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Legal and Economic Features of Real Estate Taxation Systems in European Union (Selected Problems)

Abstract

In this paper an attempt has been made to characterize legal and economic determinants of property taxation systems in the European Union with particular emphasis on the fiscal and non-fiscal functions of property tax. In property taxation systems in European Union there are no unified solutions specific to each country. In specific national tax systems, the components of the tax structure (especially the tax base, rates, exemptions and tax breaks) were formed by socio-historical conditions, which caused that in some countries there are very characteristic solutions, not existing in other tax systems. However, there are some common legal and economic features that are specific to modern property taxation systems. A common element that combines modern tax systems is that the basis (with few exceptions) of real estate taxation is its value (variously defined).

Key words: Local Taxes, Wealth Taxes on Property, Local Authorities' Budget, Legitimization of Property Tax Collection

Research Methodology

The main goal of the paper is to present and evaluate legal and economic regulations concerning systems and models of real estate taxation in the European Union countries. The analysis of legal regulations includes both the point of view of the taxpayers and public administration bodies (tax authorities). The evaluation of legal and economic regulations and solutions concerning systems of real estate taxation in the European Union countries was limited to the real estate tax and

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reflects the search for legal governance in real estate taxation from the point of view of taxpayers (individuals and entrepreneurs) and public administration units (mostly local self-governments). The evaluation of current and projected solutions and amendments to legal regulations includes both short-term and long-term perspective. This analysis will attempt at verifying the following research hypothesis: there are effective legal regulations, whose implementation into the real estate tax structure will allow us to obtain optimal legal structure of this tax as far as the principles of taxation equality and universality and tax effectiveness are concerned.

The Legal Taxonomy of Property Taxes

“Immovable property” generally encompasses both “real property” and “real estate,” terms that have different technical meaning but that often are used synonymously. Real property refers to the rights, interests and benefits connected with real estate, which is the physical piece of land and any structures on that land. Land, in turn, can have the same meaning as real estate. Much of the literature on national property tax systems speaks generally of “property taxes.” Particularly when considering property tax revenues, it can be important to distinguish among the various kinds of taxes on property. The International Monetary Fund (IMF) and the Organization for Economic Co-operation and Development (OECD) have developed largely complementary schemes for classifying taxes, which they use in presenting revenue statistics. Taxes on property include: (1) recurrent (annual) taxes on real (*immovable*) property, (2) recurrent taxes on net wealth, (3) taxes on estates, inheritances, and gifts, (4) taxes on financial and capital transactions (including real property transfers), (5) other non-recurrent taxes, and (6) other recurrent taxes on property (including taxes on movable property such as vehicles and machinery and equipment). Many countries do not have a uniform national property tax system. Several have separate land and building taxes. Several essentially let local governments tailor their systems to local conditions.¹

Immovable property taxes are suited to local governments because it is clear which government is entitled to the tax revenue from immovable property, and such property cannot flee the tax collector. Local government services are often provided to properties or their owners and occupants. The tax captures for local government some of the increases in the

¹ Property Tax Regimes in Europe, The Global Urban Economic Dialogue Series, United Nations Human Settlements Programme, Nairobi 2013, p. 1.

value of land that are partially created by public expenditures. A dedicated source of revenue promotes local autonomy. The visibility of property taxes focuses attention on the overall quality of governance and promotes accountability. Information on land, buildings, and market prices collected in the course of administering taxes on immovable property becomes part of a valuable pool of information that has numerous governmental and private uses. If up-to-date and publicly available, this information can facilitate orderly real property markets. Despite their advantages – or perhaps because of some of them – property taxes often are underutilized sources of revenue. A common, but disputed complaint about the property tax is that it is inherently regressive, although poorly administered property taxes tend to be regressive. People schooled in income and consumption tax administration can fail to appreciate the relative advantages of a wealth tax. They focus on high administrative costs and low yields, overlooking the comparative high compliance costs associated with income and consumption taxes. Valuers schooled in traditional single-property valuation methods disdain assessors and the mass valuation methods used in property taxation. The unpopularity of property taxes, coupled with opposition from taxpayers who benefit from entrenched inequities encourages “legislative neglect”.²

The greatest discrepancies and irregularities between the science and practice of economics concerns the legal interpretation of the property tax term. It is generally accepted that these performances are directly (or less indirectly) related to the possessed property – so they may burden the fact of possessing it and the fact of increasing it with exceptional circumstances. Sometimes revenue taxes also constitute a burden on a single (exceptional) property growth. However, to be able to differentiate them from property taxes, we need to supplement the definition of the latter with a statement that their structural tie with property is manifested – with only the object of taxation – in the structure of the taxation base: as we can easily prove, when defining the taxation base of income taxes, what comes to the foreground is the value of the actual benefit gained by the taxpayer – it does not necessarily have to coincide with the market value of the objects which account for property gain, and only in a few situations tax authorities can question the value declared by the taxpayer, adopting market-related values. The opposite is true in property taxes: as a rule the taxation base is the market value of an object being property gain, the so-called pure value – after deducting some costs and debts related to that object – and this is the value the

² E. Slack, *The Property Tax – in theory and Practice*, Institute on Municipal Finance and Governance, Munk School of Global Affairs, University of Toronto, “IMFG Municipal Finance and Governance”, no. 2/2011, pp. 2–3.

taxpayer can declare, even if the subjectively indicated object has a much higher value for them than market value.

Property taxes may be classified in many different ways. One of the criteria may be the frequency of imposing them. In this case we may talk of single (one-off) tributes (extraordinary), usually imposed in times of temporary deficit in the state budget, valid for a limited period of time, and of regular tribute – imposed for a specific time. Property taxes may also be divided into direct and indirect, with several criteria of such division. We may also apply the criteria of collection technique to property tribute. Direct taxes in this approach will be those paid by the entities who have direct tax obligation towards territorial self-government unit or Treasury. The economic criterion, referring to the sources of tax coverage, allows us to differentiate nominal and real property tributes. The former are characterized by the fact that it is not necessary to use any part of the property substance to pay them – a given taxpayer may pay his tax obligation with the money coming from current income or savings.

Property taxes have various legal classifications. Analyzing legislature of the EU and OECD countries, we may differentiate four classification groups of property taxes:

- 1) Taxes on possessing property (managing property). Depending on the valid tax system these may be taxes on the total value of property belonging to a given economic entity (moveable and immovable property, cash, bank deposits, etc.), or – more frequently – on its selected elements. In the Polish tax system, the taxes belonging to this group are: tax on real estate, land tax, forest tax and tax on means of transport.
- 2) Taxes on the increment (taking over) of property. The taxation object here is the obtaining of an object or property rights by means of purchase, donation or inheritance. Here we classify tax on inheritance and donations.
- 3) Taxes on the growth of value of the possessed property. They are used when this growth can be attributed to reasons not associated with the owner. An example here can be a betterment levy (fee) and re-zoning fee, paid by real estate owners due to the fact that their properties gained in value as a result of providing services and utilities, geodetic division of land, changes to local spatial development plan, etc.
- 4) Taxes on transformation of property substance. These are taxes paid in case of the sale or exchange of things or property rights into other things or property rights. In Poland, they are present as tax on civil law activity.

In principle, a tax on land value only taxes location rents (returns on a particular location regardless of how distributed, such a tax should be

more progressive than a tax on land and improvements. Site value taxation thus scores well in terms of both equity and efficiency. Indeed, taxes on land are generally regarded as one of the least distortionary taxes, although more general taxes on property do, of course, distort decisions about improvements (investment) to property. The valuation of land alone is difficult, however, because most urban real estate sales combine the value of land and improvements. The value of improvements thus needs to be subtracted to derive an assessed value for the land. While some consider such taxation unacceptably arbitrary, others argue that valuation of land alone is probably easier than valuation of property and can often be estimated directly from sales and demolition records.³ In many such countries, land and improvements are in practice assessed separately in any case, with land value being estimated on the basis of a land value map and building value in accordance with construction cost tables. Another problem with taxing land only, however, is that, since the tax base is considerably smaller than the value of land and improvements combined, a higher and more distortionary rate is needed to generate comparable revenues.⁴ The legal analysis of the structure and features of property taxes allows us to put forward the following classification criteria:

1. The legal and economic process of generating and using income (the object criterion).
2. Specification of the object of taxation (economic criterion).
3. The relationship between normatively determined elements of the taxation technique (source, object, subject of tax) and the actual state (criteria of allocation of financial resources coming from taxes).
4. The method of quantifying the taxation base.⁵

Legal Dilemmas of the Flow Logic in Property Taxes

A fundamental feature of taxes is that they always constitute a flow, as they are paid by deducting parts of other flows generated by economic entities. In order to pay the tax, they have to give part of their incomes – in

³ See more: R. Bahl, *Land Taxes versus Property Taxes in Developing and Transition Countries*, in: *Land Value Taxation: Can It and Will It Work Today?*, ed. D. Netzer, Lincoln Institute of Land Policy, Cambridge, MA.

⁴ M.B. Richard, E. Slack, *Land and property taxation in 25 countries: a comparative review*, “CESifo DICE Research Report”, no. 3/2005, pp. 34–35.

⁵ P. Felis, *Elementy teorii i praktyki podatków majątkowych. Poszukiwanie ładu w opodatkowaniu nieruchomości w Polsce z perspektywy przedsiębiorców oraz jednostek samorządu terytorialnego (Elements of the Theory and Practice of Property Taxes. Searching for the Order in Property Taxation in Poland from the Perspective of Entrepreneurs and Local Government Units)*, Szkoła Główna Handlowa w Warszawie, Warszawa 2012, pp. 72–73.

case of direct tax, or expenses – in case of indirect tax; both these figures are classified as economic categories known as flows. This feature of taxes is called then the flow logic of tax.

The conclusion concerning the flow nature of tax is elementary, but brings serious, though not always noticed, consequences. Since the tax is a flow itself, then, firstly, when creating it as a category of public finance we should always define proper reference to the value of another flow; it should be created in line with the other flow, for example the flow of income, since only the flow is an effective source of income. The tax is a monetary flow and may only be referred to a monetary flow. It is paradoxical to see some legal activities taxed, even though they are of purely internal nature for enterprises. It turns out that there is a tax on payments towards the company working capital; company articles of associations are taxed with civil law activities tax, there is tax on changes to contracts, etc. Thus tax is, as a result, becoming a sanction without any economic justification.⁶

In case of property taxes, the taxation base for real estate tax or inheritance tax is the property value. The flow nature of the tax means that the taxpayer must pay it, giving part of their flow of income. Therefore, if the taxpayer does not have such flow, they have to devote their savings or take out a loan to pay the tax, and even to cash in the whole or part of the possessed property (inheritance). Therefore it only seems natural to argue that the property tax should not lead to the diminishing of the taxpayer's property (property substance).⁷ We may pose a question whether due to lack of economic logic in property tax it should be eliminated from the tax system. In my opinion, it should not, provided the taxation is imposed on the income generated by the property. Such an approach is economically rational, since even though property is the object of taxation and the taxation base is the value of this property, the tax is paid on the flow of income from this property. We can thus point at some situations in which property taxation is justified, even though taxes do not directly reflect in their structure the flow nature of taxation:

First of all, this taxation makes sense when the income obtained from the property is hidden and there are no formal grounds to collect tax on

⁶ Compare: ERES-ESSEC Education Seminar, Paris, December 2007; A. Paugam, *Ad Valorem Property Taxation and Transition Economies*, ECSIN, "Working paper", no. 9/1999; ERES-ESSEC Education Seminar, Paris, December 2007; A. Johansson, C. Heady, J. Arnold, B. Brys, L. Vartia, *Tax and Economic Growth*, OECD Economics "Department Working Papers", no. 620/2008.

⁷ S. Owsiak, *Finanse publiczne. Teoria i praktyka (Public Finances. Theory and Practice)*, PWN, Warszawa 2002, p. 156.

it. So property tax may be a form of indirect taxation of income, as it preserves in this case its flow nature.

Secondly, property taxation is justified when the state wants to exert pressure on the owners of manufacturing property to use it appropriately. An example here is the tax on land for construction, which encourages its owners to make it profitable.⁸ The desire to exert pressure on an economic entity to use its property effectively, or the willingness to tax hidden property may also serve as justification for taxation of large residential real estates. The tax imposing authority assumes that the real estate is or may be used for paid rental, so there is income obtained from it, though such assumption may often be completely unjustified and then we will observe the negative effects of the property tax.⁹ Taxation of production property, governed by the desire to activate inactive property, may lead to weakening the motivation to invest. An entrepreneur, faced with a prospect of paying tax on inactive property – even when such property cannot be efficiently used without his fault – will be afraid to take up the investment risk, especially in uncertain economic situation conditions. In this way, property tax worsens the economic situation.

Thirdly, property taxation is economically and socially justified when the owners of particular categories of property use state services related to that property and tax is a form of payment for these services. An example here is tax on transport means (construction and maintenance of roads) or betterment levy (increase in property value as a result of particular administrative and legal activities).

Fourthly, property taxation is justified when public authorities find it necessary to impose particular restrictions (high tax rates) on some forms of property when such forms are considered economically or socially undesirable, or when some ways of accumulating such property is considered improper. In fact, in such situations it is the flow that is taxed – the flow of incomes or transactions related to that property.

One of property tax forms is the cadastre tax, based on common assessment of real estate and tying the amount of paid tax to the real estate value (based on various parameters). However, the concept of assessing the tax according to market value, underlying the tax, is logically inconsistent. The market value of real estate originates only at the moment of performing a trade transaction and is an *ex post* category, therefore we cannot determine it in advance, as it is determined by the seller and the buyer, sometimes in a long process of complex negotiations. Only their

⁸ P.M. Gaudamet, J. Molinier, *Finanse publiczne (Public Finances)*, PWE, Warszawa 2002, p. 481.

⁹ J. Żyżyński, *Budżet i polityka podatkowa (Budget and Tax Policy)*, PWN, Warszawa 2009, p. 178.

cooperation may lead to the establishment of the price for such real estate, while prices of similar real estate “being a reference point for establishing the value of the real estate” are only one of many factors supporting, but not directly determining the final price for the real estate. The system of administrative valuations generates the risk of proper establishment of tax rates. They should take into account the taxpayer’s payment capacity, defined as their flow of incomes from which the tax can be paid, without being forced to resign from other needs the taxpayer may have. It should be remembered that apart from “market value of real estate”, there are other methods of establishing the level of taxation available.

Real Estate Taxation Systems and Their Classification

In particular national systems, the elements of tax construction (especially tax base, rates, tax exemptions and reliefs) have been formed by social and historical circumstances, which accounts for the fact that some countries have very particular solutions, unknown in other tax systems. However, we can indicate certain common features, typical of modern real estate taxation systems. A common element connecting modern tax systems is the fact that the real estate taxation base (with few exceptions only) is the real estate value (defined in many different ways).¹⁰ In most European countries we can see more than one local tax. We may differentiate two dominant models:

- Those in which real estate tax is the most important local tax. This group comprises, for example, Great Britain, France and Poland and nearly all Central and Eastern European countries that joined the European Union in 2004.
- Those in which income tax is the most important local tax. This group comprises mostly Scandinavian countries (Denmark, Sweden, Norway, Finland) and Switzerland, though the group may soon be joined by Croatia and Belgium, where the growing part of income is generated by the local authority addition to income tax. It sporadically happens that the main local tax is composed of various forms of tax imposed on companies operating in the territory of the commune (for example Hungary and Germany).¹¹

¹⁰ K. Firlej, Ch. Firlej, *Porównanie systemów opodatkowania nieruchomości w Unii Europejskiej (Comparison of Real Estate Taxation Systems in the European Union)*, „Progress in Economic Sciences”, no. 1/2014, p. 289.

¹¹ D. Alibegović, *Financing Local Governments: Draft Model*, Croatian Law Centre Zagreb; A. Bajo, I. Jakir-Bajo, *Local Government Finance in Croatia*, in: *Local Public Finance in Central and Eastern Europe*, ed. Ž. Šević, Edward Elgar, Cheltenham 2002.

As we can see, in most countries of this region local authorities introduce other taxes as well, mostly real estate taxes, though nowhere is it treated as the most important or even significant local tax. The maximum share in all revenues equals 6% and is achieved in Denmark, where the real estate tax rate ranges from 0.6% to 2.4% of the property value.¹² The other burdens are not imposed universally, though. For example, at the end of the 1990s real estate tax was collected by 200 out of 435 Norwegian self-governments, although we must bear in mind that in Norway only municipal communes may impose this tax.¹³

It should be emphasized that there are no international standards defining the principles of property tax constructions, there is not any universally accepted system of such taxes. Therefore, as pointed out by Leonard Ethel “the system of real estate taxation is understood differently, depending on the country in which it is applied”.¹⁴ The systems of real estate taxation in Europe vary significantly. The issue of real estate taxes is not covered by harmonization directives of the European Union.¹⁵ It is also difficult to indicate international standards defining basic principles of the structure of taxes on possessed property. Generally the real estate taxation systems used in the European countries can be divided into two groups: the systems based on the value of the real estate as determined in the cadastre of properties and the systems in which taxation base is the area of the real estate. The former links the taxation base to the market value, defined as the price for the real estate when trading it (selling price, replacement value, discounted incomes) or rent value, defined as the value of the rent paid in a given period of time. The natural character of the taxation base covers its unit value, defined as the area of the real estate (number of square meters of the area of land and buildings).

¹² J. Blom-Hansen, *Measurement of Decentralization: The Challenge of Danish Story*, paper presented at the conference Taxonomy of Grants and Measurement of Fiscal Decentralization, Paris, 10–11.03.2011.

¹³ L.E. Borge, J. Rattso, *Local Government Budgeting and Borrowing: Norway*, in: *Local Public Finance in Europe: Balancing the Budget and Controlling Debt*, ed. B. Dafflon, Edward Elgar, Cheltenham–Northampton 2002.

¹⁴ *Europejskie systemy opodatkowania nieruchomości (European Real Estate Taxation Systems)*, ed. L. Etel, BIS, Warszawa 2003, p. 7; more: L. Etel, *Reforma opodatkowania nieruchomości w Polsce (Reform of Real Estate Taxation in Poland)*, UwB, Białystok 1998, p. 13 and next.

¹⁵ Compare: R. Wood, H. Williams, *Industrial Property Markets in Western Europe*, E&FN Spon, London 1994; N. Lichfield, O. Connellan, *Land Value taxation for the Benefit of the Community: A Review of the Current Situation in the European Union*, Lincoln Institute of Land Policy, “Working Papers”, Cambridge MA, 2000.

As seen in practice, the actions taken in this area concern not bringing closer the construction of taxes, but standardizing the principles of registering real estate in their spatial, legal, and economic aspect as well as unification and standardization of the methods of real estate valuation for tax purposes. The existing differences in real estate taxation have not been eliminated by tax reforms conducted recently in many EU countries. The implemented changes mostly referred only to one section of the system and covered mainly the changes to valuation methods, shaping tax base or depreciation of the value of buildings and land. Due to such vital differences in taxes on real estate in European countries, it is extremely difficult to create a universal and precise definition of these public tributes in the European Union. A deeper analysis of the implemented systems of real estate taxation allows us to single out a group of regular tributes, related to broadly understood holding of property, which means they are used not only on the basis of the ownership rights but also on the basis of other laws and legal titles.

The practical differences between the possible ways of quantifying the taxation base boil down to the fact that the implementation of the quantity tax concept, contrary to value-based tax, does not guarantee tax authorities regular, real growth of revenues in times of inflation. The dynamics of the quantitative taxation base is significantly lower than value-based taxes, wince the size of taxation base expressed in physical units is free from inflation effects. Adopting the natural taxation base forces us to introduce the value-raising mechanism, usually in the structure of tax rates. Value-raising rules do not always, as witnessed by Poland, bring the expected results. Moreover, using a transparent mechanism preventing the decline in real quantity tax burden as a result of inflation processes is perceived by taxpayers as increasing tax burdens. Also in taxes on value we may expect the value-raising tax revenues, but this only concerns the taxation base. This solution is not visible, though, which undoubtedly decreases the scale of social dissatisfaction.

In countries which have not had taxes on real estate (for example Russia, Ukraine and other post-soviet countries) we may observe growing interest in placing burden on land. The buildings erected on that land will be taxed later on, after land tax stabilizes. Such an approach is attributed to the fact that establishment of rational principles of building taxation requires more preparation and information flow. Such buildings, contrary to land, are usually not shown in real estate registers created for non-fiscal purposes.

Real estate taxes are obligatory tributes, therefore the obligation to provide them results directly from the act of law, whereas local authorities are

only authorized to modify some elements in their construction (rates, tax exemptions and reliefs, mode of payment). The real estate taxation systems in the European Union contain some optional taxes, imposed at the discretion of local authorities. For example, properties located in Norway are subject to self-government real estate tax provided the commune used its rights to impose such a tax (it is usually used by municipal communes in Norway). It is therefore an optional tax, whose introduction depends on the decision of local authorities. Not all communes are interested in introducing it due to its collection costs which, in case of communes where there are not many properties to be taxed, may exceed possible revenues from taxation. Optional taxes on real estate are an exception to the rule that the obligation to pay a tax is determined by the act of law.

Taxable real estate may include such typical items as land and buildings, but also ships, pipelines, railways, technical networks, ponds and lakes, forests, swamps, mining excavations, sheds, land under truffle trees, phone booths, hedges, etc. What is classified as taxable property is determined by tax law regulations. Their analysis allows us to draw a conclusion that these can be too diverse things to propose one, universal definition that would cover them all. In this book, a taxable real estate will be understood as everything defined by the provisions regulating a given tax, regardless of its qualification in civil law and other branches of law. It should be emphasized though that these are things connected with land real estate understood physically and legally. Apart from a few exceptions (such as ships) the objects of real estate tax are the elements related to the land (buildings) or things situated on this land (such as a road, a hedge, networks, etc). Recurrent taxes on real estate property are considered to be the least detrimental to economic growth given the immobility of the tax base. This reduces the behavioral effects to this type of taxation which in turn minimizes the economic distortions. Recurrent property taxes on real estate are largest in the UK, Denmark and France. Malta stands out since it does not levy this type of tax at all.¹⁶

Legal Regulations of Cadastre Systems of Real Estate Taxation

Cadastre systems are typical of the EU countries, where the real estate taxation model is directly connected with the real estate cadastre. A dominant model of real estate taxation in the European Union countries is

¹⁶ Taxation trends in the European Union, European Commission: Publications Office of the European Union, Luxembourg 2016.

the cadastre system based either on the capital value of the property – an assessed price which can be obtained when selling the property in the free market, or rental value – the highest rate of annual rent that can be obtained when letting the property in the free market. All data necessary to determine the tax are contained in the cadastre, which definitely facilitates the realization and collection of tax in its object and subject aspect. A taxpayer is usually a subject seen in the cadastre who pays the tax on the property defined there. The large significance of cadastre in real estate taxation systems explains why they are called cadastre systems of real estate taxation. They are also frequently called ad valorem systems, taking into account their value as a base for real estate taxation. There are two types of cadastre: fiscal and legal. Fiscal cadastre shows close ties with the tax system since it comprises data necessary to determine taxes on real estate taxes, such as: taxpayer's data, property value and income obtained from it. It is mostly generated for the purposes related to real estate taxation, which does not exclude the possibility of using data contained in it for other purposes. Establishment of a financial cadastre is relatively easy, as it does not require creation of any ownership relations, which is connected with high financial expenditure. It is focused on registration and protection of material rights, though it may be used for tax purposes. It contains mostly information on ownership rights as well as other rights and encumbrances on real estate. Institutions of this type are related to land and mortgage registers and in some case even replace them. The implementation of a legal cadastre is preceded by sorting out ownership rights to particular real estate and establishing their boundaries, which is connected with large financial expenditure (land surveying work) and time-consuming. There are both fiscal and legal cadastres currently in use. In France the cadastre system is deprived of any legal nature and since its establishment it has been satisfying fiscal needs. The legal cadastre, on the other hand, is used in Germany. The fundamental differences in real estate taxation systems in the European countries mostly concern the level of revenues for the budget – in case of a value system it is constant, whereas in case of a quantity tax system, taking inflation into account, it is changeable. We also have significantly lower dynamics of the quantity tax base, since its size expressed in physical units does not depend on inflation.¹⁷

¹⁷ Compare: Z. Berliński, R. Hycner, *Granice nieruchomości gruntowych i ich związki z katastrzem nieruchomości (Limits of Real Estate and Their Relationships with Real Estate Cadastre)*, „Przegląd Geodezyjny”, no. 8/1999; W. Fedorowski, *Ewidencja gruntów (Record Land)*, PPWK, Warszawa 1974; R. Hycner, M. Mika, *System KW w Polsce – analiza stanu istniejącego w aspekcie przepływu informacji o terenie i tworzenia katastru*

In the EU countries the assessment of the value of representative property in order to establish the cadastral value and also in order to make taxation maps and tables is done by real estate surveyors. Cadastral values, determined in the process of common real estate taxation should reflect differences between particular properties and they should be as close to market value as possible with principles applied in mass valuation. The basis for establishing the cadastral value of particular properties are taxation maps and tables. The value is established for the whole property or its part if it was separated as taxation objects in the real estate tax provisions. The cadastral value of a land property is the cadastral value of the land and the cadastral value of its elements. A taxation unit with reference to the land is a plot of land or its part which is used for a different purpose than neighboring plots or remaining parts of the plot, determined in local spatial development plan or another way of using a given part of the plot if there is no such plan. A taxation unit with reference to elements of the land is a building, a flat in a multi-flat building or another premise permanently tied to the land. The property value in the taxation process is determined taking into account characteristic features of the property affecting its cadastral value. For this purpose two types of land are differentiated: developed land or land intended for development, as well as land intended for other than agricultural or forestry purposes and agricultural and forestry land. The typical features influencing the cadastral value of the former are: location, purpose determined in the spatial development plan or, if such plan does not exist – the way of using, its development (technical infrastructure), class of the soil if it was determined in the real estate cadastre.¹⁸ Typical features affecting the cadastral value of buildings are also: location, type of building and its use, internal installations, technical data as understood by regulations on real estate cadastre, degree of wear and tear. On the other hand, the features of premises affecting their cadastral value are: location in the building, type of building, way of using it, internal installations, degree of wear and tear.

nieruchomości (KW System in Poland – Analysis of the Existing State in Terms of the Flow of Information on the Area and the Creation of a Real Estate Cadastre), „Geodezja”, t. 6, z. 1/2000.

¹⁸ Compare: M. Mika, *Analiza wybranych systemów informacji o terenie w aspekcie katastru nieruchomości (Analysis of Selected Land Information Systems in Aspect Real Estate Cadastre)*, Rozprawa doktorska (tekst niepublikowany) 2002; A. Przewięźlikowska, K. Skotnicki, *Wykorzystanie pruskich i niemieckich oraz rosyjskich źródłowych materiałów katastralnych dla potrzeb współczesnych, wybranych prac geodezyjnych i zagadnień prawnych (The Use of Prussian and German and Russian Cadastral Source Materials for the Needs of Contemporary, Selected Surveying Works and Legal Issues)*, „Geodezja”, t. 7, z. 1/2001.

The advantages of introducing the cadastre tax include:¹⁹

- strengthening (increasing) the income base of self-government units;
- sorting out the issue of property ownership (for example positive influence on real estate trading safety);
- limiting the so-called grey zone of local taxes;
- an impulse for using the properties that have not been used so far (including commune-owned);
- it is socially justified (owners of more expensive properties pay proportionally higher taxes);
- positive influence on wealth distribution within the society (more proportional distribution of tax burden);
- limiting speculative investment in real estate.

The disadvantages of introducing the cadastre tax include:

- it is expensive to implement (for example it requires establishment of an integrated system of information on real estate);
- it requires completing and arranging data in the register of land and buildings and in land and mortgage register;
- possible increase in costs of property rental and use;
- it may be socially unfair (the size of tax burden does not depend on taxpayer's income);
- it weakens the inclination of some owners to renovate or modernize the real estate for fear of increasing its value (as this would be connected with the increase in the amount of due tax);
- the risk of deepening disproportions between poor and rich communes (differences between the taxation base value).

Real estate registers do not only serve fiscal purposes, that is collection of tax on such property. They were created first of all to ensure safety of real estate trading. Cadastral registers contain detailed descriptions of the property, registered transactions, debt burden. Everyone may obtain information they are interested in, usually paying some fees for it. Cadastre clients mostly include potential purchasers, investors, attorneys, public notaries, land surveyors. Real estate transactions are usually valuable, therefore they require the utmost diligence when making them. Therefore, for example in Poland they must be made in form of a notarial act or otherwise they shall be deemed null and void. The act on real estate introduces a common real estate taxation and applies property transaction prices to determine the cadastral value. This shows

¹⁹ A. Grycuk, *Zalety i wady wprowadzenia w Polsce podatku katastralnego (Advantages and Disadvantages of Introducing Cadastral Tax in Poland)*, in: *Uwarunkowania rozwoju rynku nieruchomości w Polsce (Conditions for the Development of the Real Estate Market in Poland)*, Instytut Funkcjonowania Gospodarki Narodowej SGH, Warszawa 2000, pp. 196–207.

that the cadastral value is supposed to reflect the real market value. Taxes on property value are used in nearly all Western European countries as well as in Canada, USA, Middle and Far East countries. It is assumed that the tax should encourage rational management of real estate and conducting a policy favoring the investment. It is considered fairer than the system based on the property area. Revenues from this tax constitute a significant percentage of the territorial self-government revenues in most countries applying this principle. (for example in Sweden the tax goes to the state budget). On average, all over the world real estate owners pay their communes a tax of 0.5% to 1.8% of the value of each property annually. Fiscal cadastre may determine at least four different values of the taxation base: market value, rental value, income value, register value.

A cadastre is an information system, functioning continuously, which means that it is not a one-off list of properties. It is official, therefore it operates on the basis of acts and regulations and is run and supervised by state or local administration bodies. The cadastre is a system of public information, available to all interested parties, who may use the data included in it for their own purposes.²⁰ The essence of the cadastre is full conformity of the data included in the land and building register with the information contained in the land and mortgage register. Due to the scope of collected information and goals to be accomplished, we may differentiate: physical cadastre (register of land and buildings); legal cadastre (land and mortgage registers) and fiscal cadastre (register of subjects and objects of taxation). The physical cadastre is a collection of information on the area, listing real estate located in a given area according to established borders and their detailed description. It contains plans, maps, descriptions and data determining the purpose and method of using a real estate.²¹

The legal cadastre is a register reflecting the legal state of the real estate. Its main goal is to register owners and rights to a particular property. It contains mostly data on the ownership rights and other rights as well as encumbrances related to the property, such as usufruct, perpetual usufruct, servitude, lease, hire, lending for use or management. In practice this function is performed by land and mortgage register (court register of properties). There is a close relationship between the legal and the

²⁰ K. Wójtowicz, *System opodatkowania nieruchomości w Polsce (Real Estate Taxation System in Poland)*, UMCS, Lublin 2007, pp. 15–16.

²¹ M. Wróblewska, *Kataster nieruchomości (Property cadastre)*, in: *Główne wyzwania i problemy systemu finansów publicznych (The Main Challenges and Problems of the Public Finance System)*, ed. J. Głuchowski, A. Pomorska, J. Szołno-Koguc, UMCS, Lublin 2009, p. 652.

physical cadastre, since data contained in the register of land and buildings form the basis for marking property in land and mortgage register. The implementation of the legal cadastre should be preceded by sorting out legal relationships of each property and determining their borders by means of precise geodetic measurement. Both of these activities are money and time-consuming. The tax register run on the data obtained from land and mortgage registers shows a strict relationship between tax and legal cadastres.²²

Practical Conclusions

A system of property taxation should be understood as a group of taxes valid in a given country, related to ownership as well as the legal transfer of particular property elements, subject to taxation on the basis of currently valid legal regulations. Principally, their constructional ties with property should be manifested – apart from the object of taxation itself – in the construction of the taxation base. The object of taxation in property taxes is referred to a wide circle of events, often quite heterogeneous. Thus we can venture to say that it would be difficult to adopt a solution consisting in universal definition of property which the lawmakers link to tax obligation. There is no doubt that the object of taxation in property taxes has a broad scope, therefore it requires that the definition of property be adopted in its narrow or broader sense. For the purpose of this dissertation – due to the fact of narrowing research areas to taxes placing burden on possessing property – we assumed the definition of property in its narrow meaning (property mass covering only particular assets accepted by the lawmakers).

In practice, the tax policy task, apart from its fiscal function is to ensure the possibility of regulating and stimulating influence on social and economic processes.²³ With reference to property taxes, legal regulations should not omit (also with reference to implemented reforms) social and economic contexts of territorial self-government operations. It should be remembered that the expectations towards property taxes cannot be too

²² *An International Survey of Taxes on Land and Buildings*, eds. J.M. Youngman, I.H. Malme, Kluwer Law and Taxation Publishers, Deventer 1994. B. Yuan, K. Connolly, M.E. Bell, *A Compendium of Countries with an Area-Based Property Tax*, “Working Paper Series”, Lincoln Institute of Land Policy, Cambridge 2009.

²³ Compare T. Skica, T. Wołowicz, *Gminy w procesach stymulowania przedsiębiorczości (Municipalities in the Processes of Stimulating Entrepreneurship)*, „Samorząd Terytorialny” 2013, nr 7–8, pp. 88–104; T. Wołowicz, T. Skica, *The Instruments of Stimulating Entrepreneurship by Local Government Units (LGU's.)*, “Ekonomiska Istraživanja”, no. 4/2013, pp. 127–146.

high, we should also remember to take into account specific features of property taxes. Therefore in each tax policy shaped by legal norms there should be a postulate related to effective use of real estate, shaping rational special structure in cities and tax solutions ecology-oriented.

The diversity of views on classifying taxes on agriculture and forest land, developed and undeveloped urban real estate as belonging to the categories of property taxes, revenue taxes or mixed taxes, encourage us to propose certain solutions limiting negative legal and economic phenomena within property taxes. From this perspective the following would be desirable:

- 1) To organize legal regulation of property taxes by adopting permanent, easily identifiable features;
- 2) Everywhere there is separate taxation of agriculture and forestry, general principles of taxation should be introduced (for example income tax – an example of a tax imposed on generating income, property tax on the value of possessed real estate – an example of taxation on resource, VAT tax – an example of a tax imposed on the use of income);
- 3) Taking into account mechanisms of substantive selection promoting development goals, limiting disturbances to the market mechanism;
- 4) Detailed analysis of necessary elements in the construction of taxes placing burden on real estate (for example residential, agricultural, forest and other) in order to reject the unjustified approach consisting in freely determining where these taxes belong;
- 5) To simplify tax constructions in order to eliminate elements typical of revenue taxes.

Analyzing the legal and formal division of taxes into direct and indirect ones, we should take the utmost care when dealing with criteria for determining the features of property taxes belonging to direct taxes. I believe we should constrain the features of direct taxes to the least controversial ones, namely:

- 1) Direct taxes are those imposed on the income or property belonging to a taxpayer or being at their disposal in a way that allows them to obtain gains property;
- 2) The object of taxation is identical with the actual source of tax (direct relationship), since generated income or possessed property directly refer to the money with which the tax will be paid;
- 3) Direct taxes are those directly related to taxpayers tax capacity, as they are imposed directly on the source of income;
- 4) Direct taxes are those with reference to which there are possibilities of using relevant administrative registers of taxpayers and their incomes and property (cadastres) for determining their taxes;

5) Direct taxes are those that are closely related with the effects of an economic activity.

The property tax system is founded by a number of principles: uniformity, neutrality, stimulation of direct investment, transparency, public acceptance, buoyancy and cost effectiveness. Uniformity: implies proportional taxation in correlation with the “ability to pay”. A market value based system could represent a fiscal benefits because avoid the case in which taxpayers paying less than they might be willing to accept. Neutrality: a efficient tax system not distort economic decisions and encourage an optimal mix of factors of production (capital, workforce, management and land). Stimulation of Direct Investments. Tax preferences and incentive are sometimes used to attract investment in a particular area. Transparency is a characteristic of democratic society. Buoyancy is related with the ability of tax to rise or to fall in accordance with the economic evolution.²⁴

Almost all local governments worldwide rely, at least to some extent, on property taxation to pay for local services. Economists have long argued that the property tax is a good tax for local government because it is fair (in relation to the benefits received from local services), it is difficult to evade, and it promotes local autonomy and accountability.²⁵ Although most of the literature talks about “the” property tax as if it were one tax, it is really two different taxes – a tax on residential property and a tax on non-residential property. The economic case for the residential property tax is quite strong; the same cannot be said of the nonresidential property tax. In practice, however, in most countries where property taxes are levied, the tax rate is higher on non-residential properties than on residential properties.

Economists consider residential property taxes to be appropriate as a source of revenue for local governments, in large part, because of the connection between the types of services funded at the local level (for example, good schools, access to roads and transit, and so on) and the benefit to property values. To the extent that people understand that their property taxes are being used to pay for local services, there is a link

²⁴ See: I. Anghel, C. Sopsis, *Valuation for property tax purpose. Analysis of the EU transitional countries*, http://www.fig.net/commission7/Hungary_2012/6.4_paper_anghel_et_al.pdf (last visited 22.02.2105); R. Grover, I. Anghel, V. Pamfil, *Developing quality training approaches for effective property tax administration*, ERES-ESSEC Education Seminar, Paris, December 2007; A. Paugam, *Ad Valorem Property Taxation and Transition Economies*, ECSIN, “Working Paper”, no. 9/1999.

²⁵ R.M. Bird, *Subnational Revenues: Realities and Prospects*, World Bank Institute, Washington DC 2001.

between the benefits and costs of local services that encourages them to make efficient fiscal decisions.²⁶ Both the benefits derived from local services and the taxes are capitalized into property values these services translates into higher property values. Higher taxes, other things being equal, translate into lower property values, because purchasers faced with two similar houses will offer less for the house with higher taxes. The property tax (based on the market value of land and improvements) discourages building and results in the under-utilization of land. That is, the amount of capital per unit of land is less than the economically efficient amount. Both the benefit-based and capital tax views have some validity. The property tax is not purely a benefits tax, because homeowners who improve their houses face higher taxes, which would, in theory, discourage them from doing so. At the same time, the benefits of local programs are reflected in local property values. Another reason that the property tax is regarded as a good tax for local governments is that property is immovable – it cannot shift location in response to the tax – and it cannot be hidden. Even the owner of a vacant property is taxed under the property tax. These characteristics make it difficult to evade. Although a change in property tax may be capitalized into property values in a particular community, and in the long run tax differentials may affect where people locate, these effects are smaller than the distortions created by income and sales taxes at the local level. This characteristic of the property tax makes it somewhat easier to levy and collect than other taxes and thus offers municipalities the potential to raise significant revenues.²⁷

All governments had to deal with various aspects of property tax policy design – determining what is included in the tax base, assessing properties, setting tax rates, and administering the property tax system – although the focus was different in different places. This conclusions presents each of these elements of property tax reform in a little more detail. Bahl²⁸ sets out several logical steps in preparing a property tax re-

²⁶ See more: W.E. Oates, *Local government: An economic perspective*, in: *The Property Tax and Local Autonomy*, eds. M.E. Bell, D. Brunori, J.M. Youngman, Cambridge, Mass.: Lincoln Institute of Land Policy, 2010, pp. 9–26.

²⁷ Based on: E. Slack, *The Property Tax in Theory and Practice*, Institute on Municipal Finance and Governance, Munk School of Global Affairs, University of Toronto, no. 2/2011.

²⁸ See: R. Bahl, *Property Tax Reform in Developing and Transition Countries. paper prepared for Fiscal Reform and Economic Governance Project*, USAID, December 2009; R. Bahl, J. Linn, *Urban Public Finance in Developing Countries*, Oxford University Press, New York 1992; R. Bahl, S. Wallace, *Reforming the Property Tax in Developing Countries: A New Approach*, paper presented to a conference on “What Role for Property Taxes?” Georgia State University and Lincoln Institute of Land Policy 2008.

form: (1) do a detailed diagnostic of the current system to understand what is working and what is not as well as to determine clearly the objectives of the reform – revenue mobilization, fiscal decentralization, land use control, etc.; (2) develop an appropriate tax policy design with respect to choice of tax base, rate structure, exemption policies, etc.; (3) design the administrative reforms needed to implement the tax designed such as coverage, valuation, record keeping and collection; and (4) monitor carefully the success of the reform with such quantitative indicators as collection rate, revenue collections, assessed to market value ratios, etc. This advice seems sound but it is unclear that any country has actually done all this and, as the cases in Section 2 above suggest, politics seems to have dominated most country discussions of property tax reform and largely determined the outcomes.

The first key design question is what should be taxed. Some properties are exempt in most jurisdictions. For example, property owned and occupied by government is generally exempt from property taxes. Other property types that are often exempt include colleges and universities, churches and cemeteries, public hospitals, charitable institutions, public roads, parks, schools, libraries, foreign embassies, and property owned by international organizations. In some countries, agricultural land and principal residences are also tax exempt.²⁹

Some countries use variants of self-assessment, under which property owners place an assessed value on their own property. In the case of Ireland, for example, taxpayers are required to determine the value of their property and choose the correct value band. Self-assessment is an appealing procedure to countries with little administrative capacity. It does not appear to require expert assessment staff, and it seems to be easy to implement. In general, however, self-assessment seems likely to lead to inaccurate estimates of property values, with a tendency toward under-estimation. Since lower-valued properties are generally less under-estimated than higher-valued properties, this approach tends to produce regressive results with taxes being relatively higher on low-valued properties. To minimize the obvious problems of under-statement associated with self-assessment, governments must be prepared to obtain (often costly) expert assessments of individual properties in cases where it believes self-assessment is inaccurate.

²⁹ G. Färber, M. Salm, S. Hengstwerth, *Property Tax Reform in Germany – Eternally Unfinished or an Instrument of a More Equitable (Local) Tax System?* Paper presented to the Copenhagen Workshop, September 12–13.2013.

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