POLICY BRIEF

Enhancing Revenue Generation and Progressivity of Property Taxation in Kenya

December 2023

The 2010 Kenyan Constitution, in Article 209(3), assigns the responsibility of collecting property taxes to county governments. However, property tax revenues currently constitute a relatively small portion of the total revenue that county governments generate. Furthermore, there is significant untapped potential from this revenue source. The Commission on Revenue Allocation (CRA) estimates that property taxes collected across counties amount to just 36 percent of their potential: counties collected Ksh 5 billion in FY 2019/20 out of the potential Ksh 14 billion property tax potential across the country.[1] Property taxes accounted for less than 0.1 percent of the Kenya's Gross Domestic Product (GDP) in 2021, which is lower than the 0.3 percent average for African countries.[2]

Property taxation in Kenya is marked by several challenges. Outdated valuation rolls have led to many valuable properties escaping taxation altogether, while others are taxed at values lower than their actual worth.[3] The property tax system is also inequitable as some counties continue to levy property rates on unimproved site value. Limited use of technology and infrequent assessment also undermine the efficiency of the property tax system. Also, low compliance and enforcement mean that many Kenyans do not pay their property taxes and face few consequences, if any.

To improve revenue generation and the progressivity of Kenya's property tax system, reforms are needed. This brief identifies seven (7) critical reforms which are detailed in the preceding section:

i. Update property valuation rolls,
ii. Change the system of assessment from one that targets unimproved land to one that targets both land and improvements,
iii. Adopt more frequent assessments,
iv. Introduce technology to permit more regular, consistent and low-cost assessment,
v. Use a simplified points-based system for rating,
vi. Improve the administration of land titling, and
vii. Work with Kenya Revenue Authority and/or private agencies for stricter enforcement

We then look briefly at the challenge of political opposition to tax reform and offer some possible solutions to these obstacles.

[1] Comprehensive Own Source Revenue Potential and Tax Gap Study of County Governments. Link .
[2] Revenue Statistics in Africa 1990-2021. Link.
[3] Rose Wanjiru, Anne Wanyagathi Maina and Eldah Onsomu and Graeme Stewart-Wilson. "Local Government Property Tax Administration and Collaboration with Central Government: Case Studies of." (2019). Link.

1. Updating the valuation rolls stands out as the most critical reform in property taxation

The outdated nature of the current valuation rolls limits the progressivity of property taxes, both because many properties are missing from these rolls, and because those that are included are undervalued. This is a common problem across Africa; it is estimated that between 50 to 70 percent of properties are not recorded in many African countries.[4] For Nairobi City and Mombasa counties, the valuation rolls date back to 1982 and 1991 respectively. Kisumu County uses its 2008 valuation roll which covers 25,284 properties with a total estimated value of US$ 127 million. This roll, however, falls significantly short as there are approximately 55,000 properties in the county, collectively valued at US$ 1 billion.[5] Outdated rolls fail to capture the present market value of properties, which means that high-value properties are consistently assessed at lower values than their true worth and thus wealthy property owners end up paying lower taxes than they should.

2. Change the system of assessment to an improvement rating system

Once the rolls are updated, or even as that process is ongoing, counties can move away from the current practice of taxing only unimproved sites value to imposing taxation on improvement rating. To guide the imposition of property rates, the Rating Act (Cap 267) of 1963 provides for three rating systems: Unimproved Site Value Rating (USV), Improvement Rating (IR), agricultural rental rate and Area Rating (AR). The unimproved rating is levied on land only while the improvement rating includes the structures developed on the land. The area rating is levied on agricultural land at a flat rate and is based on the size of land and location only. Notably, despite the different options available in the regulatory framework, the primary tax base in Kenya is the unimproved site value (land only).

Property taxes should be imposed based on the Improvement Rating system, which ensures that the real value of both land and improvements is taxed. The taxation of land only means that the tax base is narrower and less progressive as the wealth inherent in buildings is excluded. Countries such as South Africa, Guinea and Tunisia impose taxes on both land and improvements.[6] In such cases, the standard practice tends to be an imposition of a lower tax rate for improvements compared to the land to avoid overburdening the taxpayers.

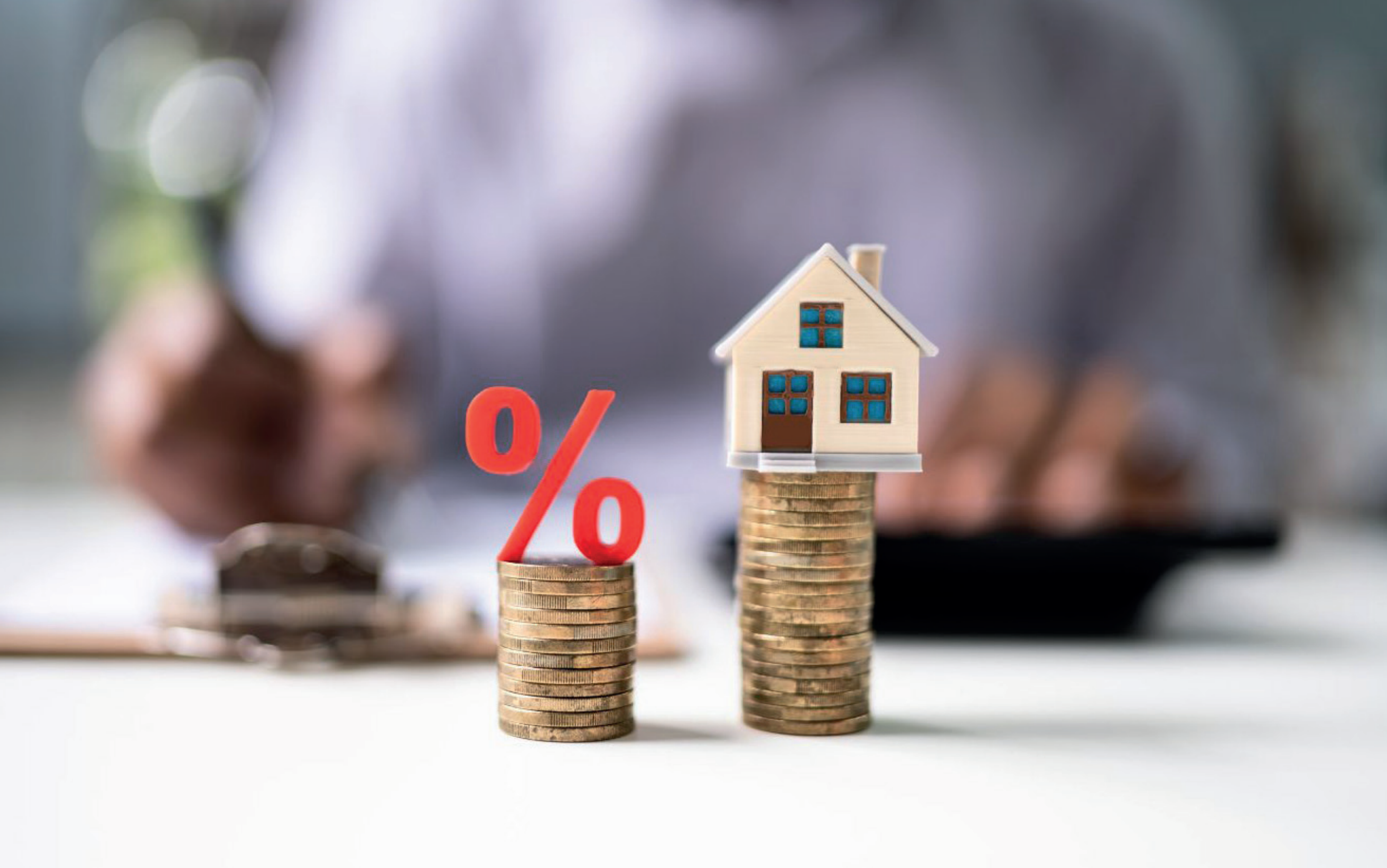
3. Adopt more frequent assessments

Whatever system is used for assessing value, Kenya should adopt more frequent assessments of property. The Valuation of Ratings Act, 1964 mandates every local authority to conduct valuations at least every 10 years. But supplementary valuations should occur every year after the year of valuation unless there are no alterations or additions needed in accordance with the act. The National Rating Bill, 2022 (re-submitted to the 13th Parliament after it had lapsed in the 12th Parliament) aims to increase the frequency to every 5 years, which would be ideal for keeping the rolls updated. The Bill was passed in the National Assembly and forwarded to the Senate for consideration.[7] To facilitate regular valuations, more cost effective and less labor-intensive approaches such as the simplified points-based system can be adopted, which we describe below.

4. Introduce technology to reduce the cost and enhance accuracy of assessment

County governments should leverage on Information Technology (IT) to simplify and improve efficiency of the tax system. IT systems are widely recognized for their critical role in improving property taxation systems. They are instrumental in addressing capacity constraints, promoting transparency, and improving administrative efficiency. The updating of valuation rolls is a repetitive and often resource-intensive process. However, integration of IT processes such as Computer Aided Mass Appraisal (CAMA) can

[4] Assessment of the effect of waiving interest accrued on land rates arrears in Nairobi County. Link.
[5] Rapid Own Source Revenue Analysis of Kisumu. Link.
[6] Property Tax in Africa. Status, Challenges, and Prospects. Link.
[7] The National Assembly, Bill Tracker. Link.



help expedite and improve the process. CAMA refers to the use of technology to automate aspects of the property tax system such as property identification, data collection and property valuation. This allows for numerous properties to be assessed at a given time using econometric models, rather than inspecting and valuing each parcel individually, as is the case in the costlier single parcel appraisal approach.[8] Furthermore, in areas where local maps are inadequate, CAMA systems can be seamlessly integrated with Geographic Information Systems (GIS) or Global Positioning Systems (GPS) to simplify the identification of property and generate property maps.

The CAMA systems can also be programmed to use the more simplified points-based system for valuation, discussed further below.[9] In Kenya, the land value in the valuation rolls has historically been based on the market value. In this approach, the value of the land is the price that a willing and informed buyer would buy the property. Adoption of this approach has however been problematic in African countries due to several reasons: shortage of qualified valuers to undertake the valuations in the appropriate frequency, high cost of undertaking valuations in this approach, susceptibility to corruption through collusion between valuers and property owners, and poorly developed property markets which makes it difficult to find accurate information on comparable transactions that would inform the market value of a property.[10]

5. Use a simplified points-based system for rating

The International Centre for Tax and Development (ICTD) recommends that African countries adopt an alternative method, the points-based approach. Points, rather than prices, are assigned to the property. The points are based on the surface area of land or building, with additional points being added for positive features such as the location, and construction materials and deducted for negative features such as poor drainage.[11]

The local authorities, however, with support from valuation officers, will still have to establish the tax amount to be levied for each valuation point, which is known as the mill rate. One way of calculating the mill rate is by dividing the total revenue that is needed from property tax by the total points of all the properties in the jurisdiction. However, this approach may result

[8] Prospects of applying Computer Aided Mass Valuation in Tanzania. Link.
[9] Valuation for Rating Act. Link.
[10] Valuation for Property Tax Purposes. Link.
[11] Training Manual for Implementing Property Tax Reform with a Points-Based Valuation. Link.

in a mill rate that is too high or too low for some taxpayers depending on their income levels. Therefore, the local authorities should also consider the equity and efficiency implications of the mill rate when setting it.

The points based approach is highly advantageous for its simplicity in implementation. Given that it is undertaken based on a formula, it can easily be automated, leading to a more efficient administration of taxes. Additionally, updating the valuation roll would be easy and cost-effective as one does not require a valuer to be present. It is also progressive as it accounts for different property characteristics, ensuring that higher taxes are imposed for properties with higher value and vice versa. It also makes it easier to adopt improvement rating.

One of the successful examples of the points-based approach is the Revenue Mobilization Program (REMOP), an Urban Tax Administration System for the automation of property taxation, which was launched by Mzuzu city in Malawi in 2013. Prior to the inception of the program, the city's property tax administration encountered similar challenges as Kenyan counties including, outdated valuation rolls, low revenue collection and incorrect property assessments. The points based system solved these problems and increased property tax revenues in Mzuzu seven-fold from USD 68,000 in 2013 to USD 478,000 in 2018. The increased revenue was attributed to enhanced accuracy in capturing all properties, as their values were previously often left out of the valuation roll due to lack of property market data. A second reason for the increase was improved transparency of the valuation process and communication with property owners which encouraged compliance and reduced disputes (the demand notices sent out to the property owners provided information about how their property values and tax amounts were calculated and they could verify the accuracy of the information). Moreover, the system was cost-effective, costing between USD 300,000 and USD 400,000 as compared to the previously used market value-based approach which costed approximately USD 1.9 million.[12]

6. Improve the administration of land titling

Streamlining the titling process would expedite the issuance of titles to citizens, minimizing disputes and facilitating more efficient property tax administration for county governments. Data from the Kenya Demographic and Health Survey (KDHS) 2022 shows that a substantial proportion of property owners lack concrete proof of ownership for their holdings. Currently, 44 percent of women and 43 percent of men who possess non-agricultural land lack the title deeds for these properties.[13] This poses a challenge in identifying the responsible party for the tax obligations associated with the parcel of land.

This can partly be attributed to delays in the registration process for land. While corruption has been a contributing factor, these delays could also be attributed to the manual process of registration used initially. This manual approach resulted in numerous inefficiencies to the extent that the Ministry of Land encountered challenges accessing its own land records in a timely manner. At times, critical documents were either misplaced or entirely missing.[14] In 2021, the National Lands Information Management System, 'Ardhi Sasa', was launched to digitize the land registration process. However, the system has faced challenges, including delays in the registration process and limited uptake of its services by citizens. Another significant hurdle has been the lack of adequate training for staff on operation of the system, which has restricted the extent to which they can resolve arising issues.[15]

The Ministry of Lands, Public Works, Housing and Urban Development should improve the titling process and foster information sharing with the county governments. This would also make it easier for county governments to administer property taxes, as they would have updated information on land ownership and transaction. Currently, the Ministry has a more comprehensive database on property ownership as all land transactions are processed at the national level. However, this means that counties governments

[12] Enhancing the financial position of cities: Evidence from Mzuzu. Link.
[13] 2022 KDHS Key Indicators Report. Link.
[14] Performance Audit Report of the Auditor-General: Waiting-time in Registration of Land Titles. Link.
[15] Better understanding: Analysis of the National Land Information Management System (Ardhi Sasa). Link.

are unaware of any changes in land ownerships and divisions. Therefore, there should be collaboration and information sharing between the Ministry of Lands and county governments so that they can access the database and acquire the information they need.

7. Work with Kenya Revenue Authority and/or private agencies for stricter enforcement

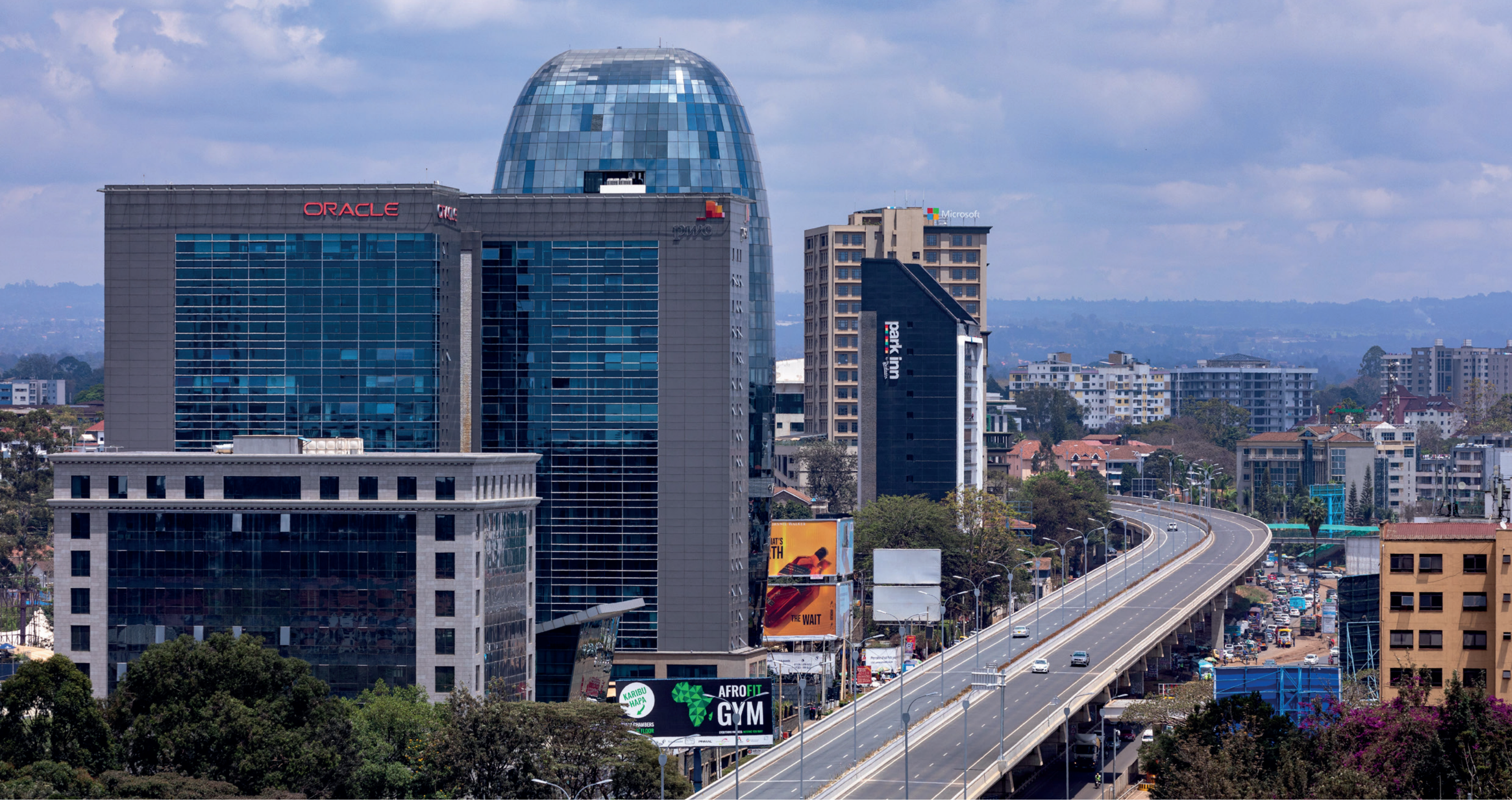
Property reforms are important, but they need to be accompanied by effective collection and enforcement, otherwise counties will lose significant revenues. However, current property tax administration is weak in enforcing and collecting property taxes, resulting in sub-optimal revenue collection. It is estimated that Nairobi City County collects approximately 45 percent of the billed amount while other counties such as Kiambu County collects only about 10 percent. Some of this might be due to defaults, but other administrative factors such as inadequate staffing for enforcement and reliance on manual billing systems also play a role. Furthermore, there are difficulties delivering the bills as 50 percent of the mailed notices are returned as undeliverable. This is because the information held by counties, including addresses of property owners, is at times inaccurate or out of date, which also makes following up on arrears rather difficult.

Moreover, the current approach to dealing with non-compliance is counterproductive. The Rating Act provides that for any defaults in payments, a monthly interest of three percent per month is to be charged. This is supposed to discourage non-compliance, but it is often ineffective as counties tend to frequently waive the penalties on land defaulters. A recent example of this is the County Government of Nakuru which offered a 100 percent waiver on the land rates for amounts outstanding up to 30th April 2023.[16] This creates an incentive for defaulters, as they know the consequences are not likely to be severe.

County governments can improve revenue collection by partnering with the Kenya Revenue Authority (KRA). Through this approach, counties get to benefit from KRA's personnel, technical expertise, and resources, such as automated systems to undertake the revenue collection. KRA has assisted counties in developing their own automated revenue collection systems, such as the Nairobi Revenue System (NTS), which was jointly created by the Nairobi Metropolitan Services and the KRA.[17] Alternatively, county governments can outsource the KRA as the primary revenue collection agent. This approach would require that county governments pay KRA a service fee of 2 percent of the collected revenue, which may be good value if KRA is effective in increasing revenue collection substantially. To ensure smooth implementation of such a partnership, county governments should ensure there is public participation in the process. Some counties, such as Kiambu and Laikipia, have encountered challenges in the implementation of their Memorandums of Understanding (MoUs) with KRA due to court cases challenging the agreements for lack of public participation.[18]

Another option for county governments is to outsource arrears collection to private sector players. This involves contracting external firms or agencies that specialize in recovering unpaid dues from defaulters. This has been successful in Kisumu County, which contracted Collection Africa Limited (CAL), a private debt collection firm in March 2019, to recover all arrears. By the end of the first month of CAL's arrears collection efforts, the land rates revenues had increased threefold compared to the revenue collected in the same month for the preceding year.[19] However, for this to work, county governments must provide the contracted parties with accurate and up-to-date data including the demand notices and property ownership information. They must also honor their financial obligations to them, such as paying the agreed fees or commissions within the agreed upon timelines. Without this, contracted parties may lose their motivation and lack the financial resources to maintain their scales of operation.

[16] County Government of Nakuru. Waiver of 100% Interest on Land Rates from 1st May to 28th June, 2023. Link.
[17] New Revenue Collection System For Nairobi City County Operationalized. Link.
[18] Local Government Property Tax Administration and Collaboration with Central Government: Case Studies of Kiambu, Laikipia and Machakos Counties, Kenya. Link.
[19] Enhancing the financial position of cities: Evidence from Kisumu County Government. Link.



Even when we know what reforms are needed, property tax reforms always face political resistance.

One of the most frequent obstacles to property tax reform is lack of public support. Numerous cases of financial mismanagement in Kenya have eroded public trust in the government's ability to prudently utilize the revenue raised from citizens and ensure that proposed reforms are in the best interests of the public. In some instances, the public may also be skeptical about the reforms because they do not understand them. Currently, most Kenyans are aware of the existence of property rates but cannot calculate their own property tax obligations. A study undertaken in Machakos, Laikipia and Kiambu counties found that only 33 percent of residents could do this. Such limited knowledge creates a fertile ground for skepticism of any reforms that might increase the tax burden. Furthermore, the existing fiscal social contract with taxpayers is weak, as citizens often fail to see a direct correlation between services provided by government and their tax payments.

The political class often benefits from the status quo and does not support tax reform. They are able to exploit loopholes and inefficiencies of the current property tax system. They may own undervalued land or use their influence to avoid paying taxes. For example, in Kisumu city, defaults in land rate payment are most prevalent among the elites and State-Owned Enterprises. Those political leaders that do support reforms may face opposition from other influential groups, such as the business community, who may stir up public or media criticism against the reforms.

Resistance to property reforms is already evident in Kenya. An example of this is in Nairobi City County, where there was an unsuccessful attempt to phase out the outdated valuation rolls. In 2019, a draft valuation roll was prepared at a cost of Ksh. 374 billion, provided by the World Bank through the Nairobi Metropolitan Services Improvement Project (NAMSIP).[21] However, despite the substantial investment in the preparation of the roll, it is yet to be adopted due to objections from property owners within the county.[22] This confirms the need for a strong political leadership to drive reforms.

Some measures can be taken to overcome the obstacles to property tax reforms.

To garner public support, local governments should establish a clear link between property tax reforms and improved public services.[23] Tax reforms only become socially desirable if they result in improved service provision to citizens. County governments should move

[21] Draft National Valuation Roll. Link.
[22] County Budget Review and Outlook Paper 2022. Link.
[23] Linking Property Tax Revenue and Public Services. Link.

beyond merely providing civic awareness programs and amplify the involvement of citizens in the formulation of reforms. This can be achieved by actively consulting with citizens to identify their primary needs, such as healthcare or education. Subsequently, county governments should set targets for improvement in these areas, which can then be used to determine property tax targets. The revenue collected should be earmarked to fund projects that meet the goals. This way, citizens have a sense of ownership in the reform process and understand the specific projects their taxes will fund. This strategy worked in Mzuzu city, where the property tax reforms were linked to improved waste management in the city from the onset.

County leaders, such as governors, senators and members of county assemblies are key drivers of property tax reforms. Therefore, there is a need to convince them of the benefits of such reforms for local development. Civil Society Organizations (CSOs) can engage them in constructive dialogue with evidence-based research and best practices from other countries and regions that have successfully undertaken property tax reform. Other stakeholders, such as the private sector, should also be part of the dialogue to build trust and consensus on the need for and direction of property tax reform, as well as address any potential conflicts and tradeoffs that may arise.

Civil society can influence county governments to adopt new reforms by running advocacy campaigns. These campaigns can include an analysis of the reforms and their benefits and use the media to disseminate them. Such CSO-led advocacy campaigns have been successful for tax reforms in different contexts and can be applied to property tax reforms in Kenya. For example, in 2012, the Action for Economic Reforms (AER) in the Philippines campaigned to increase the sin taxes for better health financing. To persuade the public and pressure the government, different tactics were adopted including engaging with the media by writing press statements, taking part in medial briefings, and writing opinion editorials as well as forming coalitions. The advocacy campaign helped overcome the vested interests of the tobacco and alcohol industries which had blocked similar reforms in 1997. In the end, the campaign was successful, as there was an increase in the sin taxes, which resulted in a decrease in smoking rates and an increase in the country's health budget.[24]

In sum, property tax reforms in Kenya are necessary for improved revenue collection and a more equitable tax system.

We conclude with specific calls to action from different stakeholders to achieve the seven reform areas we have enumerated in this brief:

Ministry of Land, Public Works, Housing and Urban Development. Given that the national government is still in charge of establishing policy and regulatory frameworks for the administration of property tax, it should provide for implementation of the simplified points system in place of the market value approach currently in use. Additionally, the ministry should work toward simplifying the Ardhi Sasa system for increased uptake and to eliminate delays in the registration process. Data from Ardhi Sasa will be instrumental in the implementation of modern valuation approaches such as the point-based valuation by counties.

National Assembly. Parliament should expedite enactment of the National Rating Bill to pave way for reforms in updating of valuation roll.

County governments. Counties should actively focus on updating their valuation rolls and conduct civic education on the reforms to be undertaken and their importance. Counties should also work with KRA or private agencies to enhance enforcement, while curbing the use of waivers.

Kenya Revenue Authority. KRA should pursue collaborative partnerships with county governments to provide technical expertise and contribute to the enforcement of property taxes.

[24] The Philippines: Critical Collaboration and Adaptability to Influence Tax Reform. Link.

This policy brief was authored by Gladys Wachira and Veronicah Ndegwa with guidance from Ruth Kendagor. Special thanks to our Senior Technical Advisor, Jason Lakin, PhD for his invaluable input. Immense gratitude to James Muraguri for his leadership. Special appreciation to Oxfam-Kenya for their financial and technical support, which went a long way in making this publication possible.

The findings and conclusions contained within are those of the authors and do not necessarily reflect positions or policies of Oxfam-Kenya.

Policy Brief, 2023