Municipal rates policies and the urban poor

PROMOTING ACCESS TO URBAN LAND MARKETS?

In urban areas, the poor continue to struggle to access well-located land. Secondary residential property markets are also constrained from functioning effectively in black townships. Recent research supported by the South African Cities Network (SACN) and Urban Landmark has investigated how municipal property rates policies are, or could be, used to promote access by the poor to urban land markets.

Property rates policies are foremost an instrument created through the Municipal Property Rates Act (MPRA) of 2004 to provide a policy framework at municipal level within which a transparent and fair system of rating, exemptions, reductions and rebates can be implemented. However, the MPRA explicitly incorporates a pro-poor objective alongside its fiscal goals and allows municipalities to explore approaches which seek to balance municipal revenue concerns with pro-poor policy intentions. By providing direct tax relief, municipal rates policies can impact on the demand side of the equation by making it more affordable to remain in one's current property or to move up the property ladder.

Direct tax relief to improve affordability for poor households

Municipal rates policies include rebates, exemptions and reductions which are targeted at vulnerable groups for the purpose of eliminating or relieving their rates liability. An unaffordable property rates account could have the following effects on property owners:

- It could result in eviction or downward movement in the housing ladder.
- Households might be discouraged from moving up the housing ladder due to fear of being unable to pay in the future.
- It reduces disposable income available for other household necessities.

To the extent that ownership by the poor of formal housing is limited by affordability, direct tax relief can assist by putting more money in the pockets of low-income property owners or prospective property owners.

Impact of the residential exclusion on the poor

The rates rebate known as the 'residential exclusion' is probably the most important instrument in the municipal rates policy for providing direct relief to the poor. The MPRA excludes the first R15 000 of the market value of a residential property. A number of municipalities have chosen to raise this limit to as much as R150 000.

At the time of the drafting of the MPRA, the amount of R15 000 was chosen to reflect the perceived average market value of a house subsidised by the government through its Reconstruction and Development Programme (RDP). Since then, however, the amount of the subsidy has increased significantly as the specifications for the standard RDP house have improved. The mandated R15 000 residential exclusion therefore has not kept up with the input costs of a government-subsidised house or the estimated resale price of a house subsidised through the government's Breaking New Ground Programme (BNG, a successor to the RDP). As a consequence, the wide variation in residential exclusion thresholds means that RDP beneficiaries in some municipalities are liable for rates while beneficiaries in neighbouring municipalities are exempt.

Johannesburg and eThekwini have the highest residential exclusion rate of R150 000. According to the current valuation roll for Johannesburg, the R150 000 residential exclusion completely eliminates rates liabilities for 32% of residential property owners, or 24% of ratepayers. However those

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properties which are entirely exempt from property rates due to the residential exclusion are a very small portion of the total properties on the roll and the total value of the roll. The total rand value of residential properties under R150 000 is R11.6 billion, which is only 3% of the rand value of all residential properties and only 2% of the rand value of the entire valuation roll.

Ultimately, the reality of lower collection rates for residents with lower-value properties means that the municipality must weigh the higher administrative costs of attempting to collect bad debts against the actual revenue foregone if that category of property owners is instead blanketly exempted from rates liabilities. Lower collection rates imply higher administrative costs and less revenue foregone.

Rebates and exemptions for vulnerable groups

Analysis of the municipal property rates policies of the nine largest municipalities shows that some limit themselves to the minimum in rebates and exemptions, while others apply more generous and innovative rebates. Cape Town, Nelson Mandela Bay and Ekurhuleni have innovative sliding scale rebates for senior citizens, pensioners and disabled persons, with varying numbers of income categories. Linking rates relief to twice the amount of the old age grant (OAG) is fairly typical.

In a number of municipalities the key driver in setting the policy was the desire to continue the principles of the old rates policy in the new rating system. The policy intent and impact of the old rates ordinance were translated into terms and mechanisms allowable under the MPRA.

Another way to improve targeting is to supplement the means test with a limit on the value of the property. The difficulty arises in situations where property owners may be asset-rich but cash-poor: for example, senior citizens who have fully paid off their homes but survive on an OAG as their only income. If hit with substantial property rates, such residents may be forced to sell and move from homes they have lived in for most of their lives.

Many municipalities, including Tshwane and Ekhurhuleni,

provide full exemptions to persons on the indigent register, although with some exceptions. Johannesburg has developed the innovative approach of targeting rates and tariffs relief for the poor through its 'social package' policy, which provides benefits based on a poverty index that takes into account factors other than income, including access to services.

Special relief for child-headed households has appeared in the rates policies of some municipalities, such as Mangaung, Ekurhuleni and eThekwini, as a progressive mechanism to provide support to vulnerable children, many orphaned by HIV and AIDS.

The key challenge for municipalities in applying rebates to vulnerable groups is that it is difficult to determine who is poor from the information on the valuation roll alone. The rebate process puts the onus on the ratepayer to access the benefit. Hence pro-poor rebates have sound social objectives but are very difficult to implement. The requirement for documents to be produced to show eligibility and low levels of public awareness keep take-up rates very low. Also the verification of eligibility information, in the case of rebates for farm workers, often relies solely on the applicants' self-reporting. As a result, a high number of eligible poor people are not accessing available property tax rebates.

Municipalities must also consider revenue foregone when selecting and designing direct tax relief measures for the poor. In the case of the residential exclusion, the revenue foregone is a function of the value of the threshold, the number of qualifying properties on the roll and the estimated collection rate. In the Johannesburg case, one of the factors in setting the residential exclusion threshold at R150 000 was the collection rate for lower-value properties, specifically avoiding the administrative burden and debt write-offs associated with chasing high numbers of low-amount arrears. The examples of Johannesburg and Buffalo City suggest that the ability to calculate collection rates of different property value bands is therefore a critical part of determining the residential exclusion amount.

Given the ability of these vulnerable groups to pay, and the rates base, revenue foregone due to these direct tax relief measures described above is not significant relative to total rates revenue. However, the total cost to the municipality of implementing any tax relief measure is the cash revenue foregone plus the administrative costs and staff time to chase arrears, verify documentation and conduct public awareness campaigns to increase uptake. Weighing up the options, the means-tested rebate instrument has higher accuracy in terms of reducing errors of inclusion. However, low public awareness and difficulty in verifying eligibility may reduce uptake and therefore lead to errors of exclusion.

Towards pro-poor property rates policies

From the perspective of local government, the main issue appears to be the legality of giving special treatment to a particular area. Some municipalities are more aggressive than others in considering and experimenting with ways to provide rates relief to categories of property or property owners, in order to alleviate poverty or promote economic growth and development. The legality of such schemes will likely be questioned, if not tested in court. Other municipalities are being more cautious in interpreting the Act regarding impermissible discrimination between property owners and property categories.

As municipalities shift their energy from sorting out start-up problems with their new policies and valuation rolls, we may see the addition of further rebate schemes and the wider spread of special rating areas. In the meantime, research on the impact of some of these measures (such as the density bonus in Johannesburg or rebates to farmers who provide services to farm workers) would be extremely useful in developing an understanding of the potential of property rates for impacting land use and property markets in favour of the poor.

Analysis suggests that the residential exclusion is one of the most effective and least costly mechanisms (from an administration perspective) for targeting the poor for rates relief. Better information on collection rates per income band and on the secondary residential property market in township areas could improve the methodology for setting the residential exclusion threshold, thus increasing its pro-poor benefits while meeting municipal revenue needs. Income-based rebates and other specific measures to target particularly vulnerable groups can then be used to fill the gaps.

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This research was prepared by Isandla Institute and PDG for the South African Cities Network and Urban Landmark. The full paper can be downloaded at www.urbanlandmark.org.za/downloads/municipal_rates_policies_urban_poor.pdf