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New market-value based Property Tax in Germany?

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Agenda

Contents

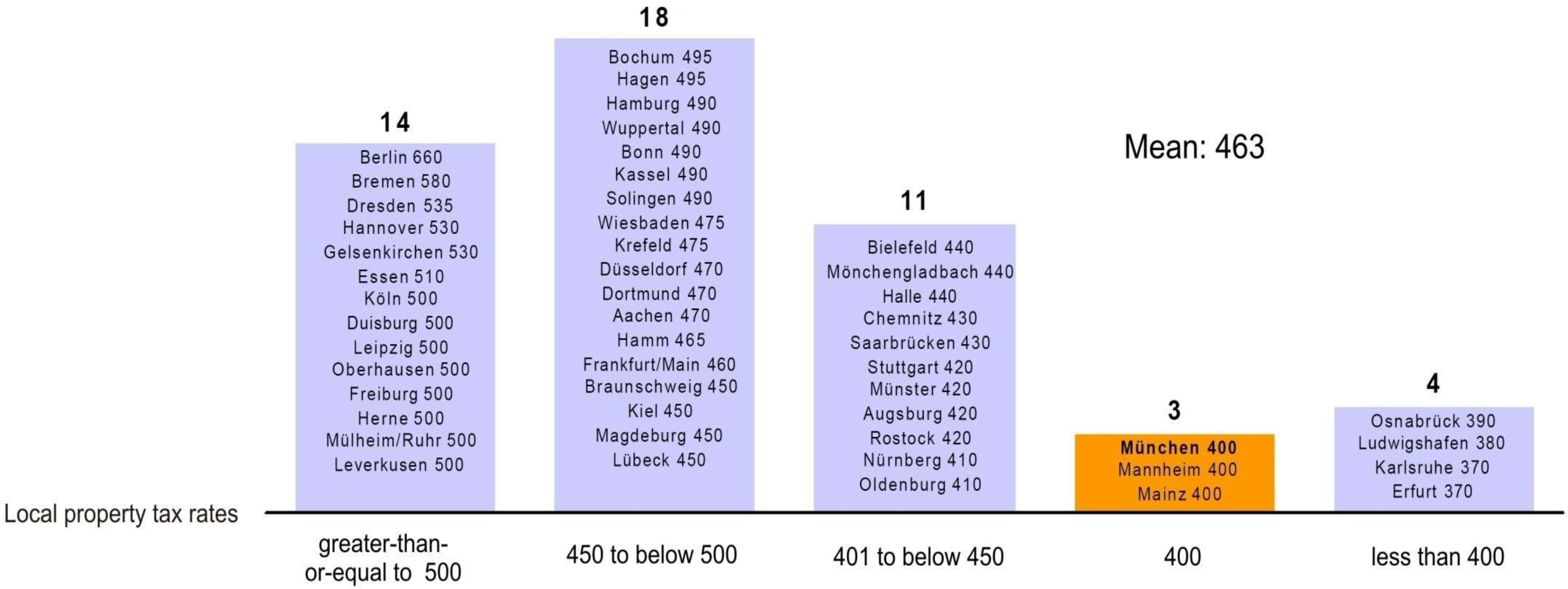
- Property Tax in Germany today
  - Determination of property tax
  - Valuation methods
  - Tax burden
- Criticism of the Federal Constitutional Court
- Reform models of property tax
- Matters of data and valuation
- Conclusions

Determination of local property tax in Germany

Unitary Tax Value (€)		
*		
Basic Federal Rate (‰)		2,6–3,5 ‰, different types of properties, fixed by Federal States
*		
Local Property Tax Rate (%)		2oo – 660 %, fixed by each municipality
=		
Local Property Tax (€)		

Local Property Tax today

Local Property Tax: Frequency of local property tax rates in 50 largest German towns



Source: http://www.ris-muenchen.de/RII/RII/DOK/SITZUNGSVORLAGE/622064.pdf am 16.06.2009

Short history of property-related taxes in Germany:

- 1925/1935: **Unitary Tax Value** was introduced (common tax base for all property-related taxes (Einheitswert))
- Till 1996 four taxes are based on the Unitary Tax Value
  - Local Property Tax (Grundsteuer)
  - Wealth Tax (Vermögensteuer)
  - Inheritance and Gift Tax (Erbschaft- und Schenkungsteuer)
  - Local Trade Tax (Gewerbekapitalsteuer)
    (Part 1: Real Assets + Part 2: Return of business)

- 1995: 1. Resolution of **Constitutional Court** referring to Inheritance Tax against Unitary Tax Value

- 1996: Wealth Tax and part 1 of Local Trade Tax were cancelled
- 1996 + 2009: Inheritance and Gift Tax has to be based on market values after 2. resolution of Constitutional Court 2006

Local Property Tax today

Determination of local property tax in Germany

Unitary Tax Value (€)

*

Basic Federal Rate (‰)

*

Local Property Tax Rate (%)

=

Local Property Tax (€)

Unitary Tax Value

- National legal basis:
  (Tax) Assessment Law
- Individual value per property
- 3 valuation methods,
  simplified assessment
- Valuation date:
  1.1.1964 (West)
  1.1.1935 (East)
- fixed by States Fin. Authorities
- high expenses in time and
  manpower

Assessment of Unitary Tax Value

Built-up properties:

– **Income capitalization method** (> 50 % of cases):
  rental income (1964) * capitalization rate (listed according to type, year, standard of building)
  + indiv. surcharges/ reductions = Unitary Tax Value
– **Replacement cost method** (if rental income is unknown):
  (ground value + construction cost (1964) + indiv. surcharges/ reductions) * factor = Unitary Tax Value

Unbuilt properties: Comparative method

Agricultural properties: Capitalization method according to standardized output from farming

Local Property Tax today

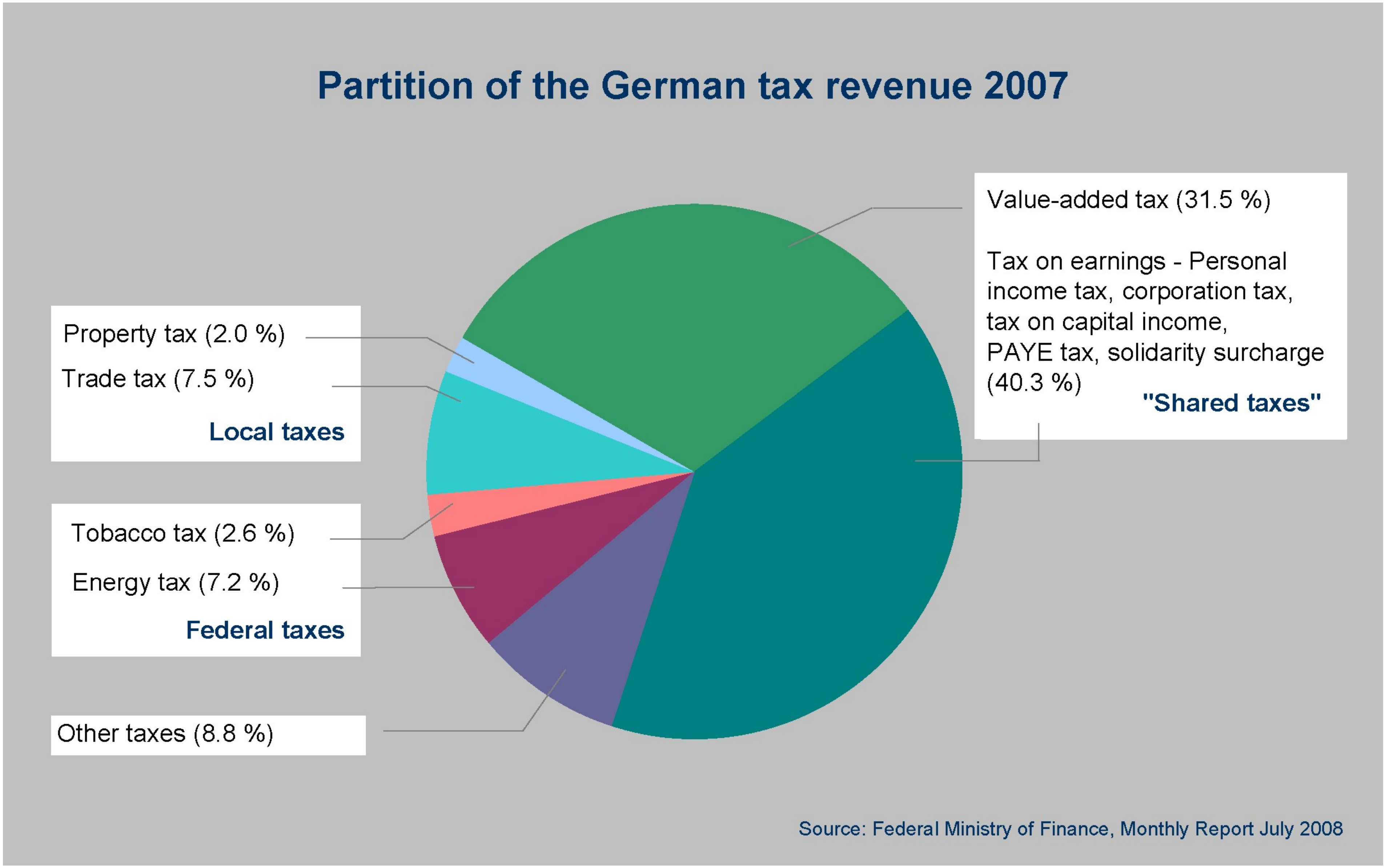
Example: Property Tax burden

Detached- 4-bedroom house, 150 m^2 living space, modernized, good quality

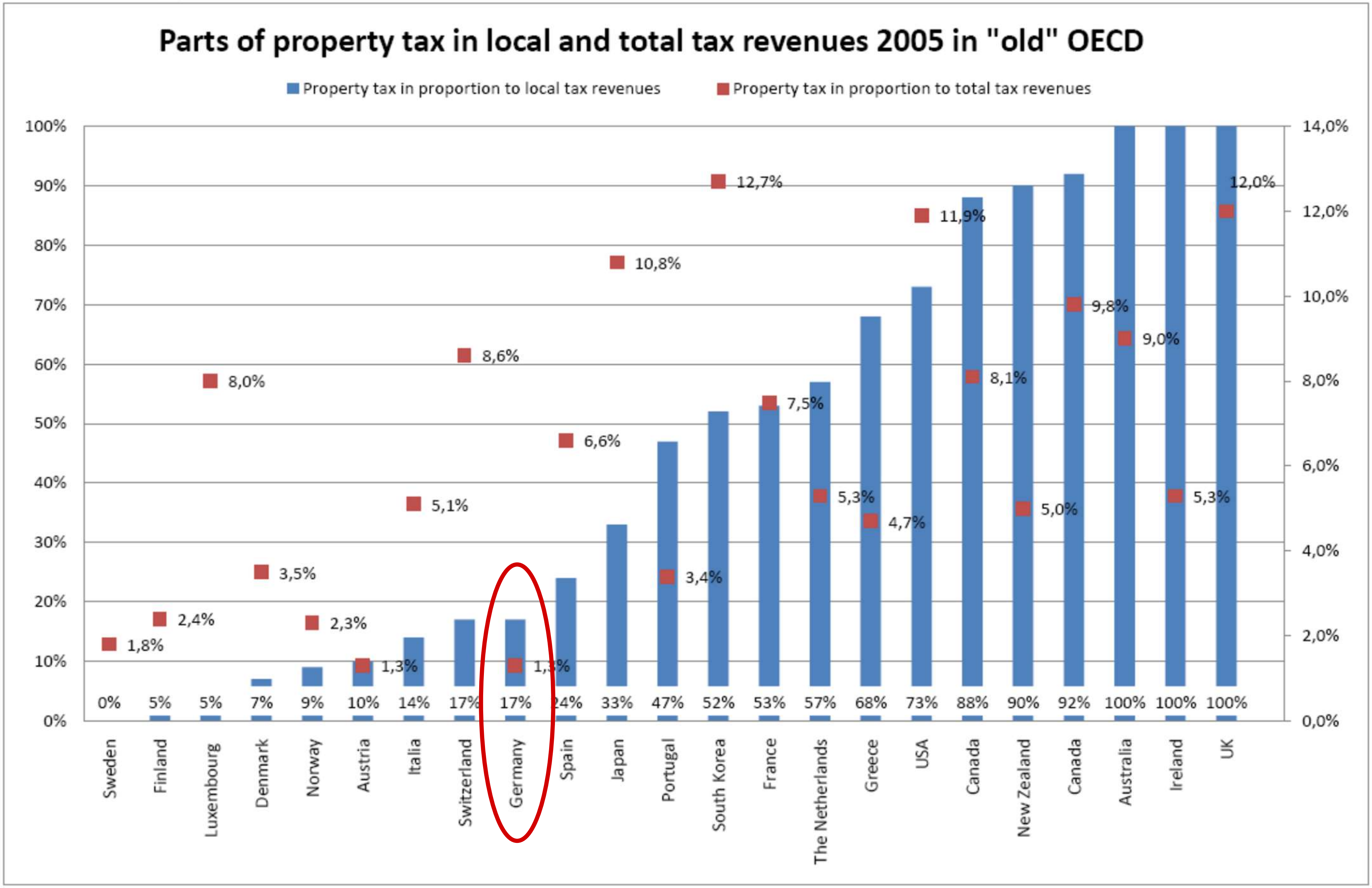
- Mid-centre-town in rural region (market value: 175.000 €)
  Local property tax rate: 360 %
  Property tax per year: 361 € (0,2 % of market value p. a.)

- Average 50 large cities in Germany (market value: 400.000 €)
  Local property tax rate: average 463 %
  Property tax per year: 650 € (0,16 % of market value p. a.)

Local Property Tax today



Local Property Tax International

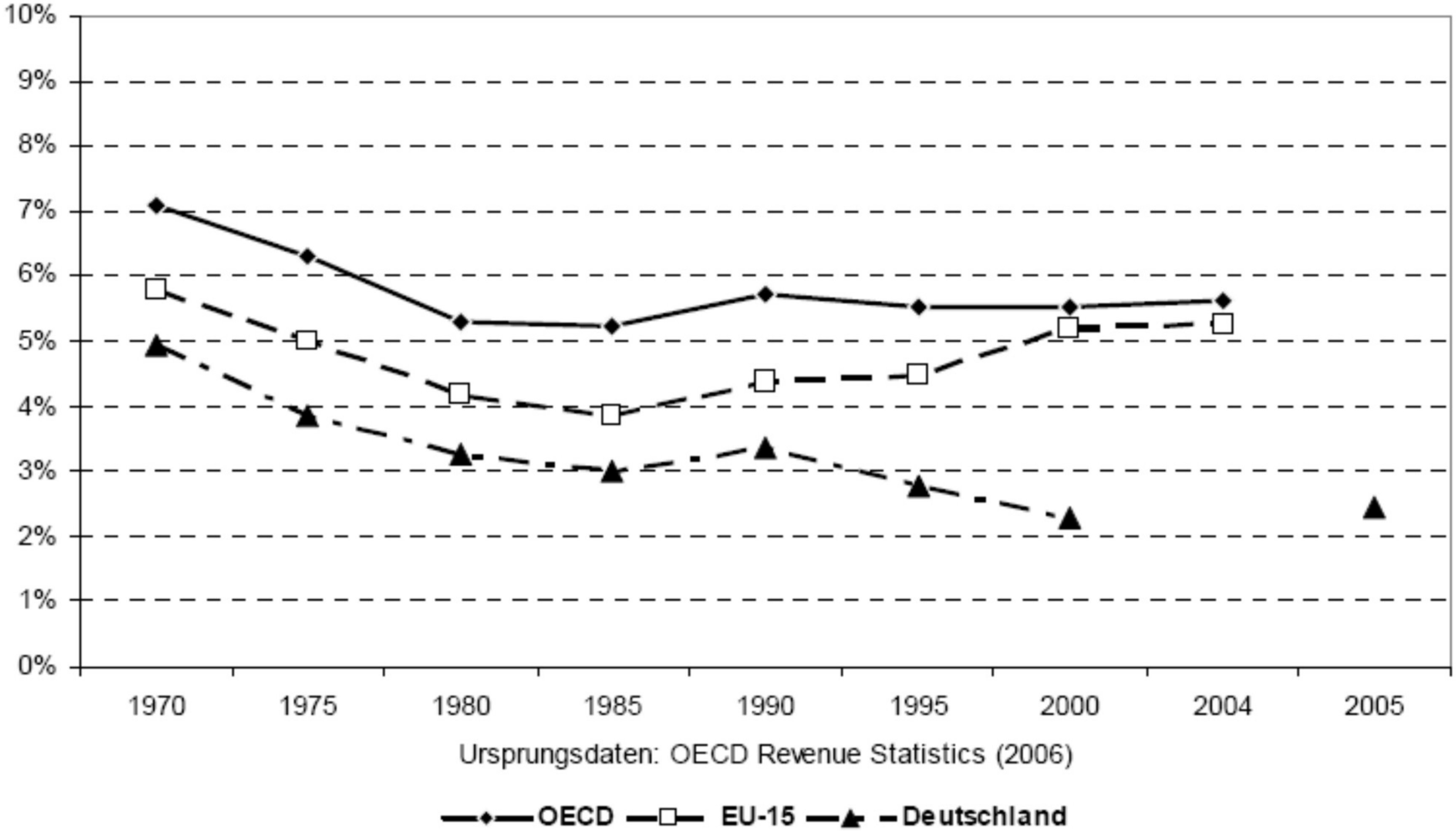


Source: Fuest/ Thöne: FiFo-Institute of Public Economics, University of Cologne, Berichte Nr. 10, Köln 2008

Local Property Tax International

<u>Tax revenue from asset-relevant taxes</u>

in proportion of total tax revenues (1970-2004/5)



Source: Fuest/ Thöne: FiFo-Institute of Public Economics, University of Cologne, Berichte Nr. 10, Köln 2008

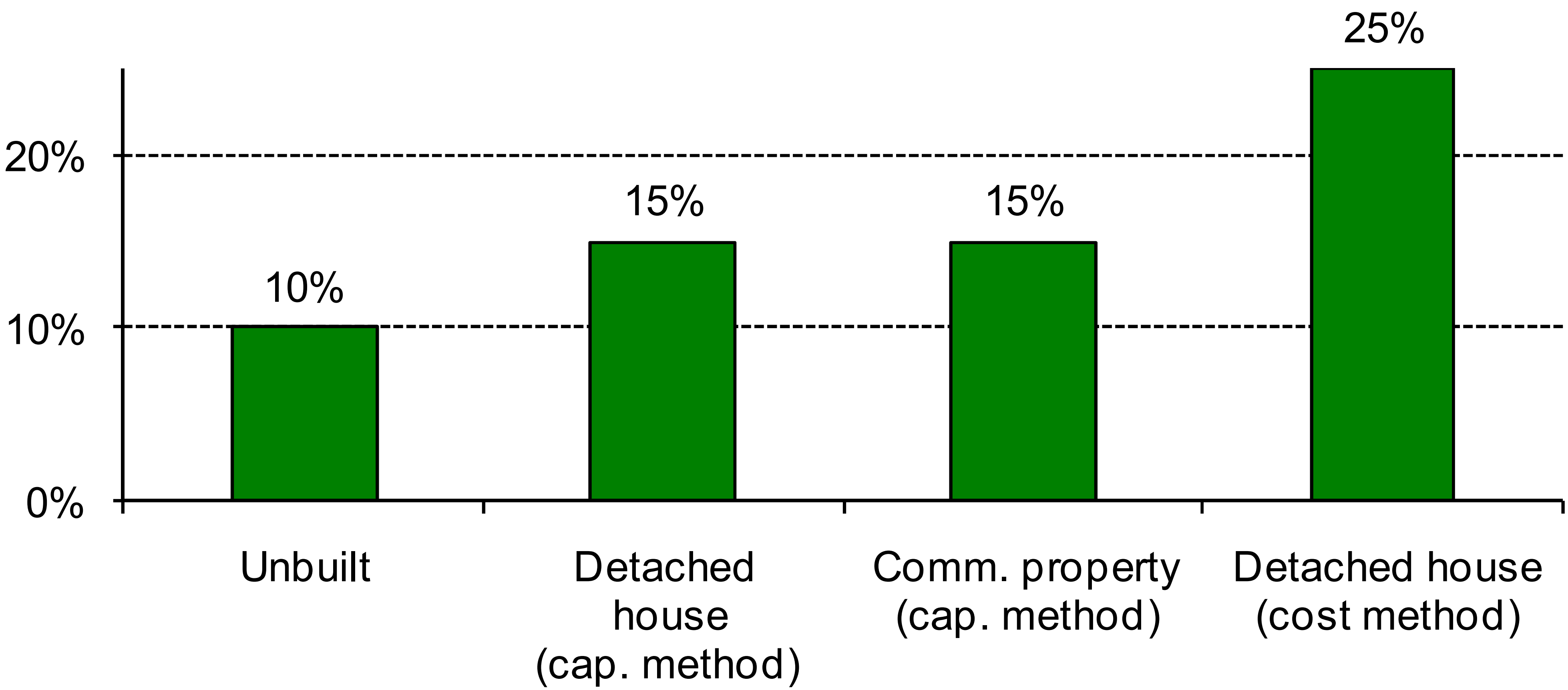
Resolutions Federal Constitutional Court

- Resolutions in 1995 and 2006 affected Unitary Tax Value referred to Inheritance Tax and Wealth Tax.
- Problem: Tax burden of property assets less than of other assets (e. g. shares, savings, obligations). Assets have to be taxed according to their real value; assets in property may not be preferred.
- Reasons: Valuation date obsolete; some valuation rules of Assessment Law do not lead to market value.
- In 2006 the Federal Constitutional Court requires a tax base for Inheritance Tax according to market value.

Resolutions Federal Constitutional Court

Discrepancies to Market Value

Average proportion of Unitary tax values to Market values



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Aims of property tax reform

New Property Tax

Requirements discussed to be met by a new property tax:

1. Simplification of adminstrative process (financial authorities)

2. Acceptability of the new tax, i.e. tax redistribution following the current tax burden (politicians, financial authorities)

3. Fairness of the tax distribution, i. e. accuracy of the valuation (financial authorities)

4. Land policy effects, e. g. mobilization of land used inadequately (planners, land managers)

„Value-related model“

Model B (2001)

Property Tax amount (€)

=

[**Standard ground value** (€/m²) x **Plot size** (m²) x Percentage

(70% built-up land/ 100% not built-up land)

+

Standardized building value (€/m²) x **Floor space** (m²) x **Age reduction**]

(1% p. a., max. 50 a)

x

Basic federal rate (0,001 not built-up land/ 0,0005 built-up land)

x

Local property tax rate (%)

Standardized Building Values

Average values of new buildings (proposal to model B)

Type of building	Standardized building value € / m²
Commercial used buildings	
Office buildings, department stores, banks, hotels etc.	1000
Manufacturing buildings, warehouses, market buildings, supermarkets, parking garages etc.	400
Light premises (e. g. sports)	200
Residential used buildings	
Detached, semi-detached and terraced houses	800
Multi-storey houses, condominiums, holiday houses	600

Source: Reform der Grundsteuer. Bericht des Bayerischen Staatsministers der Finanzen und des Ministers der Finanzen des Landes Rheinland-Pfalz an die Finanzministerkonferenz, 2004

„Land value-related model“

Model C

Property Tax amount (€)

=

Standard ground value (€/m²) x 80% x **Plot size** (m²)

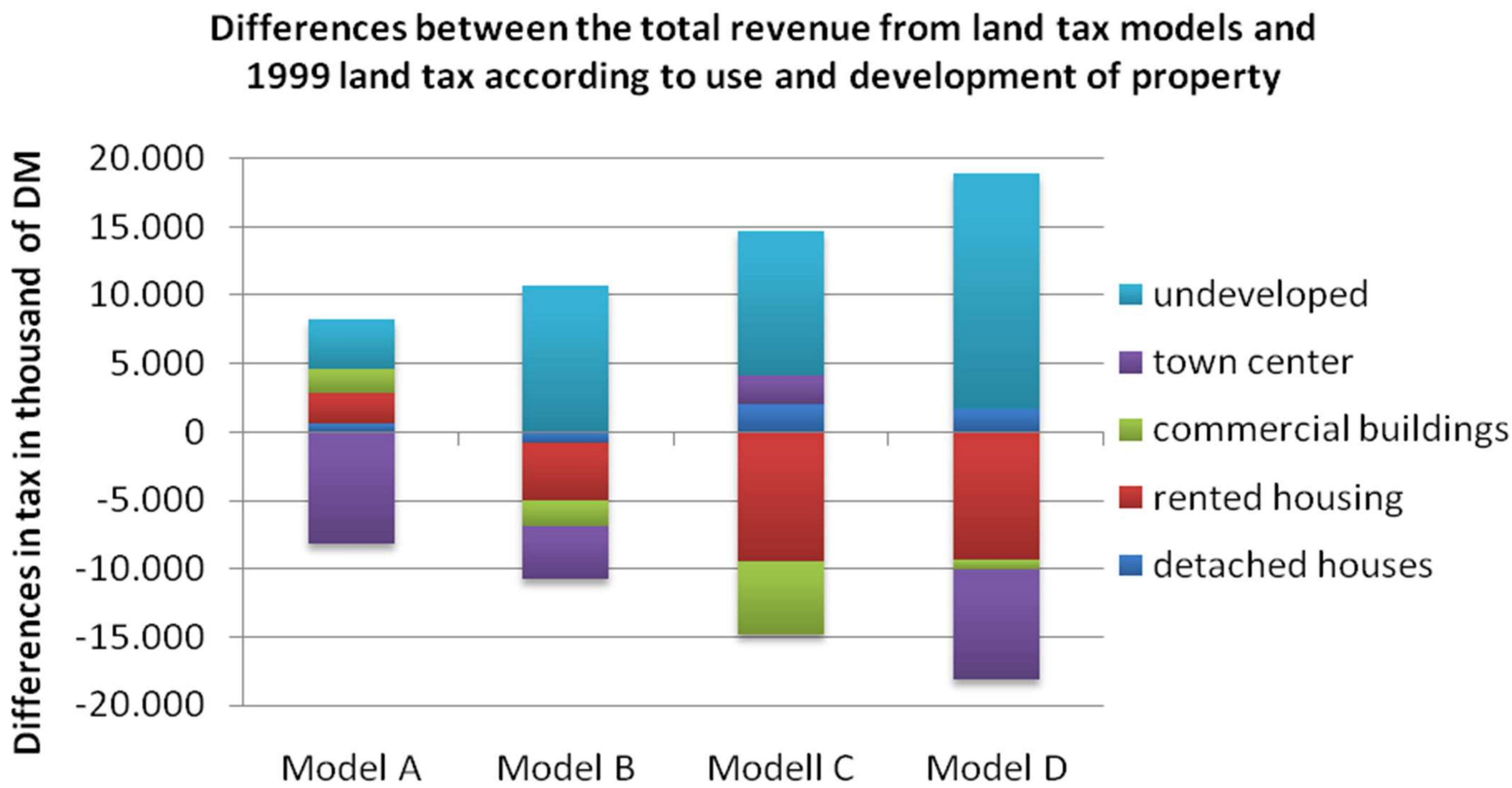
x

Basic federal rate (0,001)

x

Local property tax rate (%)

Property tax reform



N_{hoch} = 86.466, with calculated revenue-neutral municipal percentage.
Scource: Difu survey of land tax in 2000

Necessary data	Model **A** (area-related)	Model **B** (2001) (value-related)	Model **B** (2004) (value-related)	Model **C** **(**land value related)	Model **D** (combined model)
Standard ground value		**X**	**X**	**X**	**X**
Plot size	**X**	**X**	**X**	**X**	**X**
Floor space	**X**	**X**	**X**		
Standardized building value		**X**	**X**		
Age of building or construction year		**X**			
Results Aims 1 – 4:	**2: +**	**2: +** **3: +** **1: --**		**1: +** **4: +**	**1: +** **4: +**

Example: New Inheritance Tax

Inheritance Tax: Consequences in Assessment Law

- 1997: assessment rules changed (approach to market values):
  - Proportion to market value raised (50 %, single cases up to 120 %)

- 2006 resolution of the Constitutional Court:
  - New rules do **not meet the requirements** yet

- 2009: New Assessment Law requires market value now!
  - Assessment rules refer to **Federal Valuation Ordinance** (WertV)
  - Results of **Valuation Expert Committees** shall be used in a wide range; completion and standardization of their results is necessary

- Is this the way property tax reform should go?

Solution: Automated valuation ?

Mass valuation with automated price calculation

Two types are proved and in use:

- Online-real-estate-price-calculator (IPK) in Lower Saxony
  - Calculation is based on regression analysis for local districts and for different types of residential properties
- Standard-property-price-information-system (IRIS) in NRW
  - Database search allows selection of comparable purchase prices and the valuated property can be adopted

- Automated calculation of the current approximate value is possible for an individual residential property with 4 data:
  - Location / address: connection to standard ground value database
  - Plot size
  - Year of construction of the premises
  - Living space/ floor space of the premises.

Conclusions

- Reform of Germany's local property tax is necessary.
- A 100%-tax model could not be found yet; the government-prefered model is detailled, requires better data and is more expensive.

- Political decision is necessary about a generell increase of property tax burden, the shifted types of property and the use of land policy effects.
- Valuation can be supported in a wide range by the Valuation committees (data base, experience)
- Automated valuation is a solution to keep expenses reliable if
  - results approach market value (20 – 30 %) and
  - necessary data can be made available easily.
  - In some countries such property tax systems are in operation.

- Good opportunity for valuers and market valuation in Germany.

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THANKS FOR YOUR ATTENTION!

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