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Warsaw 2009 Abstracts

Sessions on Policies, legal and institutional frameworks

- [Property Taxation and Informality: Challenges for Latin America \(M. M. Smolka, Lincoln Institute of Land Policy, USA\)](#)
- [Can the “unearned increment” in land values be harnessed to supply affordable housing? \(Ms. R. Alterman, Center for Urban and Regional Studies, Israel\)](#)
- [An increase in the value of land as a prerequisite of imposing adjacency levies – critical analysis \(M. M. Gdesz, Administrative Court, Poland\)](#)
- [Land Value Tax as an Investment Mechanism for Public Transport Assets \(Ms. F. Medda, University College London, Great Britain\)](#)
- [More than a tax: some ethical implications of land value taxation \(M. R. Giles, Association for Good Government, Australia\)](#)
- [Taxing Public Leasehold Land in Transitional Economies \(M. Y. Hong, Lincoln Institute of Land Policy, USA\)](#)
- [Public Space and its Uncontrolled Appropriation in the Light External Effects Theory – Recommendations and Direction for Public System Intervention \(M. T. Markowski, Lodz University, Poland\)](#)
- [The UNECE Working Party on Land Administration after Ten Years: Policy Guidelines for Sound Land Management.\(Ariel Ivanier, UNECE\)](#)
- [Housing sector reform in Central and Eastern Europe: regulatory framework and policy development\(Mr. Claudio Acioly, Chief Housing Policy Section of UN-HABITAT\)](#)

Sessions on Land and property taxation in practices

- [Improving public-value capturing in urban development \(M. D. Muñoz Gielen, Radboud University Nijmegen, The Netherlands\)](#)
- [Improvement of land and property taxation in Montenegro as part of municipal land management and in relation to other countries in South-East Europe \(Ms. Y. Müller, German Technical Cooperation - GTZ, Montenegro\)](#)
- [Innovations in Property Taxation System in India \(Ms D. Kundu, National Institute of Urban Affairs, India\)](#)
- [Taxation and its effects on sustainable development with reference to the UK \(Mr. G. McGill, Planning and Development consultant, Great Britain\)](#)

Session on Land and property taxation: implementation and tools

- [Space Syntax as a Tool to Asses the Property Value \(Mr. A. Saeid, Wroclaw University of Technology, Poland\)](#)

- [Land Value Capture: Case Studies, Policy Implementation, and GIS Land Value Mapping \(Alanna Hartzok, Earth Rights Institute, USA\)](#)
- [Land and property tax: financing towards equality in access to housing, serviced land and infrastructure in post-apartheid South Africa \(Mr. M. Hendricks, Development Action Group, South Africa\)](#)
- [The system of land use charges in the Federal Republic of Germany. The lessons for the transition countries \(Ms J. Kopietz-Unger, Karlsruhe University, Forum for cross border cooperation in Europe, Germany\)](#)

Property Tax and Informal Property: An Essay on the Challenge of Third World Cities

By Martim O. Smolka and Claudia M. De Cesare Lincoln Institute, USA

Exploring the potential role for the property tax addressing the often overlooked challenges posed by informality, this paper examines the following propositions: informality, for its nature, has not and should not have any bearings on the property tax; the presence of informality is a factor responding for lower property tax performance; and, property tax exemptions should be an ingredient in policies to mitigate informality. The study suggests otherwise that public officials in the fiscal area - out of ignorance or outright prejudices with respect to informality - deliberately neglect a substantive segment of potential taxpayers. In addition, it demonstrates that the presence of informality is actually associated to jurisdictions with better property tax performance. Possible explanations for the phenomenon are presented, including the fact that informality, in third world cities, is related to more dynamic local economies et pour cause to jurisdictions with a more comprehensive regulatory frameworks. Finally, the study examines how a more vigorous property tax, more specifically levied on land value, could be instrumental to pursuing more preventive, in contrast to the curative, public policy to break the vicious circle of informality.

Can the “unearned increment” in land values be harnessed to supply affordable housing?

By Rachelle Alterman, Center for Urban and Regional Studies, Israel

The idea of reaping the “unearned increment” or the “plus value” of land created by society is by no means new. It was famously proposed by Henry George in 1879, with the hope that a land-based “single tax” would be able to finance all the public needs of society without causing economic turbulence. If Henry George were living today, he would have likely added “affordable housing” as one of the items on his list of social services. The underlying rationale is that much of the value of real property is created not by the landowner’s initiative and work, but by government policies that grant development rights or by broad economic and social trends. This paper addresses the degree to which recapture of the “unearned increment” is a useful approach for financing affordable housing production. For evidence I shall draw on the policies and practices in several countries across the world – in the past and currently.

One hundred and thirty years after Henry George published his seminal book, the “vote” is clear: The idea of value capture in its pure form has failed to catch on widely among advanced economies, except in a few countries. The attempts to introduce an unearned increment tax in several major countries, notably in the UK were sporadic and did not last long. The only widespread land tax is the local property tax, but it is usually much more modest than Henry George’s ambitions and usually captures only a modest percentage of property values.

However, the basic idea that government can leverage the unearned increment as a financial source for public services has not died away. In recent decades, several “mutations” of this idea have been gaining popularity in many countries, but in widely different forms and degrees. These are much more complex and less “elegant” than the value-capture notion, and present many challenges, but they are the more realistic potential instruments for funding affordable housing.

The paper first explains the importance of distinguishing among the competing rationales for value capture. Each underlying rationale leads to a different set of policy instruments and may be less or more acceptable in legal and public terms. I then present a quick review of the limited experience among advanced economies with the pure mode of value capture policy and analyze its shortcomings. The paper proceeds to review the alternative rationale for value capture – internalization of negative externalities (the impact of new

development or redevelopment). This rationale too has several sub-forms that in recent years have given birth to a variety of regulatory practices in various countries. I will analyze each of these alternative instruments and their legal and policy advantages and disadvantages for delivering affordable housing in various contexts.

The conclusions will focus particularly on the particular Polish context as a post-socialist country with a fast developing economy and a planning regulatory system that is still in its infancy. To what extent can each of the legal and policy instruments adopted in other countries be successfully transported and embedded in the Polish context?

An increase in the value of land as a prerequisite of imposing adjacency levies – critical analysis

By Mirosław Gdesz, Administrative Court, Poland

The main aim of this paper is to discuss current regulation on assessing adjacency levies in Polish legal system, which is based on ad valorem formula. This paper tries to explain if this formula is a appropriate tool of private owners and developers participation in the cost of providing local public infrastructure.

The first part of the paper, provides the historical background and the evolution of adjacency levies. One can notably mark the linking up of levies with an increase in the value of land, which dates back to 1991. The second step in 1998 saw the introduction of adjacency levies, resulting from plot subdivision.

The next part paper tries to define a term “increase in the value of land” from the perspective of adjacency levies. An impossibility of using cadastral value of land as the particular situation of Polish land use system is indicated. The next problem to examine the problem of making a clear distinction between the adjacency levies and planning fees. One can notably ask the wider question, thus explaining if there is any linkage between the increased adjacency levies (resulting from the increased property value) and the prior construction of the public road. The paper will outline some key rulings, delivered by the Administrative Courts which tend to indicate that authorities, responsible for setting adjacency levies find it very difficult to take into consideration the above-mentioned factor.

Having in mind the above-mentioned analysis, one can ask if it is justified to continue calculating the amount of adjacency levies on the basis of the increasing property value. We shall consider if such mechanism suits us best to move forward with the property developer’s contribution system. It is worth considering if the “increase of the property value” should form the base for setting the amount of the payment. The author of this paper claims that other alternative options shall be examined. He proposes to adopt a new robust calculation method, taking into account other relevant factors such as: the length of the plot’s upfront stretch, the surface and the character of the built environment. The paper also tries to find out if allowing new calculation methods can help create a more flexible property developer’s participation system.

Land Value Tax as an Investment Mechanism for Public Transport Assets

By Francesca Medda, University College London, UK

Cities worldwide have been experiencing escalating growth, especially in developing countries, with often consequential negative impacts related to the increase of transport and in particular of car mobility. Investments in transport need to seek new paradigms to solve these problems. Urban mass transit systems are capable of providing capacity and competitive levels of service for a large proportion of urban travellers. These systems, more than other transport modes, exhibit public good characteristics. Therefore, their impacts of increased accessibility, i.e. the increase in land value, should be captured and returned to the society from which the investment has been sourced. From this perspective, this paper demonstrates the necessity to introduce land value tax mechanisms in investment programs for urban public transport. We review how different mechanisms of land value capture (betterment tax, tax increment finance and joint development mechanism) can be integrated in order to finance urban mass transit systems. We then examine a taxation methodology based on the concept that transport accessibility is a merit good. The tax in this case creates an incentive for households to locate in high accessibility urban areas, thus increasing their use of public transport services. The value capture taxation and the accessibility taxation, although different in their conceptual foundations, both aim to create a financial tool capable of sponsoring public transport.

More than a tax: some ethical implications of land value taxation

By Richard Lawrence Giles, Association for Good Government, Australia

After a broad description of land value taxation and claims made about its efficacy, in making housing more affordable, public infrastructure cheaper to construct, and recessions less severe, this paper summarises the fortunes of land value taxation in Australia and New Zealand since its introduction there at the turn of the 20th Century. It is argued that its relative decline since 1970 can be traced to the fact that investors see it as reducing their returns from property. This is especially true where, as in Australia and New Zealand, there is periodically quite pronounced property speculation.

Since there is this competition between private landowners and government for possession of land value the question follows as to whether land values are private or public property. Here it is argued that land rent or land values arise overwhelmingly from differential natural and social advantages to land, factors that cannot be ascribed to individuals. Land value taxation has thus an important underpinning in ethics. It is also suggested that equity is the foundation of good taxation.

Equity is also argued to be the foundation of social justice. Here, Henry George added a further ethical dimension to land value taxation when he argued that its full application (as a 'single tax') gave equal rights in the use of privatised land. Despite what may be said in favour of land value taxation as a fiscal reform, it is argued that, ultimately, the progress of land value taxation must involve not only fiscal but moral argument.

Taxing Public Leasehold Land in Transitional Economies

By Yu-Hung Hong, Lincoln Institute of Land Policy, USA

The paper examines three issues related to land taxation in transitional economies. First, in some transitional countries where land is publicly owned, taxing public land as if it is private property can create inconsistencies with the reemergence of private ownership in real estate. Two potential solutions are discussed: (1) recognizing leasehold rights as private property and (2) taxing land and buildings separately with the tax on the leasehold land labeled as a land use tax. Second, in taxing leasehold lands, lessees may be able to shift the tax burden to the government lessor, if the supply of land use rights is fixed. The government will receive new land tax collections but earn a lower lease income because of the decrease in leasehold charges caused by the capitalization of tax liabilities into land prices. Third, there are issues related to the use of mass appraisal techniques to value leasehold rights for tax purposes. Although complications involved in valuing large quantity of leasehold sites are not insurmountable, care must be taken to understand the relationships between lease term and leasehold value. If the rental-value based approach is employed to assess leasehold values, the distinction between fair market rent and contract rent should be made explicit.

Public space and its appropriation in the light of the theory of externalities – recommendations and directions for building an intervention system by public authorities.

By Tadeusz Markowski, Lodz University, Poland

Public space as a concept has various meanings. It is a research field for scholars specialised in urban planning, sociology, political sciences, economics and management. It is interpreted and described in their specific jargon by urban planners, architects and politicians. It has a common social meaning, too. Public space by definition constitutes a theme of interest of local societies and many external users.

Only a few do realize that a specific, public dimension of public space comes from a fact that it enables usage, consumption and access to other public goods, often much more important for economic development than its common perception as a selected and appropriately managed part of a city accessible for all. This complexity of public space and multidimensional specificity of its externalities makes it an object of a strong desire, appropriation and a source of conflict situations.

The goal of the article is to present an economic approach to the public space, to indicate specific features

resulted from a theory of public and private good linked with a theory of externalities and a *theory of imperfect* housing markets. Specificity of generated public goods related to special management will be shown as well as causes and results of uncontrolled appropriation of space. An attempt will be made to create a model of management of public space, taking into consideration regulations by public authorities.

The UNECE Working Party on Land Administration after Ten Years: Policy Guidelines for Sound Land Management.

By Ariel Ivanier, UNECE

The purpose of this paper is to present some of the findings and underlying principles of the recent publications of the Working Party as they relate to legislation on taxation, the sustainability of land administration systems and their potential impact on the budget of the public sector of Member States. As stated in the WPLA document *Social and Economic Benefits of Good Land Administration* “one of the essential features of maintaining national land records is to enable national governments to establish an efficient and equitable basis for raising taxes from those who own or occupy land and property. Such systems generate public income to provide essential public services for the benefit of the community” (*Social and Economic Benefits of Good Land Administration*, page 13). Maintaining up-to-date information on land use and the attributes of land for all individual land parcels contributes to a better assessment of the value of land, and creates also positive externalities in the management of agriculture and the environment. If land use and valuation information become integrated, the land administration system contributes to sound decision-making and, in consequence, to improved welfare for the populations concerned.

Housing sector reform in Central and Eastern Europe: regulatory framework and policy development

By Claudio Acioly, Chief Housing Policy Section of UN-HABITAT

The transition from a centrally-planned to a market economy experienced by countries from Central and Eastern Europe highlights one central theme: the retreat of the State from the actual production, delivery and allocation of housing. This is a common regional feature resulting into a large-scale transfer of ownership of the housing stock. The process varies from country to country and there are specificities. Nevertheless the experience shows that the transformation from rented to owner occupation often took place in the absence of preventive policies and proper arrangements as well as institutional and policy mechanisms to enable the maintenance of the housing stock to continue under a different regime rather than state owned enterprises. After more than a decade of transition, countries like Bulgaria, Belarus, Ukraine, Moldova, Lithuania and Armenia, just to mention a few, are confronted with enormous challenges to safeguard the quality, quantity, safety and livability of multifamily, multi-storey apartment blocks that form the basis of many neighbourhoods in major cities of these countries.

This paper and presentation looks at the current situation of the Housing Sector in some of these countries. It draws from experience of the author in assisting local and national governments in developing capacities and policy responses to deal with the new scenario emerged after large scale housing privatization. It explores the specific features regarding the institutional, legal, regulatory and policy environments and assesses to which extent progress has been achieved in establishing the basic conditions for housing sector performance under a market context. The paper and presentation depicts a first attempt to make a situation auditing and revisit government measures and initiatives geared to establish a sustainable form of housing maintenance and housing stock management that call upon homeowners' responsibilities for property tax and homeownership service fees geared to create a sustainable basis for housing stock maintenance and management.

The author makes an attempt to compare situations and countries where he has worked as development consultant. The paper reviews initiatives to design basic legislation right from scratch in order to adjust to a new regime of home ownership that implies new responsibilities to owners and to new emerging actors such as home owners' associations, condominiums, property management companies and local government agencies.

The paper and presentation highlights recent measures and discusses the challenges and potentials in both countries after analysing reforms and measures introduced to create an enabling regulatory framework and policy developments to cope with the adverse effects of privatisation and retreat of the state particularly in the areas of building maintenance and management of the housing stock. If nothing is done to reverse the ongoing deterioration of the building stock it is likely that the situation will become explosive with large numbers of properties running the risk to become derelict. Research sponsored by the Dutch government reveals that it will be necessary of more than €350 billion to bring the housing stock in the CEE region to a level of an acceptable liveability and energy efficiency with works to be implemented during 40 years.

Improving public-value capturing in urban development

By Demetrio Muñoz Gielen, Ph-D candidate Radboud University Nijmegen, the Netherlands

This paper focuses on the innovative public practices of capturing land value in urban development (i.e. public-value capturing). There are significant differences between England, Spain (region of Valencia) and the Netherlands. The English and especially the Spanish/Valencian public bodies manage to transfer the bill for paying and/or providing public infrastructure to Property developers. Public infrastructure refers to: public roads and space, sewerage, public facilities and buildings, affordable and social housing, etc. In addition, the public bodies manage to capture part of the value increase that accrues from rezoning land. This contributes to the public budget and helps to improve the quality and quantity of public infrastructure.

This paper will analyse two variables that are responsible for the bulk of the differences in public-value capturing. The first variable is flexibility in planning, i.e. the level of certainty about future development possibilities before negotiations between developers and local planning bodies take place. The second variable deals with an important aspect of property rights on land, i.e. whether public bodies are dependent on private parties to provide the infrastructure.

The data for the paper support on my research of English, Spanish (Valencian) and Dutch urban regeneration projects, further complemented with expert interviews and other indirect sources.

Improvement of land and property taxation in Montenegro as part of municipal land management and in relation to other countries in South-East Europe

By Yvonne Müller, GTZ, Montenegro

Alongside Kosovo, Montenegro is the youngest nation in the community of European peoples and one of Europe's smaller states with a population of some 620,000 living within an area of around 14,000 square kilometers. Foreign direct investments in land and real estate increased tenfold since 2004.

Since 2003, local self-governance units are in charge to levy and collect real estate tax. The first part of the paper presents policy, legal and administrative framework of real estate taxation in Montenegro and sets it in relation to real estate taxation in other countries in South-East Europe. Applying figures on development of local revenues during the past years as well as on development of land market and urban development in Montenegro, key problems and challenges for further improvement of this framework as well as its implementation are identified.

In the second part, a software tool for improving taxation of land and objects implemented in Montenegrin municipalities and lessons learnt during implementation are presented.

One major source for the paper is a guideline on "Improvement of local property tax administration in South-East Europe" published by the Network of Associations of Local Authorities of South-East Europe (NALAS) in March 2009. The findings of this paper are supplemented (and partly amended) by facts and experiences made during projects of German Technical Cooperation (GTZ) in Montenegro as well as in other countries of former Yugoslavia.

Innovations in Property Taxation System in India

By Dr. Debolina Kundu, and Dr. Debjani Ghosh, National Institute of Urban Affairs, India

Property Tax is an important local revenue source in many countries, but is often underutilized as a source for financing local expenditures, especially housing for the poor. In India, many local governments have initiated administrative and valuation reforms to improve collections from property taxes. In this paper, we examine reforms and their implications on the revenue base of the municipalities, taking case studies of two Indian cities, viz, Bangalore and Ahmedabad. The paper concludes that reform efforts which, make assessment of the property tax base more realistic (market-based), bring positive impacts on revenue generation in per capita terms. Although the present reform measures are a good step towards improving the performance of the property tax, structural issues such as improved valuation, increasing buoyancy of the tax and tax payer's confidence need to be addressed to make these reforms sustainable and replicable. The paper strongly recommends a change in the assessment system of taxation with an inbuilt system of automatic revision. Such a system would be sustainable once it is linked with simultaneous administrative reforms.

Taxation and its effects on sustainable development with reference to the UK

By Greg McGill, Planning and Development Consultant, England

This paper is about the effects taxation can have on sustainable development and how land is used. It focuses on the different effects taxing labour and capital can have, instead of taxing land, by explaining the adverse effects of the former taxes and how they encourage speculation in land and the withholding of land from productive use. Such actions are identified as discouraging urban regeneration and encouraging urban sprawl with a number of adverse consequences leading to less efficient, less effective and more damaging environments which is unsustainable.

As part of this process the paper appraises the effects this has on town planning in trying to overcome the adverse effects that are identified. The conclusion is that it does not succeed and that town planning actually helps to make things worse.

In contrast, if taxation is shifted towards land instead of labour and capital the effect is to create more efficient, more effective and more equitable environments. Importantly, it would encourage sustainable development, urban infrastructure development and service delivery. It would also help rather than hinder the aims and objectives of town planning.

Space Syntax as a Tool to Assess the Land Value

By Ahmed A. H. Saeid, Ph.D. Student WrocBaw University of Technology. Poland

This paper aims to relate the duality concept of urban economic models; monocentric and polycentric, with the urban morphology theory; space syntax. The basic of urban economic models depends on that index of accessibility within the urban spatial structure which plays significant key to determine the land prices. In this paper, the index of accessibility was analyzed by space syntax parameters to investigate the effect of spatial characteristics on the land prices in whole-parts concept of urban structure.

The findings showed, the whole urban structure of the city is monocentric concept which works as a micro-economic process. This global process determined by global spatial characteristic (mean depth) to value the land price. At the same time, the sub urban structures (parts) are polycentric concept which works as a socio-cultural process. This local process determined by local spatial characteristics (local integration and connectivity), to value the land prices.

The paper used hedonic regression model to analyze the correlations between the spatial characteristics of urban structure of Wroclaw City in Poland as a case study and land prices.

Land Value Capture: Case Studies, Policy Implementation, and GIS Land Value Mapping

By Alanna Hartzok, Co-Director, Earth Rights Institute

The beginning of this paper presents brief case studies of two cities in the state of Pennsylvania, USA that have shifted their property tax towards land value capture. These case studies give an overview of strategy,

results and potential next steps that can be useful to other municipalities around the world. This paper also describes steps and stages necessary to implement land value capture policy for municipal public finance including a 14-question initial survey. The components of a land value capture system are set forth along with a recommended sequencing. Details of best practices for land value assessment include factors contributing to land value such as physical attributes, legal and government forces, social, demographic and economic factors. Principles of valuation and procedures for data analysis and verification are described along with the use of GIS land value maps and computer estimated land valuation. The paper is illustrated with 20 photos, charts and diagrams and includes ten pertinent quotes. The conclusion states eight reasons why a community would benefit from a land value capture approach to public finance.

Land and property tax: financing towards equality in access to housing, serviced land and infrastructure in post-apartheid South Africa

By Kailash Bhana, Moegsien Hendricks & Anzabeth Tonkin

The policy and practice of property taxation and land value capture aimed at financing housing, serviced land and infrastructure to enable access for South Africa's urban poor, are under-developed and insufficiently mainstreamed. This paper asserts that the limited reach of land management policy and regulatory systems, and an unregulated land and property market contribute to growing inequality, poverty, marginalization, and spatial segregation. Land value tax and other land value capture mechanisms as a source of additional revenue for local municipalities are not optimized as an enabler to finance pro-poor development. The findings presented in this paper are based on the work done by the Development Action Group (DAG) over a two-year period as part of DAG's core Value Capture Programme work. Results presented were obtained through primary and secondary methods including, but not limited to, a literature review, grassroots participatory action research, interviews with government officials, academics, land and property experts, international case study analyses, records from the deeds office, and valuation rolls of selected municipalities. Follow-up engagements with selected municipalities post DAG's value capture and land management course, are also presented. DAG found that South Africa has a tax system that acts as a disincentive to the intensive use of land and that encourages land speculation and contributes to urban sprawl, resulting in unsustainable and inefficient functioning of our cities. The new Property Rates Act (2004) has effectively done away with pure site value taxation and composite rating. Considering the benefits of a site/land value tax, which even those in favor of flat rating have to accede to, the question beckons what the motivation was for the South African government to eliminate this option from new property tax legislation. Lessons learned from South Africa's local government finance and land and property tax reform experience are presented and pertain to themes including the need for political will and champions of innovative approaches; active participation of civil society; partnerships between government, the private sector, civil society; changes in both policy and practice, especially at local government level; and capacity development of politicians, officials and civil society role players. Future research efforts should be aimed at appropriate and contextually relevant land taxation and value capture mechanisms and lessons learnt from their implementation internationally.

The system of land use charges in the Federal Republic of Germany.

The lessons for the transition countries

By J. Kopietz-Unger, Karlsruhe University, Forum for cross border cooperation in Europe, Germany

Once an entry is made in the spatial development plan, the taxation of land plots is changed.

In Germany, the land tax is provided for under Article 106 sec. 6 of the Basic Law (GG) and the Real Estate Tax Act (GrStG).

Income derived from such taxes is passed exclusively to municipalities.

The interconnection between local planning or planning in which municipalities participate, and the tax and revenue authority is realized through the procedure of publicizing, so that the revenue office is provided with projects as part of the procedure of establishing regional, general and specific plans.

Municipalities charge two types of taxes:

Type A land tax on rural areas.

Type B land tax on construction areas.

There are two ways to estimate the tax rate, a different one for rural and forested areas and a different one for construction areas.

- taxation is made on the basis of the so-called uniform value for built-up and non-built-up areas. The uniform value is determined and fixed by the revenue authority.
- based on the value, municipalities collect the taxes that accrue to them, and the rates thereof are fixed by the municipalities according to the appropriate key; the land tax is a municipality tax.

Determination of the level of the tax and of the key is based on the municipality council's resolution. Receipts from such taxes, like all other receipts, must be recorded in the municipality budget, and so must the tax rates and amounts being the basis for such receipts.

Municipalities charge, at their own discretion:

- Fees for service infrastructure.

- Service infrastructure is necessary for the plot to be built up. It is a precondition for a site that is awaiting future development to become a construction area.
- Construction permit can be issued only when the plot is provided with service infrastructure.

A plot is considered to have the service infrastructure if it is provided with technical utilities (water and sewage system, electricity supply, access to telecommunication network) as well as road transport infrastructure.

Just as in case of fees for service infrastructure, municipalities collect fees for road development to build access roads. They serve mainly to have plot owners co-participate in renovation of severely damaged streets. Fees can also be charged for development or repair of a street or a part of a street.

Municipalities charge, at their own discretion:

- Redevelopment fees.

Redevelopment sites are designated by a municipality and historic site protection authority.

Once a formal redevelopment area is designated, the right to support is created for all facilities according to §7h EStG (German Income Tax Law).

Municipalities charge a compensatory payment in accordance with §154 of the Federal Building Code (Baugesetzbuch, BauGB) on everyone within the redevelopment area. The fees are collected upon completion of the redevelopment, also in social residential buildings. The argument provided in support of their collection is that the land value has increased for each plot as a result of redevelopment of the area.

On redevelopment and redevelopment areas.

A redevelopment area may cover the entire municipality, a district or a street. It may take two forms: specific or simplified redevelopment procedure.

- Procedure in case of specific redevelopment according to §§ 152ff BauGB is based on political concept of increase of land value index, which assumes that the municipality will have its expenses reimbursed in the form of redevelopment fees as a result of future increase of the value of land resulting from the

redevelopment, upon completion of the procedure. In this case no fees are charged for provision of service infrastructure. This form of redevelopment takes place in areas that require significant improvement of land infrastructure.

- According to §142 Abs. 4 BauGB, simplified redevelopment procedure may only take place if no specific legal provisions for redevelopment stipulated in §§ 152 bis 156 BauGB apply, i.e. when no or just a minimum increase of land value index can be anticipated. In this case, residents of a given street may be charged with fees for provision of infrastructure according to municipal tax law (KAG) in case a new street is built or the value of re-constructed street is significantly increased.
-