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Property tax reform in Vietnam: Options, direction and evaluation

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ABSTRACT

Vietnam has seen significant economic growth over the past decade resulting in the need to develop solutions to finance infrastructure in its cities. Own revenue sources for cities are largely based on fees and charges and a form of property taxation from agricultural and non-agricultural land which is based on rice productivity. This paper analyses current land based revenue sources and concludes that these sources are unsustainable, lack buoyancy and represent a declining revenue base. Whilst the paper advocates a recurrent property tax based on land values empirical analysis provides some evidence that the government's proposal for a land based tax has several structural problems that will directly affect revenue buoyancy. However, the proposed land tax is at least a positive and important step in developing a sustainable revenue source for city and local governments.

Introduction

Vietnam since the economic and structural reforms known as *doi moi* has made significant progress from a centrally planned state to a market based economy. The last 25 years have seen comprehensive reforms, especially in land administration and land policy (Ravallion and van de Walle, 2008; Schmidt, 2004). The combination of rapid urbanisation rates and rising urban incomes is leading to a dramatic increase in the effective demand for the production and provision of essential municipal infrastructure and services throughout the country (Nguyen, 2009; IER-UNDP, 2007; Quang and Kammeier, 2002). This is placing considerable strain on scarce financial resources for cities and urban areas, highlighting the urgency of improving both municipal revenue generation and the efficiency and effectiveness of municipal expenditures.

Whilst the focus of government policy has been to develop the capacity of urban services to support continued economic growth primarily through industrialisation this had led to significant urban development problems. Ineffective urban management and the lack of development control have resulted in the development of cities that lack structure and basic services especially housing, water supply, and transport to meet the needs of rapidly growing urban populations (Dapice et al., 2010). Expansive urban development in terms of high rise/high value residential property along with office, retail and industrial property has been created. As with many other developing countries the government has been seeking tax sources that can help fund the delivery of quality services as well as basic human necessities such as water, power, sanitation, education and primary health (Bahl, 1998). It is clear that the main cities have a major challenge in financing infrastructure and to deliver efficient and effective services. For example, in respect of HCMC approximately 80% of the second largest single source of local regular revenue (the major source is debt finance through bonds) comes from the registration of new and transferred real estate. This mode of financing is not sustainable and is estimated to decrease over time (Trinh and McCluskey, 2010). In contrast, only 6.3% of local regular revenue generated in 2004 came from annual fees and charges on the city's greatest store of wealth, its rapidly appreciating stock of land and buildings (IER-UNDP, 2007).

Finding ways to finance investment in infrastructure and basic services in a sustainable and equitable manner is a tremendous challenge facing the city's policymakers. One tax with the potential to raise sufficient revenue from fast developing cities is the property tax (Bahl and Martinez-Vazquez, 2007; Bahl, 2009). The property tax can be viewed as a tax on real estate wealth/value and within cities like HCMC and Hanoi there is a considerable store of wealth attached to real property (Deininger and Songqing, 2003; Kato and Nguyen, 2010). It is also clear that government funded infrastructural development can have positive effects on property values hence it could be argued that by taxing the value of property that part of the wealth created by government is being recouped. The property tax in various forms exists in most countries (Bird and Slack, 2004; McCluskey, 1999). In both principle and practice, this tax can have important fiscal and non-fiscal benefits (Paugam,

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1999; Brzeski and Frenzen, 1999). The revenue that such a tax produces is often of critical importance to local and in some cases higher levels of government.

Real property taxes are often cited as 'good' candidates for independent subnational administration (Bird and Bahl, 2008). It provides a predictable and durable revenue source for local budgets; fosters local autonomy and provides a fiscal mechanism for decentralisation (Bird and Bahl, 2008). Indeed, few fiscally significant taxes are more susceptible to local administration than the property tax (Bird and Slack, 2004; Mikesell, 2003; Bell, 2003). The immovability of the tax base makes clear which government is entitled to the tax revenue. The tax captures for local government some of the increases in the value of land that are partially created by public expenditures. As McCluskey (1999) points out, real property is visible, immobile, and a clear indicator of one form of wealth. The property tax is especially attractive when compared with other potential sources of local taxes (Bird, 2011). The property tax is thus difficult to avoid and if well administered can represent a non-distortionary and highly efficient fiscal tool.

The introduction of ad valorem based property taxes tend to accompany reforms in land ownership, land titling and registration. Good exemplars of this process can be seen in several ex-socialist countries in Central and Eastern Europe (Aleksienne and Bagdonavicius, 2008; Tiits, 2008; McCluskey and Plimmer, 2007). The privatisation of real property rights in association with property registration creates the environment for the establishment of a property market (Ngo, 2005). This in turn provides the basis for fiscal and legal cadastres upon which the property tax can be based. In Vietnam, projects involving land registration and titling are under way; the fundamentals of land ownership security in association with the granting of Land Use Certificates and land transfers is paving the way for more transparent support of property rights (Kim, 2004). In support of these reforms the Vietnam government in 2002 created the Ministry of Natural Resources and Environment which has primary responsibility for the State management of land policy development and regulatory policies in addition to land surveying, mapping, land allocation, land use planning and valuation.

This paper examines the potential for the introduction of a land based property tax in Vietnam and in particular how this tax could effectively replace existing inefficient taxes on land. The key objective of this research is to demonstrate the efficacy of introducing a land tax and the revenue potential of such a tax particularly for the large urban cities. The paper is organised into six sections. "Introduction" has provided the contextual background and the case for considering the introduction of a property tax; "Current land based taxes and charges in Vietnam" outlines current land based taxes and charges highlighting their inherent weaknesses; "Proposed property tax reform" examines the government's current proposed property tax reform; "Revenue simulation" provides some evidence as to the revenue potential of the new tax; "Discussion" provides a discussion around some of the problems associated with the proposal to introduce a land tax; and finally "Concluding remarks" draws some conclusions.

Current land based taxes and charges in Vietnam

Vietnam has several land based revenue sources that are allocated to local budgets and a plethora of other charges and fees (Trinh and McCluskey, 2010). Land represents a valuable asset that can form the basis of a tax revenue instrument through its value, use and transfer. Within the Vietnamese national budget there is no distinguishing between real property taxes and other real estate revenue sources (Trinh and McCluskey, 2010). Besides the transfer tax levied when the land users sell their land use rights, there are two main forms of revenue: single event revenue sources and annual recurrent revenues. The single event revenue is largely based on the land use charge, land rent and the sale of state-owned housing. Recurrent property based revenues are derived from the Agricultural Land Use Tax and the Land and Housing Tax.

The 1993 Land Law recognised that land had value, albeit through a government based land "pricing mechanism". Prescribed land values were set as the basis for revenues generated from the land use charge, land rentals and the sale of state-owned housing. Table 1 illustrates the importance of these land based revenues for central government showing just over 2% of GDP for 2008. Whilst such revenue is modest in comparison to the total taxes, charges and fees it nonetheless is an important source of revenue.

Single event based property taxes whilst being important revenue sources have a major problem in that the revenue lacks buoyancy and will decline in real terms over time. For example, the land use charge (LUC) is levied when the State allocates land for use by individuals and organisations. As more and more land is allocated with land use rights it is anticipated that this source of revenue will decline in the future (see Table 1). In 1994 the state introduced a scheme allowing occupiers of state owned housing units to purchase rights in their property. This scheme has been extremely successful in terms of the number of properties sold. Since implementation, some 45% of the State-owned housing stock has been sold representing some 256,000 apartments (Ministry of Construction, 2008). Table 1 illustrates the initial growth of revenue during years 1996–2004 followed by a decline in revenue from 2006. The tax on the transfer of land use rights again represents an important revenue sources (see Table 1) however due to problems

Table 1
Total land-related and real property revenues in Vietnam (billion VND).

Categories	1996	1998	2000	2002	2004	2006	2008
GDP	272,036	361,016	441,646	523,654	715,307	974,266	1,215,287
State budget revenue	62,387	72,965	90,749	131,451	190,928	279,472	323,000
Tax, charges and fees	59,324	69,200	86,867	113,510	121,500	151,682	174,300
Land-based revenue	5421	5638	5533	7590	20,201	19,935	27,068
Land use charge	1173	800	1016	3244	14,202	13,500	16,500
Land rent	180	382	390	459	846	690	1569
Registration fees[a]	1120	1016	934	1332	2607	3200	5194
Tax on land use right transfer	319	355	213	327	640	840	1974
Sales of state-owned houses	347	822	838	1120	1338	1130	1051
Agricultural Land Use Tax	1902	1956	1776	772	130	85	82
Land and Housing Tax	380	307	366	336	438	490	698
Land-based revenue/GDP	1.99%	1.56%	1.25%	1.45%	2.82%	2.05%	2.23%
Real property tax/GDP	0.14%	0.09%	0.08%	0.06%	0.06%	0.05%	0.06%

Source: General Statistics Office and Ministry of Finance, 1996–2008.
[a] Including automobiles, ships, etc.