



# The Effect of Potential-based Land Tax on Land Utilization

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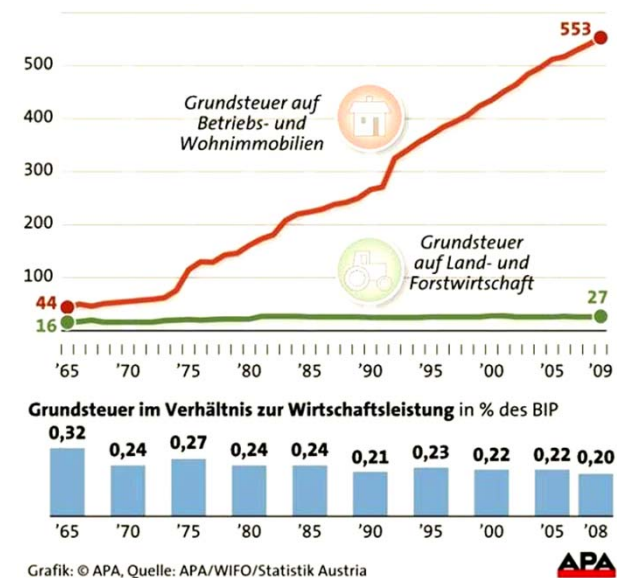
# Introduction (1)

Property tax has a long tradition

**Advantage:** Land cannot be transferred to other countries → stable source of income

Importance reduced with industrial revolution

More tax revenues on buildings than on land



# Introduction (2)

Land tax in Austria based on unit value

Developed in the 19<sup>th</sup> century for agricultural land

Unit values not adapted to market changes →

Austrian Highest Court required adaptation (VfGH, 2012)

Chance for change of approach?

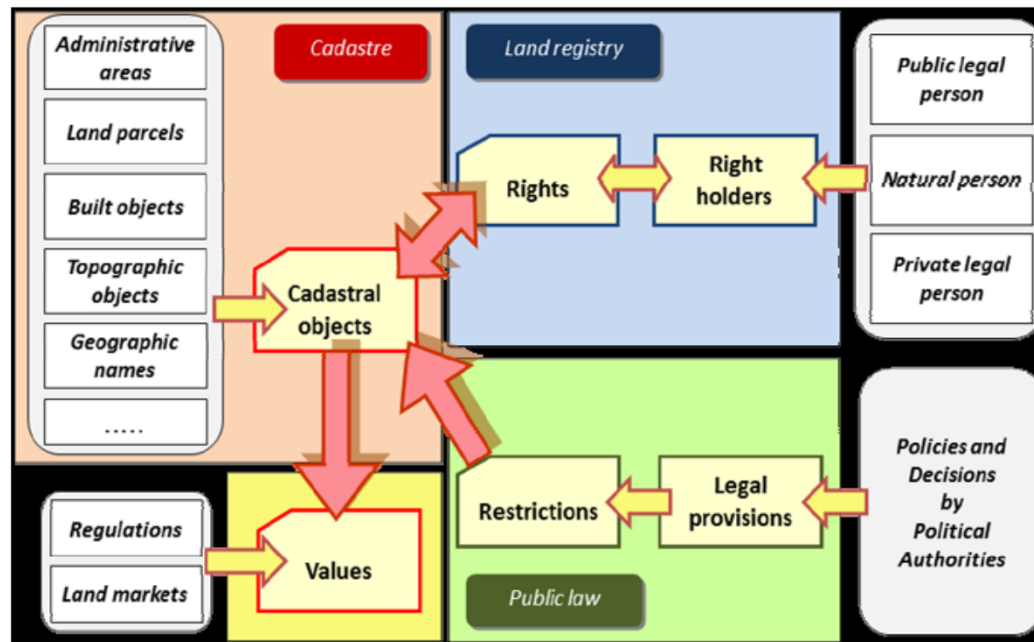
Potential-based land tax?

**What would be the effect?**

# Land Administration

Basic processes that provide information on available resources

Information used in management processes



(Horisberger, 2011, as cited in Muggenhuber et al. 2011)

# Property Tax (1)

*“The property tax is, economically speaking, a combination of one of the worst taxes - the part that is assessed on real estate improvements ... - and one of the best taxes - the tax on land or site value”* (Vickrey 1999: 17)

Land tax shall relate to the location value of land instead of the value of improvements (George & Drake, 1879)

# Property Tax (2): Policy

Several goals (Muggenhuber & Twaroch, 1998)

- **Guidance:** High land tax may motivate land owners to sell land, which they do not need.
- **Distribution:** reallocate wealth
- **Income**

Tax assessment should be

- **Objective**
- **Fair**

# Property Tax (3): Austria

Land tax based on unit-value (last complete survey done in 1973)

Unit-value determined by

- soil quality
- availability of water, and
- climate

Improvement of land does not influence land tax

Does not work properly in complex situations like built environments



# Property Tax (4): Reform Idea

Value of land is an objective criterion

Reflects the wealth of the land owner → it is also fair

Market value is based on different factors including general economic situation, location, and potential use

Mass appraisal can provide good estimates of market value

# Potential-Based Land Value (1)

*“Fair market value”*: Definition by International Accounting Standards Board (IASB) – included *“highest and best use”* as an element for determining the market value in 2013

Parameters applied to the definition of “highest and best use” are:

- The potential use is legal.
- The potential use is physically, economically and financially feasible.

Value: potential use fully exploit, regardless to the current use.

# Potential-Based Land Value (2)

Austria has data sources suitable to determine land value (Muggenhuber et al., 2013), e.g.,

- physical and geometrical properties
- private law or public law restrictions

No new data needs to be collected!

# Effects of Potential-Based Land Tax:

## Economic considerations

- Land is wasted, if the potential is not used
- Investors may hope for increasing value – no intention to use or improve the land
  
- Land tax based on market value will be fair
- Decreasing land value automatically reduces tax burden
- No data acquisition – setup is cheap (re-use)

# Effects of Potential-Based Land Tax: Ecological considerations

- Better use of resource land – contribution to sustainability of our eco-system
- Avoidance of unnecessary infrastructure for not utilized properties

# Effects of Potential-Based Land Tax: Political and social considerations

Transparency is one of the key aspects of good governance (UN 1996):

- Effects of decisions in spatial planning become evident (= change in value)
- Costs of public law restrictions like national parks assessable

Is it fair that land owners pay higher tax if the value increases?

- NO, if increase based on improvement by land owner
- YES, if increase based on public investment

# Conclusions

- Land tax in Austria currently not fair!
- Potential-based land tax
  - “punishes” land owners, who do not exploit the full potential
  - provides automatic compensation for loss in value
- Mass appraisal systems document the financial effects of political / spatial planning decisions