

# Real Market Value to Determine Property Tax

By [Irina Filatova](#)

February 14, 2012

**The  Moscow Times**

If the government's plans come to fruition, this year will be spent completing property evaluations across the country according to market-based standards, paving the way for the implementation of a new property tax, which could partially enter into force as early as 2013.

The idea of introducing the new tax — which is called the unified property tax and is supposed to replace the existing land tax and individual property tax — was first voiced by the government 11 years ago, and Prime Minister Vladimir Putin said in 2009 that the move should lower the tax burden on owners of small apartments. Analysts said it might put more properties on the market and bring down prices.

The new tax will be based on a property's market value, not the current artificially low numbers set by technical inventory bureaus, or BTI — a system created during the Soviet era.

The Federal Service of State Registration, Cadastre and Cartography is responsible for the

evaluation process and said it hopes to get the complete picture by the end of this year.

Evaluation has been completed only in 12 regions, including Kaluga, Tver, Kaliningrad, Krasnodar, Krasnoyarsk and Rostov. The service said it targets completing evaluation in another 29 regions by July, and to finish the task for the remaining 42 regions by late 2012.

The overall results of the evaluation will be published in the regional press, in line with the current legislation, and will be available on the service's website.

## **Setting the Value**

The BTI evaluations of property value were traditionally based on three major factors — construction costs, degree of wear and tear, and an adjustment for inflation, said Alexei Shteinikov, head of the property evaluation department at the Federal Service of State Registration, Cadastre and Cartography.

Now a process of cadastral evaluation is being implemented that will include all property lines and their exact location, and will provide more detailed information on properties.

The major difference between the old and the new processes for determining value is that the cadastral evaluation also takes into account the location of the real estate itself — a key factor in determining market price, Shteinikov said.

In order to determine the property's market value, appraising companies that won a tender organized by the Federal Service of State Registration, Cadastre and Cartography analyze these factors and collect information on real estate deals concerning similar properties.

The property's cadastral value will in fact be equal to its market value, Shteinikov said.

The BTI value of an apartment in the city center and one located on the outskirts that has a similar size, construction and degree of wear and tear will be equal, but the cadastral value might be different because the market price of the centrally located property is higher, Shteinikov said, adding that the cadastral evaluation determines "the fair value" of property.

For example, an apartment with a BTI value of 300,000 rubles (\$9,700) could have a market value of 10 million rubles.

"The inventory value has nothing to do with the market value and could be underestimated dozens of times," said Vadim Zasko, director of the institute of tax management and real estate economics at the Higher School of Economics.

Indeed, the size of the tax base in the Kaluga region and Tatarstan republic, where market-based property evaluation was completed in July, increased 500 percent and 800 percent, respectively, Vedomosti reported in August, citing a report by Soyuzekspertiza, a nongovernmental certification agency with the Chamber of Industry and Commerce.

## **Tax Leads to Supply**

Introducing the property tax — which will be collected by municipal authorities that now collect the two existing taxes — will have the biggest impact on those who own several

apartments, but it's "very good news" for anyone who plans to buy housing because it will make property more available, said Oleg Repchenko, head of the Irn.ru real estate portal.

Supply in the domestic housing market is rather limited because some homeowners have several apartments that they bought to invest free money. The lack of free space results in overpriced housing, he said by telephone.

After the introduction of the property tax, housing prices are likely to decline because such homeowners might start selling or leasing out their idle apartments, adding to the pool of available property, Repchenko said.

The unified property tax is largely considered a tax on wealth, but is not intended to increase the burden of homeowners with modest incomes, who got their apartments in the Soviet times and subsequently privatized them or inherited them, said Zasko, adding that a mechanism of providing tax breaks to small homeowners is needed.

Putin suggested in 2009 that the new tax rate be higher for those owning expensive apartments or big plots of land and lower for owners of small apartments and houses, and the Economic Development Ministry later proposed not to charge owners of small apartments of up to 55 square meters.

In 2004, the State Duma passed a first reading of a bill designed to update the property tax system, but the work has stalled since then.

The Finance Ministry is preparing amendments to the Tax Code to be discussed later in 2012, Sergei Razgulin, head of the ministry's tax policy department, said in November, RBC reported.

After the amendments are made, municipal authorities will have to pass laws regulating the introduction of the tax in the regions, he said.

## **Devil in The Details**

But even if the evaluation process is completed this year, it remains unclear when the unified tax can be rolled out nationwide.

In June, President Dmitry Medvedev called for collecting the unified tax starting in 2012 in the regions where the property evaluation is completed. However, both the Finance Ministry and the Economic Development Ministry said introducing the tax in some regions is only possible in 2013.

The new tax could appear in 2013 in some regions where the cadastral evaluation has been completed, Economic Development Minister Elvira Nabiullina told journalists in late December. But introducing the tax across the whole country might take at least five years, she said.

"It will be a long time before we have the unified property tax. It's our joint position — the Finance Ministry, the Federal Tax Service and ours," Nabiullina said.

However, the Finance Ministry said in November that full implementation of the tax is

possible in 2014.

Nabiullina said one of the major obstacles hampering the introduction of the new tax is the current procedure for registration of property rights because land plots and buildings usually have separate ownership documents.

In order for the unified tax to be introduced, owners should start registering their land and structures as single properties, she said.

Industry players see that requirement as an additional opportunity for bureaucrats to extort money from citizens.

"Basically, the entire effort is designed to be another feeding trough for officials, who will have new chances to get side payments for reregistering properties, producing evaluations and so forth," a property registration specialist at a Moscow region development company told The Moscow Times on condition of anonymity due to the sensitivity of the subject.

Another problem is the size of the tax rate, which remains undetermined, since there's no full information on the tax base. Nabiullina said the government is discussing a rate of 0.01 percent of the property's market price.

The government can't make a decision on the size of the rate and any tax breaks to be provided based only on the information from the 12 regions where evaluation has been completed, Deputy Finance Minister Sergei Shatalov said in October.

"It's one of the most important questions. ... We don't want to suffocate citizens or collect additional taxes," he said, Rossiiskaya Gazeta reported.

The size of the land tax currently ranges from 0.3 percent to 1.5 percent of the plot's cadastral value, according to the Federal Tax Service's website.

The individual property tax rate is up to 0.1 percent of the property's BTI value for real estate worth up to 300,000 rubles, and can reach 2 percent for property whose BTI value exceeds 500,000 rubles, according to the service.

Property tax revenues are supposed to be spent by municipalities on upgrading infrastructure like hospitals and kindergartens.

### **And If You Don't Agree?**

Ultimately, the contestation mechanism for the evaluation results should be created in 2012, so that it could be used by property owners who don't agree with the evaluation, Nabiullina said.

"Citizens and businesses might be unsatisfied with the evaluation. ... There should be a simple contestation procedure in order to regulate the tax base, and then we'll be able to introduce the tax based on the property's market value," she said.

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