



Municipal Urbanization Tax and land-use management—The case of Tomar, Portugal

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ABSTRACT

The Municipal Urbanization Tax (MUT) can be adjusted so as to promote or deter new construction for certain land-uses or different areas of a municipality. Tomar (Central Portugal) is characterized by scattered settlement and has experienced construction outside urban perimeters. The historic center of the City of Tomar and the more remote rural areas of the municipality underwent population losses, while a suburban ring around the city grew exponentially. The new calculation formula for the municipality's MUT, presented in the paper, attempts to correct these trends.

The new formula innovates in that: it reflects the real costs of infrastructure associated to each different land-use and location in the municipality; it includes an accurate assessment of the municipality's investment in infrastructures, according to their local or municipal scope, and average maintenance costs; it allows for a constant updating of these costs; it corrects the lack of transparency for which the formula it replaces was criticized, namely by making more evident the gap between real cost of investment and the value recovered through taxation; finally it is also easier to calculate than the formula it replaces.

Because most municipalities in Portugal charge MUTs well below the effective cost of reinforcing and maintaining infrastructure, the municipal government required that the formula included a mechanism through which to establish a reduction to the total tax, in order not to decrease the municipality's attractiveness to investment. This slightly distorts the MUT's objective assessment of costs and the underlying effort of guaranteeing the long-term economic sustainability of infrastructure investments by the municipality. Individual municipalities are apprehensive as to the possibility of taking the lead in reflecting the real costs of urbanization in their tax instruments, and this situation is unlikely to be resolved without a coordinated collective action.

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Introduction

The Portuguese Urbanization and Building Law contemplate the collection of a specific tax for the construction, maintenance, and reinforcement of urban infrastructure. The Municipal Urbanization Tax (MUT) is a one-time charge against new development through land subdivision (*Loteamento*) or individual buildings, similar to an impact fee (Nelson, 1988; Singell and Lillydahl, 1990; Brueckner, 1997; Silva et al., 2012). The calculation formula and parameters are determined at the municipal level.

This law further determines that municipal land-use regulations must provide a technical justification for the MUT's calculation formula, bearing in mind, namely:

- The costs of building, maintaining, and reinforcing infrastructure, as published yearly on the municipal Multi-year Investment Plan (MIP). These costs can be spatially segregated.
- Differentiated rates according to land-uses, building typologies and, optionally, the location and specific infrastructure requirements.

The General Municipal Tax Regulation, to which all municipalities have to comply, reinforces the need for an economic justification of the formula and the resulting values. As this legislation was only recently revised, all Portuguese municipalities are in the process of updating their municipal land-use regulations, including the MUT.

Prior to the publication of these laws, the vast majority of municipalities' MUTs showed some limitations: the formula's complexity and difficulty of calculation was a prevailing issue; the collected value was typically much lower than the municipalities' actual investment in infrastructures; and the former MUTs tended to be tolerant of construction outside urban perimeters, promoting urban sprawl.

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This paper presents the new MUT calculation method for Tomar (Central Portugal). Some of the goals of the new formula are:

- Restoring the balance between cost and benefit of the investments in infrastructure, insuring that the municipality collects (wholly or in part) the investment costs resulting from new construction or redevelopment.
- Reinforcing the nation-wide effort to contain sprawl, encouraging instead the densification and planned expansion of existing urban areas.
- Making the formula easier to calculate by the municipal urban planning services.
- Promoting a simpler concept, so as to make the calculation more accessible to the general public.
- Bearing in mind the constitutional principles of adequate balancing of public and private interests and the principle of equity, reflecting concerns with social justice.

The municipality of Tomar recently promoted the revision of its MUT. Our Team was charged with the development of the new formula for the calculation of this tax, in collaboration with the Municipal Services. Our efforts were consistent with the new concerns and goals of the national land-use policy: until recently, in Tomar and elsewhere in Portugal, the quest for development was intrinsically connected with growth, both in terms of population, and economic activity; the sobering reality of continued population losses and stagnating economic activities have progressively redirected the rationale of development towards quality, rather than quantity; although most municipalities still aggressively compete to attract new investment by keeping land-use taxes (and especially MUT) artificially low, new concerns are now being reflected in revised MUT formulas. Among these is the uncertainty about the long-term budget balance or the capacity of the municipalities to maintain the same level of services provision without the added tax income from new constructions.

Also, social justice issues arising from the added cost of pushing infrastructure so as to serve remote and isolated buildings, rather than concentrating efforts on good service provision to planned and compact development in consolidated urban perimeters, is now a major preoccupation of national and local planning policies. One of the consequences is a generalized push towards full-cost recovery for isolated buildings, while focusing tax ‘discounts’ on more equitable land-uses and typologies. Other countries face similar dilemmas, with an overarching concern with justice in taxation efforts (Delaney and Smith, 1989; Horne and Felsenstein, 2010), the introduction of urban containment policies (Casey and Nelson, 2002) and the influence of taxes in containing development outside urban perimeters (Altes, 2009; Singell and Lillydahl, 1990; Song and Zenou, 2005).

“Land development and taxation in Portugal” of the paper provides an overview of the past and present land use taxation instruments in Portugal and their possible implications to land use policy and spatial planning. These instruments are framed within an international context. A brief introduction to the case study municipality is provided in Section “Study area: Tomar municipality”, and Section “Previous calculation of the Municipal Urbanization Tax” focuses on the previous formula for the calculation of the Municipal Urbanization Tax, and describes the problems arisen by it. The need for a new formula is established and we present our new methodology for the calculation of the Municipal Urbanization Tax in Section “Proposed methodology for the calculation of the Municipal Urbanization Tax (MUT)”. In Section “Results and discussion” we discuss the problems and opportunities that derive from the necessary revision of these taxation instruments, as well as the specific hindrances faced during the revision process. Section “Conclusions” wraps-up the paper with what we believe

to be the most relevant take-home messages learned from this process.

Land development and taxation in Portugal

Following is an overview of the different land use taxation instruments used in Portugal. We introduce the different taxes, with an emphasis on the Municipal Urbanization Tax, provide an international context to the instruments and to the overarching planning issues they may address.

Portuguese land-use taxation system

In Portugal, real-estate taxes constitute an important share of the municipalities’ budget and is supported by four different instruments (Correia, 2001; Bird and Slack, 2002; Sá, 2005): (a) property tax (*Imposto Municipal Sobre Imóveis*; Municipal Real-estate Tax – MRT); (b) tax over real-estate transactions (*Imposto Municipal Sobre Transmissões Onerosas de Imóveis*; Municipal Transmission Tax – MTT); (c) taxes over benefits resulting from public investments (similar to the concept of value-capture from betterments described by (Connellan et al., 2004)); (d) tax over the construction, maintenance, and reinforcement of urban infrastructure (*Taxa Municipal de Urbanização*; Municipal Urbanization Tax – MUT). This latest will be the subject of this paper.

- (a) The recently revised MRT is based on the principle that income from property should be taxed, with the beneficiaries, the landowners, being the subjects of taxation. The tax includes mechanisms that promote urban rehabilitation. The necessary efforts of real-estate value assessment have been somewhat hampered, in Portugal, by the incapacity of the public administration to regularly update and expand the assessments in new or existing properties. It is commonly recognized that the lack of realistic assessments on real-estate values greatly reduces the yield of the tax and, by consequence, increases the relative importance of other taxation mechanisms, such as the MTT. The use of location coefficients, an integral part of the latest version of the Portuguese MRT, constitutes a mechanism for sprawl containment, especially relevant in the suburban fringes around the Lisbon and Porto metropolitan areas.

The MRT can be equated to an *ad valorem* real-estate tax, not dissimilar to the *property* tax extensively adopted in the United States (Song and Zenou, 2005). Although the MRT is prone to criticism as it spatially discriminates between landowners, overall the effect in urban containment is expected to be positive, as discussed equally for the United States’ case (Brueckner, 2000; Song and Zenou, 2005), The Netherlands (Altes, 2009) or the United Kingdom (Connellan et al., 2004).

- (b) The MTT, also recently revised, applies a flat rate over property transmissions. Under its former configuration, it was frequently considered to be one of the reasons behind the municipalities’ promotion of urban expansion: the higher price of new houses was directly reflected over the value of the collected tax, and this tax was an important source of income for the budget of fast-expanding municipalities; the eagerness of these municipalities led to a strong encouragement of very fast development of poorly planned expansions.

The recent revision of the tax framework has reduced the global impact of this specific tax in the municipalities’ budgets, but it is still considered a partial obstacle to normal real-estate market operation, as its value tends to be reflected on a higher selling price for new homes. The fact that it is applied over a necessarily declared transaction, though, makes its collection process very effective.

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