

PECULIARITIES OF THE IMMOVABLE PROPERTY TAX POLICY FOR SUSTAINABLE DEVELOPMENT IN LATVIA

Sanda Geipele, Tatjana Tambovceva
Riga Technical University, Riga, Latvia

Abstract

Economic, political and social development of each country is determined and affected by its ownership of real estate resources – land, natural resources, buildings, structures, etc. Real estate is one of the most important economic resources and one of the essential components of national wealth. Immovable property tax is a very important component in the economy of each country. It is paid for each immovable property that is at one's ownership, possession or lease. The aim of the research is to evaluate peculiarities of changing immovable property tax from which it can be concluded that introduction of this taxation will significantly influence the development of real estate market and secondary - the economy of the country as a whole. Thus the further studies are closely related to the in-depth analysis and evaluation of socio economic system that will serve as the basis of the development of sustainable social economical model of real estate of Latvia.

Key words: real estate resources, tax policy, real estate market, sustainable development.

Introduction

The mission of a country is to implement a macroeconomic policy that ensures a high level of employment, welfare of the population and economic growth of the country. By using the financial policy, a country can ensure macroeconomic stability, which is one of its most important basic tasks.

The economic recession in Latvia can be attributed to the unfavourable banking credit policy, the marked unavailability of money resources both in the public and in the private sectors and the high level of unemployment, as well as the low purchasing power of the population. According to the macroeconomic and state budget report prepared by the Ministry of Finance, at the end of September 2010 the public debt in accounting value was LVL 4717 billion. In 2009 the indicators of implementation of the state budget were influenced significantly by the situation in the local and the international finance market and trends in the recession of the Latvian economy. According to the Central Statistics Bureau (CSB) data, the GDP in comparable prices in the 3rd quarter of this year if compared to the corresponding period of the previous year increased by 2,7%. This was the first quarter since the 1st quarter of 2008 when the GDP increase is to be estimated as moderately positive.

Information has already been published in the mass media that starting with 2011 new changes in taxes are expected part of which have already been widely disclosed and discussed previously, but another part the effects

of which will be felt by a large share of Latvian taxpayers has possibly been missed by the majority of the public.

From 2010, immovable property tax for living spaces – apartments and private houses – is to be paid. Until 1 January 2010 immovable property tax of 1% had to be paid only by owners of land and commercial areas. As from 1 January, the tax on land and commercial areas has been increased to 1,5% of the property's cadastral value.

On the basis of the above, the *aim* of the research is to evaluate the peculiarities of the immovable property tax policy in Latvia.

In order to achieve the set purpose, the following *tasks* have been defined:

1. To find out the meaning of the concept of immovable property and the subject of immovable property tax;
2. To investigate the conditions of application of immovable property tax and develop proposals for improvement of the immovable property tax policy for sustainable development in Latvia.

The topicality of the research is to be linked with comprehensive analysis and evaluation of the existing socio-economic system. Hence it is to be concluded that further increase of tax rates in the country would influence negatively the future course of recovery of the national economy by damaging the business and investment attraction environment where a predictable tax policy is a very important factor.

1. The concept of immovable property and the subject of immovable property tax

Single registration of immovable properties in Latvia is carried out by the State Land Service in accordance with the Immovable Property State Cadastre Law of 1 December 2005 of the Republic of Latvia. Registration is subject to all immovable properties located in the territory of Latvia irrespective of their ownership.

The State Land Service registers immovable properties as a set of objects of immovable property, units of land, buildings, premises groups, parts of units of land and their characterising data (including the type of use of the land and changes thereof) in the Cadastre Information System [5].

In defining the concept of immovable property, it is necessary to apply actively the experience of various countries having a developed market economy.

In the world's literature the meaning of the concept of immovable property is defined as land and all the related improvements which are corroborated permanently thereon. In laws of most of the countries the term „land“ is defined as a cone-limited space that crosses the boundaries of a parcel of land. Land is the basic element of immovable property, since in the course of time the buildings, constructions, etc., on the land wear-out, but land is not subject to depreciation because it remains physically unchanged, and therefore it is an eternal value. Oil, gold discovered on a parcel of land belongs to the land owner; however, for example, in Latvia certain limitations exist. In other countries there are limitations which are related to property rights in respect of land layers and air space [7].

Significant feature of the concept of immovable property is that any land improvements – buildings, roads, communications – are considered to be in close relation with the land: an immovable property does not exist without a plot of land.

The concept of immovable property can be viewed in a wider sense which includes not only the land surface and everything that exists on it or that has attached permanently thereto but also any legal rights to objects of the immovable property [2].

In accordance with all the above, it can be defined that immovable property is a real estate the ownership of which is registered in the Land Register. A real estate (immovable object, immovable property) is a plot of land and any im-

provements thereon closely related to the land, i.e. objects the transfer of which from one place to another by their meaning is impossible without creating unreasonable losses [7].

Due to the fact that the concept of immovable property includes a very large number of objects, immovable property definitions are given different interpretations. For example, E.I.Tarasevich, without going into details about the essence of immovable property, expresses in his publications a completely different opinion by interpreting immovable property as a type of property which is land, which exists in relation to land and which brings income [6]. This view has a close link with the basic principles of market economy which stipulate that resources are just as valuable as far as it is possible to use them profitably. E.I.Tarasevich focuses himself more on the validity and value – the material manifestations – of immovable property.

Whereas the Latvian immovable property appraisers recognise the following immovable property definitions:

- Immovable property is land as a physical object and everything that is closely related thereto and located thereon [1].
- Immovable property is any property which consists of a plot of land, as well as buildings which are found on the land [1].

Economic, political and social development of any country is driven and influenced by immovable property resources being in its possession – land, mineral resources, buildings, constructions, etc. Immovable property is one of the most important economic resources and of the most significant components of national wealth which in general accounts for 50% of the world's entire wealth.

However, the other side of legal and economic relations of any tax is taxpayers. In Latvia immovable property tax payers are natural or legal persons of the Republic of Latvia or foreign states and groups of such persons or their representatives formed on the basis of contracts or agreements, who are carrying out taxable activities or who have been guaranteed income in the future and who own or legally possess immovable property.

The immovable property tax payer by applying to his municipality as a taxpayer presents documents proving the rights of possession and provides the following information regarding the immovable property in writing: cadastre number,

cadastre designation of the cadastre objects included in the immovable property (units of land, buildings, constructions, groups of premises) as well as provides information on whether the building included in individual residential house constructions, the part of an apartment residential house, the artist's workshop, or the auxiliary building included in constructions of these houses are used for execution of economic activity.

Immovable property tax payers can be divided into the following groups: owners; legal possessors; users; lessees.

Within the meaning of the Law on Immovable Property Tax, as the owner of immovable property shall be considered a person whose ownership rights to the immovable property have been confirmed in the Land Register or whose immovable property has been registered with a local government or with the State Land Service. As the legal possessor of immovable property shall be considered a person into whose ownership, in the course of land reform, land has been transferred (granted) for payment or whose ownership rights to the land have been restored and the land has been determined (surveyed) on site, in accordance with the decision of the appropriate authority (in Riga – the Land Commission), as well as a person who has come into possession of immovable property on the basis of inheritance rights or on another basis. As an immovable property tax payer shall be considered also a person who has the right of use or lease to an immovable property owned by the state or municipality [3].

Immovable property tax for immovable property which belongs to several persons or is in joint possession, on the basis of joint property rights, shall be paid by each joint owner (joint possessor) proportionate to his or her share of the joint property. This share is called undivided share. Only in rare cases small properties belonging to several owners are divided into real shares by concluding a contract for common use, and usually such shares are determined on the basis of an oral agreement without concluding any special agreement. An undivided share can also be very small, even of a few square metres, which is particularly the case in the division of units of land located beneath apartment houses where the proportion of areas of the apartments in the house are observed.

Immovable property tax regarding existing land and buildings which are owned by the State

or local governments shall be paid by the user thereof, but if there is no such user – by the lessee [3]. As a *lessee* shall be considered a person to whom lands and buildings are leased out on the basis of a concluded lease contract. This means that not always a lessee shall be considered to be a user of an immovable property. As a user of land and a building shall be considered a person to whose possession land and buildings owned by the State or local governments have been transferred (granted) in accordance with the decision of a state or municipal institution, whereas as a user of land on which an apartment house owned by the State or local government and transferred for privatisation or privatised is located shall be considered the manager of the apartment house. Up to the moment when a person who, as a result of privatisation, has acquired an apartment which includes an undivided share of the unit of land, registers the property rights in the Land Register, the payer of the immovable property tax for the land under the apartment house in which the particular apartment is located shall be the manager of the apartment house.

2. Peculiarities of the immovable property tax policy in Latvia

Immovable property tax is a very important element in the national economy of any country. It is paid for every immovable property which is owned, possessed or leased.

Immovable property tax shall be paid into the budget of the local government of the city or municipality, in the administrative territory of which the immovable property or part thereof is located [4]. Immovable property tax in Latvia is administered by local governments which carry out administration of immovable property tax in their administrative territory (registration and accounting of immovable property tax payers, calculation and charging of immovable property tax, preparation and sending of immovable property tax payment notices to taxpayers, as well as granting of tax abatements for individual categories of population).

If the immovable property is located in the administrative territory of several local governments, the immovable property tax shall be calculated and collected by each local government proportionately to such part of the immovable property as is in its territory [3].

Local government as the administrator of immovable property tax is an independent or-

ganisation which continuously carries out the tasks entrusted to it in accordance with statutory procedures. Interference with issues which are within the competence of the tax administration and any influencing thereof in order to achieve an unlawful decision, a privileged status or to acquire other benefits shall be prohibited [4].

Immovable property tax is a mandatory payment into the local government budget, hence it is quite difficult to evade its payment.

Tax calculation is made at a certain amount and at a certain period of time thereby ensuring stable budget income. Of course, there are cases where immovable property tax payers deliberately evade payments of this tax; however, local governments are competent enough in this field to detect the taxpayers which are unwilling to make payments and, accordingly, local governments have the right to punish such taxpayers.

The cadastral value of an immovable property tax object shall be determined by the State Land Service of the Republic of Latvia in accordance with the requirements of the Immovable Property State Cadastre Law [3]. On the basis of information provided by the State Land Service of the Republic of Latvia regarding the cadastral value of each immovable property tax object, a local government calculates immovable property tax and sends a tax payment notice to the taxpayer. From 01.01.2010, immovable property tax is calculated from the cadastral value of an immovable property tax object according to the situation as at 1 January of the tax year, but before this date the tax was calculated from the last established cadastral value of immovable property. If an immovable property tax object has been registered in the Immovable Property State Cadastre Register during the tax year, the tax shall be calculated from the cadastral value of the object as at the moment of registration.

Immovable property taxation period is the current calendar year.

Immovable property tax shall be imposed upon tangible things which are located in the territory of the Republic of Latvia and which cannot be transferred from one place to another without being externally damaged:

- up to 31 December 2006 – upon land, buildings and constructions;
- from 1 January 2007 – upon land and buildings [3].

Whereas from 01.01.2010, in accordance with amendments to the Law on Immovable

Property Tax, immovable property tax is also imposed upon:

- residential buildings (single and two-family residential houses, apartment houses (parts thereof) irrespective of whether they are divided into apartments, parts of non-residential houses the functional use of which is living and which are not used for execution of economic activity);
- buildings registered in the Cadastre Register but not yet commissioned (i.e. irrespective of whether a non-commissioned building is used (for example, for living) or is not used);
- engineering structures, except for engineering structures being in the ownership or possession of the State, a local government, capital companies of the State or local governments, or capital companies which provide regulated public services; engineering structures owned by natural persons, which are not used for execution of economic activity, motor roads, streets and roads, water supply and effluent piping of local significance, power transmission and communication cables of local significance, etc.

The Law on Immovable Property Tax stipulates that immovable property tax shall not be imposed upon immovable property of a local government, which is used by a local government city council, as well as of those authorities and institutions established by it, which are financed from the resources of the local government budget and are located in the administrative territory of such local government; immovable property owned by a foreign state, which is utilised for the needs of its diplomatic or consular offices if, pursuant to the laws of the relevant foreign state, the Republic of Latvia enjoys the same rights in respect of the immovable property owned by Latvia in the foreign state; public waters and land beneath common use highways, roads, underground roads, tunnels, streets, railway tracks, city rail tracks, bridges and trestles; immovable property of religious organisations, which is not utilised for economic activities, etc.

In accordance with the Law on Immovable Property Tax, immovable property tax rates are the following:

- from 1 January 2007 to 31 December 2007 – 1,5% of the cadastral value of

the immovable property for land, non-residential houses or parts thereof (except for exemptions stipulated in the law) [3];

- from 1 January 2008 to 31 December 2009 – 1% of the cadastral value of the immovable property for land, non-residential houses or parts thereof (except for exemptions stipulated in the law) [3];
- from 1 January 2010 – 1,5% of the cadastral value of the immovable property for land, buildings or parts thereof (except for exemptions stipulated in the law) and engineering structures [3].

In 2007, the State Land Service approved the newly-developed basis of cadastral values, as a result of which in 2008, with the entry into force of the updated basis of cadastral values of land, for all groups of immovable property in the whole territory of the State multiple increase of the cadastral value of land and hence of immovable property tax for land was forecast. In order to prevent multiple and significant increase of immovable property tax, on 29 November 2007 amendments to the Law on Immovable Property Tax and Cabinet Regulations No 495 of 18 December 2007 "Procedures for the Application of the Provisions of the Law on Immovable property Tax" were adopted which entered into force on 01.01.2008 and from which it arises that the amount of immovable property tax for each individual unit of land and each building for 2008, 2009 and 2010 may not exceed the amount of the tax calculated for the previous tax year (without taking into account abatements) by more than 25%. At the same time, it arises from the wording of the Law and the Cabinet Regulations that this limitation of 25% on increase of the tax may not be applied in the following cases:

- if the purpose for use of the property has been changed;
- if immovable property tax calculation for 2007 has not been carried out for the property (newly-created object subject to immovable property tax).

From 01.01.2010, immovable property tax rates for living areas are the following:

- 0,1% of the cadastral value which does not exceed LVL 40 000 [3];
- 0,2% of the cadastral value share which exceeds LVL 40 00 but does not exceed LVL 75 000 [3];

- 0,3% of the cadastral value which exceeds LVL 75 000 [3].

This means that in calculating immovable property tax for a residential house the cadastral value of which is, for example, LVL 100 000, the tax for the cadastral value share of up to LVL 40 000 is 0,1%, for the cadastral value share exceeding LVL 40 000 but not exceeding LVL 75 000 – 0,2%, and for the cadastral value share which exceeds LVL 75 000 – 0,3%.

With regard to 2011, the authors note that in accordance with the adopted amendments to the Law on Immovable Property Tax, also in 2011, just like this year, the amount of immovable property tax may not exceed the amount of the tax calculated for the previous year by 25%.

Whereas, from 01.01.2011, immovable property tax rates for living areas are doubled and are the following:

- 0,2% of the cadastral value which does not exceed LVL 40 000 [3];
- 0,4% of the cadastral value share which exceeds LVL 40 000 but does not exceed LVL 75 000 [3];
- 0,6% of the cadastral value which exceeds LVL 75 000 [3].

At the same time, it has to be noted that local governments can develop binding provisions which provide for abatements for individual categories of immovable property tax payers. Abatements for individual categories of immovable property tax payers can be stipulated by local governments at 90%, 70%, 50% or 25% of the amount of immovable property tax.

The minimum payment of immovable property tax for each taxpayer in each local government is LVL 5, although in cases where immovable property tax objects of a taxpayer have been subject to tax abatements and after their application the total tax calculated for the tax year in the respective local government is less than 5 LVL. If the amount of immovable property tax for needy and low-income population after granting of tax abatements of 90% is less than LVL 5, the local government has the right not to send a tax payment notice to the taxpayer. In this case, the calculated amount of tax shall be accrued up to the moment when, as a result of changes or tax calculation for the next tax year, the total calculated amount of tax exceeds LVL 5, and the local government shall send a common payment notice for all the tax years for which the calculated tax was accrued [3].

Taking into consideration the above peculiarities of changes of immovable property tax described by the authors, it can be concluded that imposition of this tax will influence significantly both the development of the real estate market and – secondarily – the national economy in general.

Conclusions

Economic, political and social development of any country is driven and influenced by immovable property resources being in possession of the public – land, mineral resources, buildings, constructions, etc.

In accordance with rights in Rem of the Civil Law of the Republic of Latvia, as immovable property shall be regarded land and a set of all the properties located thereon – buildings, constructions and engineering structures, as well as the air space above it and the subterranean depths beneath it. There is no defined precise concept of immovable property, since the issue of transferring a residential house from one place to another in case it is granted the status of a movable property is not specified.

From the point of view of theory of economics, when there is low economic efficiency and unemployment of the society, stimulating fiscal policy is necessary. It can be implemented by a government by reducing taxes. It has to be noted that in Latvia the opposite can be observed – tax bases are extended almost every year thereby increasing the specific tax rates and introducing new taxes. In the authors' opinion, taxes must serve as a means for stimulating the economy.

After summarising the peculiarities of immovable property tax, it can be concluded that tax rates change practically every year due to the government's decisions. The analysed increase of immovable property tax by 25% for land is not imposed upon newly-created units of land, although it is practically possible to require from the State Land Service that the historical cadastral value of an immovable property object be imposed. Accordingly, the authors would suggest that, in order to optimise the administration of immovable property tax, amendments to the Law on Immovable Property Tax be introduced which would stipulate that in case of a newly-created unit of land a taxpayer has to provide to a local government the historical cadastral value of the unit of land in order to en-

sure that the limitation of tax increase of 25% is applied automatically in tax calculation.

The limitation of tax increase of 25% will be applied also in 2011, although in the current economical situation in the country when there is a high level of unemployment and low purchasing power of the population the government should consider the imposition of the tax more carefully at least with regard to individual categories of the population, as in principle since 2008 immovable property tax for land has been increased by 25% every year and from 2011 the tax for living areas will be doubled.

One has to support the view expressed in the mass media which states that the immovable property tax policy in Latvia should take also other countries' experience into account where the tax policy is based on population's income, that it, the calculated amount of tax may not exceed 5% of the average annual income of a household. Accordingly, in calculation of the tax and if the amount thereof exceeds the threshold value of 5% of a natural person's annual income, the population should be given the possibility to turn to a local government and require revision of the calculated tax.

Taking the above analysis and the overall tax policy situation in Latvia into account, it is to be concluded that as at the present moment the regulatory basis of the Republic of Latvia and its predictability is unstable.

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