



Impact of Land Use Charge on Property Letting Transaction in Lagos State

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ABSTRACT

The Land Use Charge Law (LUCL) of Lagos state is a form of public intervention in urban land market to generate the needed revenue for government expenditures, and for wealth redistribution. As a property tax, it was meant to correct the perceived distortion in Lagos land market – a situation whereby less than one percent of the population controls more than ninety percent of its land value. Although, the tax policy is laudable, the society is not always aware of the impacts such policies have on real estate market, yet they are not without implications either positive or negative. This paper therefore examined the perspectives of landlords and the Estate Surveyors and Valuers in Lagos, Nigeria on the impact of Land Use Charge (LUC) on volume of property lettings, rent and other letting fees in the study area. Structured questionnaire was randomly administered on 135 Estate surveyors and Valuers and purposively on 135 landlords. The data collected were analyzed using descriptive statistics. Findings reveal that the LUC had no effect on volume of property letting, and larger percent of the Valuers (70.8%) and landlords (88.8%) affirmed that rent has increased in Lagos due to LUC. The paper concludes that though LUC has had no noticeable impact on volume of letting transactions probably due to limited land size and high population of Lagos, it has however led to increase rent and other letting fees in the state with its attendant consequences on urban renters

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Introduction

Urban real estate, unlike any other investment media has witnessed many government interventions in form of land policies. While some policies could limit property right to income, some others could erode ownership right on landed property. However, urban real estate policies usually evolved as a result of a number of influences which are incorporated into real estate law, and principle of land use and development. Although, factors influencing urban real estate policy vary according to the social background of an area, they are mostly of economic needs, political, religious beliefs, cultural, customs and tradition, environmental consideration, public aim and objectives [1, 2].

The Land Use Charge Law (LUCL) of Lagos state, Nigeria is an urban tax policy on real estate within the metropolitan Lagos. It a public intervention in urban land market of Lagos for wealth redistribution and revenue generation for the provision of infrastructural facilities. Since real estate market is insufficient on its own to produce an efficient land use allocation and adequate wealth distribution because land ownership is not evenly distributed among members of any community [3] government intervention is inevitable. For instance in Lagos, it was reported that the value of landed property in the state was about ₦3.4 trillion while some 150,000 individuals or companies (i.e. less than 1% of the population) were holding over 90% of this land value [4]. This perceived distortion coupled with dwindling federal subventions and the indispensability of finance for sustainable governance necessitated the consolidation of the

existing land charges into a comprehensive property charge commonly referred to as Land Use Charge (LUC) [4].

However, according to [5], the outcome of urban real estate policies either positive or negative are not usually glaring and the society is not always aware of the impacts that those policies are engendering. [5] also noted that governments are vast in policy formulation and execution but are lacking in those policies devised on sound economic basis or that which address obvious market failures. Similarly, sub-Saharan urban land policies are found to be politically motivated [6, 7] whereas economic implications of those policies are enormous on both the government and individual market participants [6].

This paper thus, examined the impact of LUC on property letting transactions in Lagos state. This is because the law has been described as “a very bad law in its entirety; and cannot be sanitized by cosmetic amendment [8] citing editorial report of The Estate Surveyors and Valuers 2002. Also, transaction in real estate either outright sale or letting purpose is often get complicated due to the complexity of the property itself, government regulation and transaction costs involved. In Nigeria, real estate transaction costs are many and could be very expensive and discouraging. For instance, [9] revealed that the cost of acquisition of landed property in Lagos include: the actual property price plus agency fee (10%), legal fee (10%), governor consent (15%), stamp duty (3%), capital gain tax (10%) registration of title (1%) and legal fee for processing of Certificate of Occupancy (10%). These other fees, aside actual property price are potential

bottlenecks to the progress of real estate market. However, this study examined the effect of LUC on property letting in Lagos and its associated impact on variables like volume of property lettings, rent, agency fee, management fee and service charge from the perspectives of Estate surveyors and Valuers, and the landlords which they represent as agents in the study area. The paper therefore provides answer to the following questions: Does LUC has effect on the volume (number) of property lettings in the study area? Do landlords request additional amount to pay LUC? If they do, at what time do they make such request? And lastly, has the LUC led to increase in rent and other letting fees in the study area.

Literature review

Several studies have attempted to determine the effects of property tax on rental and capital values of real estate. Other studies examined economic and statutory impacts of property tax. Such studies are [10], [11], [12], [13], [15], [16], [17], [18] and [19] amongst others. Research on impact of taxes on real estate is very scarce in Nigeria and the above mentioned studies are foreign except [17] which only assessed the impact of tax administration on government revenue in Nigeria and has nothing to do with real estate. The reason for this is lack of data bank for every transaction in real estate and the secretive dealings in real estate market in the developing nation like Nigeria. This is an indication that the market is still maturing. However, in the developed economies, data on real estate transactions could be readily available because of their efficient and matured real estate markets. Thus, in the United States, [10] used two-stage least squares estimation techniques to determining the effects of local property taxes on local expenditure programs on property value. Findings suggest that, an increase in property taxes unaccompanied by an increase in the output of local public services will result in reduced property values. It was also noted that an increase in community tax rates and employment of the receipts to improve its school system roughly offset the depressive effect of the higher tax rates on local property value.

[19] is also an empirical study in the United States that investigated the impact of residential property taxes on residential rents. The study found a one standard deviation increase in property tax rate raised residential rents by roughly \$400 annually. This is an indication that rents on residential properties are very sensitive to tax increment. Similarly, [18] estimated the impact of changes in stamp duty on house prices and housing turnover. The result showed that stamp duty has statistically significant outcomes on both the house prices and housing turnover. Also, [16] empirically assessed the impact of local taxation on property prices in two French cities: Dijon and Besancon using data on property taxation and real estate transaction over the period of 1994-2004. The result revealed that the amount of taxes paid seemed to have negative effect on property price, though the local property tax rate had no impact on property prices. In addition, [12] discussed the effects of property taxes and development cost charges on urban development in Toronto and Ottawa. In the study, the developers interviewed were of the opinion that property taxes had very little impact on project densities and would not see the taxes as increasing the cost of capital improvement on land. The developers however claimed the high taxes resulted in early demolition of low-yield buildings but do not affect replacement rates. Again, [20] provide evidence of distortionary effects of property transaction taxes (stamp duty) in the UK.

The study employed administrative data on all property transactions from 2004 to 2012. The outcome of the study showed that transaction taxes strongly affect the price, volume and timing of property transactions on the one part and a temporary cut of a 1% transaction tax increased housing market activity by 20% in the short run. It was also noted that after the re-introduction of the 1% tax, the market activities shrink by less than that of the initial stimulus. Furthermore, earlier study [21] revealed that Pittsburgh's changes in property tax rates played a major role in stimulating the building boom experienced between the period of 1960-1979 and 1980-1989. Meanwhile, the Nigerian studies related to the Land Use Charge Law of Lagos state are: [9], [22], [23], [24], and [25]. None of these studies examined the effect of LUCL on property transactions. Although, [9] discussed the probable effects of LUC on property market, mortgage, local government and housing, the study was not empirical and neither does it examine impact on rent and other letting fees.

Research Methodology

The study examines the perceptions of Estate Surveyors and Valuers, and property owners in Lagos state on impact of LUCL on property letting transactions. Perceptions of the two responding groups rather than empirical data were sought because real estate market in Nigeria is still evolving and transaction data on real estate are very scarce or difficult to obtain. [25] also used perceptual analysis for the purpose of evaluating the LUCL. These authors similarly noted that Lagos State Government has kept virtually all information on the operation and performance of LUC Law from public view. Thus, questionnaires were randomly administered on 135 estate surveying and valuation firms in Lagos and a landlord from the management record of each of the firms was purposively selected. Descriptive statistics was used in addition to frequency and percentage distribution to analyze the data gathered. Likert scale of strongly agree, agree, neutral, disagree and strongly disagree were assigned weight values of 5, 4, 3, 2, and 1 respectively to arrive at the mean of each variable. Out of the 135 questionnaires administered on the firms of Estate Surveyors and Valuers, 106 were returned. This represents 78.5% response rate. The landlords on the other hand returned 64 questionnaires out of 135 administered on them. The low response of the landlord might have to do with the timing of questionnaire administration and government threat on property owners (LUCL 2001, Sections 10, 11, 17, 18 & 19 which spell out penalties for non-compliance) [25].

Results and findings

The study started by examining the age of the respondents as well as the years of experience of the valuers and years of ownership on the part of property owners. This is to ascertain that the responding landlords, and valuers were not minors and they have had experience with the Land Use Charge and therefore qualify to give useful information. About fifty-five percent (54.71%) of the valuers and 87.5% of the landlords were above the age of 36 years. This is an indication that most of the respondents were of age as at the time the law was enacted and could as well give reliable information. In addition, majority of the valuers had work experience of between 11 to 15 years while most of the landlords had owned their property between 16 to 20 years. Thus, information given by these respondents can be adjudged reliable.

Perceptions on Land Use Charge impact on volume of lettings

Whenever landed property changes hands a lot of cost implication is involved which could stifle real estate market. Effect of LUC on the volume of property lettings is therefore determined in this section.

In Table 1 below, the mean value of 3.9 and 3.4 from the perspectives of valuers and landlords respectively indicate that the LUC had no impact on volume of property letting in the study area. Notwithstanding, a sizeable number with mean value of 3.1 and 3.3 of the valuers and the landlords respectively agreed that LUC had small negative effect (i.e. decreasing property letting by 1-10%) on volume of property letting.

The inference drawn from both perspectives is that the impact of LUC on the volume of letting transactions was not noticeable though could be negative but negligibly small. The small negative effect of LUC on volume of letting could be that some tenants cannot afford additional amount to cater for LUC (see Table 2 and 3) which consequently might lead to delay in getting tenants. Although, based on individual respondent's experience in practice, some other perspectives exist as seen in the table, yet the popular opinion is that LUC had no effect on volume of property letting. The reason for "no effect" can be adduced to the increasing population of Lagos State, and high demand for accommodation. Similar situation was noted in [12] where property taxes were found to have very little impact on project densities in Toronto and Ottawa.

Table 1. Perceptions of impact of LUCL on the Volume of Letting Transactions.

Effect of LUC	Valuers		Landlords	
	Mean	Ranking	Mean	Ranking
No effect	3.9	1 st	3.4	1 st
Small positive effect (increasing property letting by 1-10%)	2.3	4 th	2.6	3 rd
Large positive effect (increasing property letting by 11-25%)	2.2	5 th	2.3	5 th
Larger positive effect (increasing property letting by 26-50%)	2.1	7 th	2.0	7 th
Considerable positive effect (increasing property letting by 51-75%)	2.1	7 th	1.8	8 th
Small negative effect (decreasing property letting by 1-10%)	3.1	2 nd	3.3	2 nd
Large negative effect (decreasing property letting by 11-25%)	2.5	3 rd	2.4	4 th
Larger negative effect (decreasing property letting by 26-50%)	2.2	5 th	2.3	5 th
Considerable negative effect (decreasing property letting by 51-75%)	1.6	9 th	1.8	8 th

Source: Author's Analysis

Request for Additional Money from Tenants

In an attempt to further investigate the effect of LUC on letting transaction two questions were asked. One, do landlords specify that tenants should pay an additional amount to cover LUC and, if they do, at what stage do they required such additional payment. This is because any additional payment can affect letting transactions.

Documented in Table 2 and 3 below are the responses of both the valuers and the landlords.

Table 2. Landlords Request for Additional amount to cover LUC.

Does landlords request for additional amount for LUC?	Valuers		Landlords	
	Freq	%	Freq	%
Yes	62	58.49	-	-
No	19	17.92	13	20.31
No response	25	23.58	51	79.69
Total	106	100.00	64	100.00

Source: Authors' Analysis

It is shown in Table 2 that 58.5% of the estate valuers affirmed that landlords requested tenants to pay additional amount to cover LUC while 17.9% of them disagreed. Also, some 23.6% did not respond. However, the respond of the landlords was not impressive. In the same Table 2 majority of the landlords 79.7% did not respond while 20.3% disagreed that landlords specified that tenants should pay an additional amount to cover LUC. This shows that the landlords were hiding under "no response" an indication that they do demand for extra amount for the payment of LUC. The reason for this is not far-fetched. The LUC Law stipulates that owners of property are liable to the property tax (LUCL, Section 4 [26]). Moreover, another question was asked to ascertain the exact time landlords make request for additional payment.

Table 3. Time of Requisition for Additional amount to cover LUC.

At what time?	Valuers		Landlords	
	Frequency	%	Frequency	%
During negotiation for lease	30	28.3	25	39.06
When demand notice come	9	8.49	2	3.13
During rent review	46	43.40	23	35.94
No Response	21	19.81	14	21.89
Total	106	100.00	64	100

Source: Authors' Analysis

Analysis in Table 3 from the valuers view revealed that most landlords requested for additional amount to cover LUC from tenants during rent review and negotiation for lease. For instance, 43.4% were of the opinion that landlords made request for additional amount during rent review and another 28.3% believed that it happened during negotiation for lease. Only few (8.5%) agreed that landlords demanded for additional amount when demand notice come.

It is disturbing to note, that landlords who did not respond to the question on whether they demanded for additional amount to cover LUC, later responded to what stage did they make such request. While 39.1% of 64 landlords agreed that additional amount was requested to cover LUC during negotiation for lease, another 35.9% agreed that additional amount was requested during rent review. Only 3.1% indicated that such demand were made when demand notice for LUC were administered on them. It is deducible that landlords do make request for additional amount to cover LUC mostly during rent review or negotiation for new lease.

Perceptions on Impact of LUC on Rent and Letting fees

The views of valuers and landlords on impact of LUC on rent and other letting fees are expressed in Table 4. The question was asked to know the view of the respondents on

whether LUC has led to increased rent and other letting fees since 2001.

Table 4. Effect LUC on Rent and other letting fees.

LUC has led to increase in rent and other letting fees	Valuers' Perception							Me an	Ran king
	Agreed (5&4)		Undecided (3)		Disagreed (2&1)				
	Fr eq	%	Fr eq	%	Fr eq	%			
Rent	75	70.76	10	9.43	21	19.81	3.9	1 st	
Service charge	29	27.36	36	33.96	41	38.68	2.9	2 nd	
Management fee	22	20.76	33	31.13	51	48.11	2.7	4 th	
Agency fee	25	23.59	35	33.01	46	43.40	2.8	3 rd	
LUC has led to increase in rent and other letting Fees	Landlords' Perception							Mean	Ran king
	Agreed (5&4)		Undecided (3)		Disagreed (2&1)				
	Fr eq	%	Fr eq	%	Fr eq	%			
Rent	44	88.75	18	28.13	2	3.13	4.1	1 st	
Service charge	28	43.75	29	45.31	7	10.9	3.5	3 rd	
Managemen t fee	28	43.75	28	43.75	8	12.5	3.5	3 rd	
Agency fee	32	50	27	42.19	5	7.81	3.6	2 nd	

Note: Strongly agree is rated as 5, Agree is 4, Undecided is 3, Disagree is 2 and strongly disagree is 1.

In table 4 above, majority of the Valuers (70.8%) agreed that LUC has led to rent increase in the study area. The mean value of 3.9 also lends credence to this fact. Also, another 27.36%, 23.59% and 20.76% of the Valuers were of the opinion that service charge, agency fee and management fee had increased respectively as a result of LUC. The implication is that the property tax has been shifted on tenants in form of rent increase and rent increment has a direct relationship with other letting fees in property market.

In addition, the landlords view of LUC impact on rent and letting fees concurred. With the mean value of 4.1 being 88.8% of the landlords' opinion, rent has increased in the studied area as a result of the introduction of LUC. The mean values of 3.6, 3.5 and 3.5 show that agency, service charge and management fee had also increased. It could be inferred from the table that LUC has led to rent increase in the study area. This is because landlords were demanding additional amount to cover LUC (see table 2 & 3). This they smartly achieved by embedding LUC into rent during negotiation for lease or during rent review. This finding corroborate the earlier assertion of [19] that says rent on residential properties are very sensitive to tax increment, and also in agreement with [16] that showed that the amount of taxes paid have effect on property prices.

Meanwhile, the Estate Surveyors and Valuers had expressed their displeasure over LUCL and called for its abrogation. As documented in [8] the Valuers observed that the law seeks to consolidate taxes with differing bases and principles. They noticed that the tax is not equitable while the enumeration and assessment were carried out by non-professional valuers. In addition, the tax was found to be too high, representing 30% of annual rental value of property. Nevertheless, the rate has been reduced in response to criticisms.

Conclusion

Urban real estate policies are not without implications either positive or negative, and the implications are not usually glaring to the generality of the public. This paper has

established the effects of LUC on volume of letting transactions, rent and other letting fees in Lagos state. This paper revealed that LUC has had no noticeable impact on the volume of property letting in Lagos state and the reason for which might not be unconnected with high and rising population in the state which has also resulted in high demand for accommodations. However, the LUC has led to increase in rent and other letting fees like agency fee, management fee and service charge in the study area. This was achieved by inclusion of LUC into rent either during rent review or negotiation for lease or sometimes embedded in service charge while agency and management fees have direct relationship with rent.

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