Property Taxation Challenges in Post-Apartheid South Africa

The Lincoln Institute has supported the authors' work on property taxation in South Africa for several years, and in February 2002 the Institute published *Property Taxes in South Africa: Challenges in the Post-Apartheid Era*. Edited by Bell and Bowman, the book presents major portions of their own work, together with chapters by several of their colleagues in the U.S. and in South Africa. This article provides an overview of seminars on property tax issues conducted by Bell and Bowman in South Africa in March 2002.

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The end of apartheid in South Africa nearly a decade ago presented new opportunities and challenges to every aspect of national life, including fiscal issues. The government faced the task of extending the property tax to previously untaxed areas and adapting it to provide services through a set of radically restructured local governments. The final reorganization of local government took effect in December 2000, and the new governments now must develop comprehensive property tax (rates) policies.

Several key pieces of apartheid-era legislation had established the spatial basis for racial separation:

- ***Natives Land Act of 1913:*** Adopted soon after formation of the Union of South Africa in 1910, this law outlawed black ownership or leasing of land outside reserves established for blacks.
- ***Population Registration Act of 1950:*** Often termed the cornerstone of apartheid, this statute established categories to which people would be assigned: white; black or bantu; colored, for people of mixed race; and later, Indian. This classification scheme made enforced racial separation possible.
- ***Group Areas Act of 1950:*** This law instituted strict racial separation in urban areas, providing zones that members of only one racial group could occupy and limiting the presence of blacks in restricted areas to short time periods. A pass system required nonwhites to carry identifying papers or permits.

These policies greatly complicated efforts to amalgamate former white and black local authorities (WLAs and BLAs), with important implications for property taxation. Specifically, for local governments, the legacy of apartheid includes:

- skewed settlement patterns with the geographic and social segregation of residential areas;
- extreme concentrations of wealth and property tax base, since commercial and industrial activity was located almost exclusively in the former WLAs;
- large areas and numbers of people in BLAs, which had inferior infrastructure and a backlog of demand for public services under amalgamation; and
- nonviable municipal institutions—small rural townships, known as R293 towns, close to the borders of former bantustans (black homelands or traditional authority areas) that have large populations, limited financial resources and only a minimal level of services.

Post-Apartheid Local Government Structure

The dismantling of apartheid began in the mid-1980s and was essentially complete by the early 1990s. At the end of 1993, the Local Government Transition Act (LGTA) was signed by then-President de Klerk and, symbolically, by Nelson Mandela, leader of the African National Congress (ANC). The LGTA provided for short-, medium- and long-term transformation of local governments to create nonracial self-government. It created two-tier local governments in metropolitan areas, with powers and responsibilities shared between a geographically larger unit and two or more smaller units within the same area. The Municipal Structures

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Act of 1998, providing for single-tier metropolitan government, was implemented after the local elections of December 2000 as part of a general and final redemarcation of local governments that reduced the number of authorities from approximately 845 to less than 300.

Amalgamation of municipalities brought new areas into the property tax base, including former BLAs, bantustans and their associated rural R293 towns, but the residents of these newly incorporated areas had never before paid property taxes. Thus, it was necessary to develop the information and administrative infrastructure needed to value properties, determine tax liabilities, distribute tax bills to those responsible, and collect the taxes due, all in an equitable manner. Moreover, the new tax system had to overcome the psychology of payment boycotts, sometimes characterized as a "culture of nonpayment," an important resistance technique used against the apartheid government.

Combining formerly taxed areas with different valuation rates or systems into a single municipality produces inconsistencies within the property tax roll of the amalgamated area, multiplying inequities among property owners with different effective tax rates. Both those new to the tax and those who historically have paid property taxes often question whether their tax shares are equitable and how the resulting revenue is being spent. In some instances, tax boycotts have occurred in former WLAs.

National Property Tax Policy

Although property taxation remains a local tax in South Africa, the 1996 Constitution authorizes central government regulation of property taxation. A national Property Rates Bill, scheduled for adoption in 2002, will replace current provincial property tax laws. Each locality now must adopt an explicit and comprehensive property rates policy.

Our seminars took place in this context of national legislation, municipal consolidation and municipal property rates policies. We collaborated with local institutions of higher education: Port Elizabeth Technikon in Nelson Mandela Metropolitan Municipality and the University of North West in Mafikeng Local Municipality. Seminar participants included current and former elected city councilors, newly enfranchised and long-time non-elected officials, and students and faculty of the educational institutions.

Nelson Mandela Municipality is one of South Africa's six metropolitan municipal governments, the only local government within its geographic area. Its population and business center is the former city of Port Elizabeth. Principal property tax concerns raised at the seminar included: (1) unifying the tax rolls of the various jurisdictions making up the metropolitan area, since their valuation dates range over a number of years; (2) bringing former black local authority (BLA) areas into the property tax base; (3) deciding on the appropriate way to deal with rural (agricultural) land, previously not taxed but now part of the municipal area; and (4) accomplishing these things in a manner that is sensitive to the special circumstances of those with very low incomes.

Mafikeng, the capital of the North West Province, lies within the Mmbatho District Municipality in the former Bophuthatswana homeland near the Botswana border. Some property tax concerns raised at the Mafikeng seminar were the same as in Nelson Mandela Municipality. In addition, Mafikeng is wrestling with incorporating tribal (traditional authority) areas and the black urban agglomerations (R293 towns) of the former bantustan. Tribal areas present two special problems: property ownership is communal, not private; and the traditional authority structure remains in place, even though these areas now are included within municipal borders, creating a dual authority structure that further complicates amalgamation.

Key Property Taxation Themes

Policy Framework

New national legislation requires each local government to produce a property rates policy to address such issues as whether to include all real properties in the tax base; whether to apply uniform or differential rates to the many categories of property included in the tax base; and what form of property relief should be given, and to whom. If the property tax is to be a viable local revenue source, local rates policies must be guided by the following principles:

- ***Legitimacy.*** Taxpayers must accept the tax as a legitimate, appropriate levy. This means administrative outcomes must be in accord with accepted legal requirements.
- ***Openness.*** The tax must be transparent, so taxpayers can understand its workings. Further, a simple, low-cost means must be available to resolve taxpayers' complaints.
- ***Technical Proficiency.*** The tax must be administered in a professional manner. This requires appropriate administrative structure, tools, and personnel.
- ***Fairness.*** The tax must be administered in a manner that treats taxpayers uniformly and fairly with regard to asset value, but with provisions for relief that take into consideration broader notions of ability to pay, such as current income.

These fundamental characteristics of a property tax system provide a framework for restructuring property taxes in South Africa, with tradeoffs made through an open and transparent political process at the local level.

Monitoring

The property tax base is fair market value. Because most properties do not sell in a market transaction each year, however,

TABLE 1 Level and Uniformity of Residential Property Assessment in South Africa, Selected Localities, Mid-1990s

	Assessment/Sales Ratio		
Jurisdiction (n)	**Median**	**CD (a)**	**PRD (b)**
Johannesburg (75)	125.0	47.0	1.256
Cape Town (15)	8.0	46.7	1.333
Witbank (150)	75.0	25.7	1.068
King William's Town (32)	51.5	15.4	1.003
Bisho (12)	88.9	16.7	1.005
Oyster Bay (32)	91.0	24.6	1.047
Seafield (41)	86.0	55.3	1.306
Seaview (23)	80.0	24.9	1.132

(a) CD = coefficient of dispersion, the average absolute deviation of individual-parcel ratios from the median ratio, expressed as a percentage of the median ratio.

(b) PRD = price-related differential, the ratio of the mean ratio to the aggregate ratio.

Source: Adapted from Bell and Bowman (2002, 84) estimating market value is the task of trained assessment professionals. Differences in location, depreciation and other characteristics make valuation partly an art, not strictly a scientific or technical endeavor. Uniformity relative to market value may not always result, even though it is required and the assessors follow the procedures intended to achieve that result. Thus, a system for monitoring valuation outcomes is needed, which may include three dimensions of assessment quality:

- The overall closeness of the fit between assessed value on the tax roll and actual sales price for properties that have sold. A measure of central tendency of such ratios for a sample of properties indicates the average assessment level relative to market value; the median ratio generally is preferred.
- The extent to which assessment ratios for individual properties are scattered or clustered around the median ratio. A standard measure of assessment uniformity is the coefficient of dispersion (CD), which is interpreted as a measure of horizontal equity. A CD greater than zero indicates that different properties may bear different effective property tax rates even if they have the same market value and are subject to the same nominal tax rate.
- Vertical equity, evaluated by the price-related differential (PRD). If the PRD = 1, there is no systematic bias in favor of either high- or low-value properties, while a PRD above 1 reveals a regressive bias favoring high-value properties.

Formal assessment/sales ratio studies have not been done in South Africa, but we calculated simple ratios for several cities. The results in Table 1 indicate that assessment uniformity generally needs to be improved, since coefficients of dispersion across the case study cities are typically high and the price-related differentials are generally substantially above one.

Targeting Tax Relief

Although property taxation is a tax on value, it is paid out of current income, and thus may place an unacceptable burden on property owners with low incomes. Property tax relief is any reduction in tax liability. Indirect relief results from changes that take pressure off the property tax: reduced expenditures or increased revenue from alternative sources. Alternatively, direct relief comes from a change in the calculation of property tax liability.

Direct relief was the focus of our studies and the seminar discussions. In South Africa direct residential property tax relief typically is a uniform percentage credit, termed a rebate, which generally is 20 percent or 25 percent of gross property tax liability. The rebate approach has two limitations. First, most of the tax relief goes to those with the most expensive properties. Second, low-income property owners are still required to pay most of their property tax liability, which still could be burdensome relative to income.

While an income-based circuit breaker is our preferred approach for targeting tax relief to those in need, it would be extremely difficult to administer in South Africa because income information is not readily available, in part because of the extensive informal economy. An alternative way to target property tax relief to those most in need is to exempt a fixed amount of the base from taxation.

Table 2 illustrates the effects of moving from a 25 percent rebate to a R20,000 exemption (US$1,740). Under the partial exemption alternative, the lowest valued properties, including those hardest to value at this time, are removed from paying taxes, and net taxes are reduced on all properties up to about R100,000 (US$8,700). The aggregate cost of property tax relief under this approach is substantially reduced because each property receives the same exemption. Durban and Johannesburg now are experimenting with the partial exemption approach to property tax relief.

TABLE 2 Residential Tax Relief Alternatives: Comparison of Uniform Percentage Rebate with a Credit Equal to the Tax on a Specified Amount of Value, Hypothetical Data by Property Value (Amounts in rands, South Africa's currency unit)

Property Value	Gross Tax at 0.9% Rate	25% Rebate		Credit on Value = R20,000	
		Net Tax	Relief	Net Tax	Relief
15,000	135	101	34	0	135
25,000	225	169	56	45	180
50,000	450	338	112	270	180
150,000	1,350	1,012	338	1,170	180
500,000	4,500	3,375	1,125	4,320	180
2,000,000	18,000	13,500	4,500	17,820	180

Note: In the rebate example, amounts have been rounded to the nearest whole rand, rounding down/up if .5 follows an even/odd number. The credit is the amount of tax on R20,000 (R20,000 x 0.9 percent = R180), equivalent to exempting R20,000. In 2002, US$1 equals approximately R11.5.

Source: Adapted from Bell and Bowman (2002, 154)

Dealing with Previously Untaxed Areas

As a result of the local government restructuring in December 2000, South Africa now has local governments throughout country. Three types of areas previously outside the property tax now are to be brought into the tax: former BLAs and R293 townships, agricultural areas and tribal areas. In the former BLAs and R293 townships property is being transferred to private ownership and these areas must be surveyed by the national Surveyor General to establish individual property boundaries and identifications necessary to administer the property tax. Different localities are at different stages in this process.

Property taxes were levied on rural agricultural lands in the past, but these lands have not been in the property tax base since the late 1980s. Bringing them into the tax base now poses two problems. The first is developing the property record information necessary for tax administration. The second is the question of how taxes on such properties should relate to taxes levied in the urban portions of a municipality, as farmers often provide themselves and their workers with services typically associated with local government. One possibility is use-value assessment of agricultural land, an approach endorsed by a national commission that reviewed the taxation of rural lands. Alternatively, differential rates for different categories of property are allowed under current provincial property tax laws and the draft national Property Rates Bill. If there is to be differentiation in effective tax rates, imposing a lower rate on market value assessments provides greater transparency and understanding of the tax and should be part of the local government rates policy.

Bringing tribal areas into the tax base presents another set of issues. First, given communal land tenure systems existing in these traditional authority areas, how does one establish ownership, a necessary condition for the application of property tax based on the principle of private property? Second, because there is no land market per se, how are estimates of market value to be made? Finally, given the two competing governance structures that now exist in tribal areas, how does one make the payment of a property tax acceptable to residents who did not previously pay the tax? These issues are clearly the most intractable ones that must be addressed in the newest round of local government reform in South Africa.

Conclusion

The property tax has been an important part of local finance in South Africa for centuries and is likely to play an increasingly important role in the future, as newly amalgamated local governments wrestle with addressing the legacies of apartheid and the requirements of new national property tax legislation. There is no single right answer to many of the perplexing questions surrounding the design and implementation of a local property tax, but it will continue to evolve to meet changing circumstances and needs.

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■ REFERENCES

Bell, Michael E. and John H. Bowman. 2002. Property Taxes in South Africa: Challenges in the Post-Apartheid Era. *Cambridge, MA: Lincoln Institute of Land Policy.*

Brown Receives NAHB Honor

Lincoln Institute President Jim Brown was inducted into the National Association of Home Builders (NAHB) National Hall of Fame on June 8. In the ceremony in Washington, DC, Brown was described as "an internationally acclaimed academic with a heart for housing" and someone who "believes that each individual's access to land and an affordable home is the key to the quality of life…a belief that inspired him to fight fiercely for policies that would put home ownership within the reach of more Americans." The official program also noted that "as President and CEO of the Lincoln Institute of Land Policy, Brown continues as a preeminent spokesperson on land and tax issues that will increase housing opportunities for future generations."

David C. Lincoln Fellowship Applications Due by September 17

The Lincoln Institute of Land Policy invites applications for David C. Lincoln Fellowships in Land Value Taxation, a program designed to develop academic and professional interest in land value taxation through support for major research and curriculum development projects. The Fellowship honors David C. Lincoln, chairman of the Lincoln Foundation and founding chairman of the Institute.

Projects may address either the basic theory of land value taxation or its application to domestic or international issues, with an emphasis on specific investigations, case studies and theoretical work rather than general discussions of land valuation and taxation principles. The research may deal with land value taxation from the perspective of economic analysis, legal theory and practice, political science, administrative feasibility, valuation techniques, or other approaches in order to achieve a better understanding of its possible role as a component of contemporary fiscal systems.

The Institute invites proposals from scholars whose work has not previously addressed these issues. Funding for each approved project is between $20,000 and $40,000 per year, and may be renewed to support projects up to three years in length. As part of the Fellowship program, recipients present a seminar at the Lincoln Institute and attend a symposium with other current Fellows.

The application deadline is September 17, 2002, and Fellowship awards will be announced by November 15, 2002. For more information and application guidelines, see the Lincoln Institute website at www.lincolninst.edu or send email to rfp@lincolninst.edu.