolished beginning in January of 2005.²⁰ Its abolition received wide popular support and was passed in the Parliament by a vast majority of votes. The dissenting minority – mostly Communists – opposed the law because elites stood to gain the most from it (RIA Novosti, 2005). The

¹⁸ The Land Code identifies several categories of land: (a) agricultural land, (b) land under settlements, (c) lands occupied by industrial, energy, telecommunications, defense, and security installations, (d) lands under special protection, (e) forest lands, (f) bodies of water, and (g) the land reserve (Article 7 of the Land Code).

¹⁹ Municipal government set the rate for residential land under apartment buildings at 0.1 percent and 0.2 percent rate for residential land under individual housing or garden plots. The land occupied by commercial and industrial objects is taxed at 0.4 percent. The land under public facilities is taxed at 0.123 percent; the land tax for city electric transportation facilities is set at 0.1 percent (Interfax-Povolzh'e, 2005)

²⁰ Only gifts between spouses and close relatives were exempted from tax.

wide-spread popular support for the abolition of the inheritance and gift tax, however, was founded on two key considerations: on the one hand, the assets of the elites were hidden in the off-shore accounts anyway and they had easy access to means to avoid the inheritance and gift tax. On the other hand, the burden of the IGT fell disproportionately on the low -income individuals who possessed assets as a result of privatization but who could not bequest or transfer their assets as gifts to their relatives because of high taxes and who could not afford to avoid the tax. Moreover, if the goal of IGT was to tap into transfer of assets by those who disproportionately profited from privatization, this tax base was incorrectly assigned to the municipal level of government. As a local tax, IGT could be more easily avoided by the local elites who were closely connected to the local officialdom than by the poor.

Although classified as regional, fifty percent of the revenue from the enterprise property tax is allocated to the local budgets at the point of collection.

Individual property tax and the enterprise property tax

Individually owned buildings and structures are subject to a tax rate of 0.1 to 2 percent of the inventory, the structure of the tax rates is progressive, with property under RUR 300,000 taxed at 0.1%, that in 300,000-500,000 range taxed at 0.3%, and property valued over 500,000 taxed at 0.3% to 2% .²¹ The tax rate on the property of legal entities (organizations) set by provincial governments, but not to exceed 2.2%. Individual

²¹ The value of the inventory established either by the Bureau of Technical Inventory (BTI) or at the mandatory insurance value. For certain vehicles (excluding automobiles) engine power is use as the basis for taxation.

property tax revenue goes to the local budgets and the enterprise property tax is allocated to provincial budgets (Federal Tax Service, 2005).

As with land taxes prior to the reform, there were substantial regional disparities in the levels of taxation explained by the fact that different municipalities applied their own indexes to categories of individual property to correct for inflation. Inflation adjustments have led to overvaluation of certain classes of property, raising their taxable value above the market price. These adjustments particularly affected valuation of housing.

Collection of individual property taxes on housing which has not been registered during privatization has been problematic. Much valuable new real estate escapes taxation by remaining “unfinished” and thereby unregistered by BTI. In 1999, by Tax Ministry’s estimates there were over 5 million uncompleted houses and apartments on which no taxes were assessed or paid. (Interfax Russian News 1999, August 17).

All taxes are collected by the local branches of the tax inspectorate, the federal tax service. The tax inspectorate then allocates exclusively local tax revenue to the local budgets, while federal and shared tax revenue is transferred to the local office of the federal treasury. The latter separates the shares of different levels of government and transfers the funds accordingly

The way forward

The reform of land taxation has proceeded in a gradual fashion through a series of steps on two fronts: technical and legislative. The sequencing of the reform is informative.

On the technical front, the property taxation reform required creation of a cadastre of properties, which in turn meant development of a new sphere of expertise in land assessment and evaluation. In 1999-2006, Rosnedvizhimost created the land cadastre from scratch. Over this period, over 3500 land assessors were trained and the market for land assessment services was legalized and the licensing of land assessors was introduced.

On the legislative front, as the land cadastre was being developed, the government (a) moved to rationalize assignment of the land tax, making it an exclusively local tax, thus making local revenue flow more predictable; (b) simplified the land tax rate structure; (c) applied uniform rate to all taxpayers; (d) reduced the number of property taxes by eliminating the inheritance and gift tax.

Further reforms on the technical side will involve continued investment into the training of the land assessors is required to support periodic re-assessment of properties; it is expected that reassessments will be conducted every 3 to 5 years. The Leningrad oblast government has recently requested a reevaluation of the land value since the market value of the land has increased threefold since the last cadastral assessment in 2000 (Kommersant, 2006). Clearly soaring real estate prices and construction boom in the capitals put additional pressure on the assessment agencies.

Creation of the land cadastre was conceived as the first stage in creating the technical foundation for the land reform. The next step - on the technical side - is creation of the cadastre of all buildings in addition to land.

Once the cadastre of land and buildings is created, it will be possible to further simplify property taxation by introducing a unified real estate tax, which will succeed the land tax, the individual property tax, and enterprise property tax. The intent to establish real estate taxation and the provisional nature of the current land tax is affirmed in Article 65 of the Land Code. At the moment, the implementation of the single real estate tax has been postponed until 2008-09 due to lack of adequate cadastral maps in some regions.²² The real estate tax will be classified as a regional tax but will be shared with local governments.

The real estate tax has been piloted in two cities – Tver and Novgorod. In Novgorod, a cadastre of all properties has been developed to enable their appraisal. The real estate tax was introduced gradually; at the first stage it covered only legal entities which own the land on which they are located, but at later stages the real estate tax will cover all the legal entities – those which own the land and those which lease.

The experience of many countries with land value taxation indicates that a parallel development of effective methods of dispute resolution is necessary because of a degree of subjectivity in value assessment. Currently land disputes are handled by the courts or arbitration courts. Aleksei Overchuk, the deputy chief of the Federal Real Estate Cadastre Agency, emphasized the need (a) to create organizational infrastructure to enable effective handling of appeals of cadastral assessments (the total number of tax-related disputes filed in courts grew 400 percent and in 2000-2005²³, and the trend in

²² The lagging regions are Nizhny Novgorod, Sakhalin, Vologodsk, and Tula oblasti, as well as in the Republic of North Osetia-Alania and the Aginsky Buryat AO.

²³ Federal Tax Service, http://www.nalog.ru/document.php?id=22664&topic=nal_statistik.

contested land taxes is likely to be similar), and (b) to educate the public about cadastral assessment.

Lessons for reformers

- The sequence of reforms was reasonable: first land cadastre was created and land value assessment carried out, followed by the creation of real estate cadastre. It is intended that a single real estate tax will replace the three property taxes currently collected.
- It took the Russian cadastral agency six years to implement cadastral assessment “from scratch.” This gives Chinese reformers a reference point, although it is not clear how quickly cadastral assessment of land in China will take. Obviously its territory is smaller, but the number of landholdings is much larger. On the other hand, China’s good economic performance is likely to generate resources – human and financial - for carrying out assessment.
- Implementation of land value taxation increased the revenue base of the local governments and boosted local revenue.
- As in Ontario, inflation has significantly affected property values and resulted in “unreasonably” high tax amounts.
- The rate schedule has been considerably substantially simplified.
- Because of the small size of land markets, it was impossible to base land value assessment on observed market rates. Mass valuation techniques have proved a viable substitute.

- Russia is facing a number of challenges: (a) complete real estate assessment, (b) continue building human capacity for assessment; (c) educate the public regarding ad valorem taxation, (d) improve dispute-resolution in relation to land taxation.

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Appendix 1

Transition Ratios, Revenue-neutral by Class.

Property Class	Matched Year-end 2005 CVA	2006 CVA	2005 General Tax Rates	Revenue Neutral 2006 Rates	Revenue Neutral Ratios	2006 Starting Tax Ratios
1. Residential	\$1,000,000	\$1,100,000	0.80%	0.73%	1	1
2. Multi-residential	\$500,000	\$550,000	1.00%	0.91%	1.247357	1.25
3. New multi-residential	\$0	\$0	0.00%	0.00%	0	0
4. Commercial (vacancy-adjusted total)	\$835,000	\$835,000	1.60%	1.60%	2.195349	2
5. Industrial (vacancy-adjusted total)	\$501,300	\$451,170	2.00%	2.22%	3.049096	2.5
6. Pipeline	\$10,000	\$10,200	0.60%	0.59%	0.807114	0.75
7. Farm	\$200,000	\$210,000	0.20%	0.18%	0.25	0.25
8. Managed Forest	\$100,000	\$110,000	0.20%	0.18%	0.25	0.25
Total	\$3,162,000	\$3,282,000				

Source: Government of Ontario (2006)

Appendix 2

