

An Empirical Study on Impacts Caused by Excessive Profits Tax on Land of Korea and Counterproposal

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1. Introduction

1) Purpose of this study

It is not necessarily to succeed land supply for urban housing, even though it is time to transit for Korean to an advanced society through successive economic growth. Now, a weakpoint in Korean land policy is discord due to economic growth, which it never be rectified by the existing tax system related to land and housing supply methods. Then, the Korean government has introduced recent land policy reform measures in order to stabilize circulating system of land market, without a parent law involving effective land use planning.

This paper aims to study empirically impact of excessive profits tax on land, the third part of the recent land policy reform measures, and to offer an alternative measure in order to promote urban land supply. Specifically, firstly, we investigate the consensus on effects of the law. Secondly, we investigate how to affect urban land supply for housing, by evaluating the effects and the problems caused by excessive profits tax on land. Thirdly, we propose an alternative measure on reestablishment of excessive profits tax on land, in order to make a counterproposal on the urban land supply suitable to social needs.

2) Method of this study

The impacts caused by recent land policy reform measures ought to result in land use mechanism, even if the measures aim to recover the order of land markets. It is just why this paper should investigate the changes in people's perception, because changes caused by the law begin to show up not yet in city planning, but in people's perception now. Especially, this paper investigates to evaluate the acts or the effects of excessive profits tax on lands: People agree the aims of the law, then, do they recognize the acts or effects of the law, too? What happen with the land market mechanism or the land use mechanism, and what is the matter if it is so?

In this paper, we are to suppose the effects and the problems of excessive profits tax on lands according to reviews and interviews with professionals, and to investigate general consumers' perception according to questionnaires. However, it was too early to investigate general perception at that time. Moreover, they are hardly to understand contents of the law. Then, we are to investigate to well-informed people of Korea who they can understand the law. In addition to this, we do investigation on people involved in real estate market. Finally, we are supposed to confirm impacts to administration and local government, and to offer the counterproposal to reestablish land supply method for urban housing (Table. 1).

Table 1. Questionnaires in this study

	Questionnaire to the well-informed people	Questionnaire to the real estate agents	Questionnaire to the administrative staff
Period of questionnaire	17th.-29th. Feb. 1992	1st-14th. Feb. 1993	6th.-11th. Dec. 1993
Method of questionnaire	A poste restante	A poste restante	A poste restante
Subject of questionnaire	Professors of department related to land, Researchers, Postgraduate students of department related to land	Real estate agents, Developers, Consultants, Landlords, The staff of corporation	The Ward office, The city office, The administration office, Ministry of construction, The taxation office, The tax administration agency
Rates of collection	51% (190/370)	75% (300/400)	68% (189/280)

2. Why was the excessive profits tax on lands established?

1) Background of the law

Korea has experienced rapid industrialization and urbanization during the past three decades. It has not been enough to supply urban land for housing, then, the origin of land problems in Korea may be attributed to discord with supply and demand. We can summarize the background of establishment by the law as follows.

Firstly, discord with land supply and demand is prevailing, because of being small in area and lack of capacity in land supply.

Secondly, soared land price hinders regional development involving the equipment of urban infrastructure and firms operation. Because soared land prices may lead to higher production costs for firms, and a greater fiscal burden in investing infrastructure.

Thirdly, land prices have increased rapidly compared to other economic indicators. Moreover, capital gains from lands are not fully recaptured, and induced land speculation.

Fourthly, the rate of land ownership in general is conspicuously low and the skewed ownership used to hamper social stabilization, especially, in the late 1980s, many low income families could no longer bear soaring rents. That is why the Korean government has to rectify the social distortion politically, namely, in order to

enlarge the middle class.

2) Purpose of the law

The excessive profits tax on lands intends to recapture windfall gains on an accrual basis. It is more of an anti-speculation measure as it taxes only idle land or excessive land holdings. Ultimately, the law aims to encourage efficient use of idle land and stabilization of land price, by recapturing capital gains from land.

3) Contents of the law

Contents of the excessive profits tax on lands can be summarized as follows.

Firstly, it taxes on idle lands only. Specifically speaking, it subjects to idle lands being possessed for capital gain, except for public use laid down by presidential decree. And basic decision on idle lands for non-profit making firms is laid down by presidential decree.

Secondly, the tax duty is obliged to real land owner.

Thirdly, tax period is made it a rule to 3 years (1st. Jan. 1990~31st. Dec. 1992). Exceptionally, however, in regions where apprehensive soaring land price is, or in regions where their land price rates are 1.5 times higher per 1 year, assessment is done ever year.

Fourthly, 50% of capital gains after completion of tax period are charged every 3 years.

Fifthly, assessment method is as follows.

Land price after completion of tax period—{Land price after beginning of tax period*(1+Rate of normal land price increase during tax period) +Improvement cost+Capital expenditure sum}

Sixthly, the excessive profits tax on lands is to apply differentially as a transfer periods, which aims to induce transfer.

3. Impacts caused by the excessive profits tax on lands

1) Realities and effects of the law

First of all, the Korean government has investigated 610 thousands parcels being recognized as idle lands, about 250~300 thousands parcels among them are assessed. And people can ask for reinvestigation if they are not satisfied it. The government has assessed 31 thousands parcels in 1991, which land prices had increased more than 30.87% as compared with past year. For the first time, the government has carried out a regular assessment of the excessive profits tax on nationwide idlelands for three years(Table 2).

Table 2. The actual results of assessment

Classification	'91 (Expected taxation)	'92 (Expected taxation)	'93(Final taxation)
Nationwide increase rate of land price	20.58%	12.78%	34.26%
Tax subject	in regions where their price rates are higher than 30.87%	in regions where their price rates are higher than 19.17%	in regions where their price rates are higher than 44.53%
The number of tax cases	31,722	5,475	
Tax areas	1,730,000 Pil	540,000 Pil	
The average amount of tax	463 billion Won	34 Billion Won	947 billion Won
The number of tax payers	23,381 persons	4,103 persons	94,147 persons

Origin ; the taxation office

The law contributes to stabilize land price and to suppress speculation, though it is severely defied by taxpayers. Expecially, it encourages supply and use of idle lands, suppression of the whole demands of lands. Moreover, we can also anticipate the effects in land use mechanism when we achieve suppression of land price, and also the financial effects in local government.

2) Weakpoints of the law

We have investigated that the excessive profits tax on lands involves many weakpoints through reviews and inter-

views with professionals, which it apprehends to hinder the land supply for urban housing in some cases.

Firstly, the law involves unconstitutionality because it burdens us with taxes not in transaction step but in possessing step of real estates. Also, we can't remove unconstitutionality of unrealized capital gains tax thoroughly, with partial revision of contents.

Secondly, definition of idle lands is ambiguous. It doesn't reflect reality fully in standards and extends of judgement. As a result, ambiguous definition induces undesirable land use in order to avoid the law.

Thirdly, it can't be recaptured if they are not idle lands, even though there are huge capital gains generated by change of land quality and form. In addition, definition of profit and non-profit idle lands is artificial and arbitrary.

Fourthly, the excessive profits tax on lands is assessed on public declaration system of land price which based on assessment standards of 300 thousands parcels. However, it is assessed by public officials related to land in regions, except on the assessment standards, so, it is quite within the realms of possibility discretions intervene on assessment of capital gains.

Fifthly, the law is never stable financial resources for urban land supply. It is because it is not assessed while land price is stable. Moreover, the government has not laid down a provision on refund, though we can suppose restoration when the land price decreases.

Sixthly, it is not appropriate to assess the capital gains tax based on single increase rate of land price(nationwide increase rate of land price), because land price of same region is different in a site.

Seventhly, the excessive profits tax on lands apprehends to hinder firms management, namely, that would double taxation in the case of firms, whenever firms possess only one parcel.

3) Evaluation of the law and points to be revised by questionnaires

In order to investigate people's perception on what is happening, questionnaire is distributed to well-informed people and people engaging in market. We have found that more than 80% of the people insist on revision to increase efficiencies of the law, although they recognize the purpose of the law(Fig. 1).

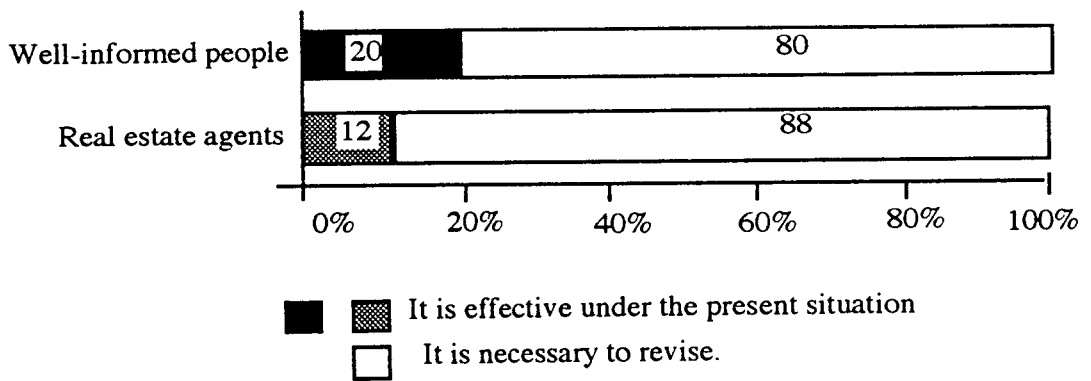


Fig.1 Evaluation of the effects on excessive profits tax on lands

Then, what does the law influence on the land supply for urban housing? How should the law be devised to form consensus on the effects of the law? We are supposed to confirm serious weakpoints by reviews and interviews. Findings are as follows. It is proposed to prescribe idle lands more definitely, because it is quite within the realms of possibility of undesirable land

use, in order not to apply the law(Table 3). And, they insist the counterplan how to encourage effective land use. Then, the effects on land use are in accord with each other in perception. However, people involved in land market recognize constitutionality and secondary effects on firms activity more seriously than well-informed people.

Table 3 Perceptions on weakpoints of excessive profits tax on lands

	Weakpoints of the law	Well-informed people	Real estate agents
Excessive profits tax on lands	Definition of idle lands	65	41
	Undesirable land use	53	40
	Unconstitutionality	14	31

Findings are got by plural selection(unit; %).

Compositely speaking, it is necessary to prescribe the tax subject and assessment method of the excessive profits tax on lands, to devise a proper measure in order to encourage efficient land use. Especially, we have to know that vacant lands are developing and constructing in order to avoid the law, they hinder the land supply for urban housing longtimely. Unconstitutionality can't be removed thoroughly by partial revision. Moreover, it may be operated only the law of time limit, because the law was established on the assumption of rising land price. Accordingly, it is hardly to anticipate the good effects on land supply for urban housing under the present situation.

4. A socio-economic impacts on urban land supply for housing caused by the excessive profits tax on lands

Recent land policy reform measures aim to rectify skewed ownership, to recapture capital gains from lands, to suppress speculation, which they mean to change land market mechanism ultimately. In general, land market mechanism correlates to land use mechanism, which influences upon supply and demand of land. For this reason, we are supposed to investigate socio-economic impacts involving secondary impacts, and to analyze how to connect the impacts to land supply policy for urban housing.

1) Unintended secondary impacts

We can't build up the land supply policy without consensus on the effects of the law, because the laws are established on

the political background, namely, enlargement of middle class. Unintended secondary impacts shown now are summarized as follows.

Firstly, government is gone to law against the taxpayers, because of unrealized capital gains tax and non-objective public declaration system of land price.

Secondly, the law will waste immensely administrative cost, because the excessive profits tax on lands is established on the assumption of rising land price and now it happens to actualize restoration of levy taxes.

Thirdly, it intimidates the balance with macro economics policy, for it doesn't connect with macro economics policy and balanced regional development policy. Especially, lack of construction materials and labours owing to construction market abnormally overheated has influenced upon nationwide economics.

Fourthly, it doesn't influence upon increase of land supply for urban housing but construction behavior, even though the law aims to increase supply of the idle lands. Moreover, the idle lands are developed for commercial use, not for housing use.

Now, negative effects on land use are conspicuous, because it doesn't leave much to be developed big units of land for decrease of idle lands.

2) Impacts on real estate market

Recently, land price has been declining all over the country, and supply for housing land has been increasing. Many professionals and people involved in market take a stand it results of deflation, and people don't recognize the effects of ownership increase, because housing price is

still too high to acquire(Reference 1, 2, 3). Therefore, we can't assert the existing trend in real estate market to the results

of the law, we ought to observe the trend from now on. Fig.2 is describing fluctuation of countrywide land price.

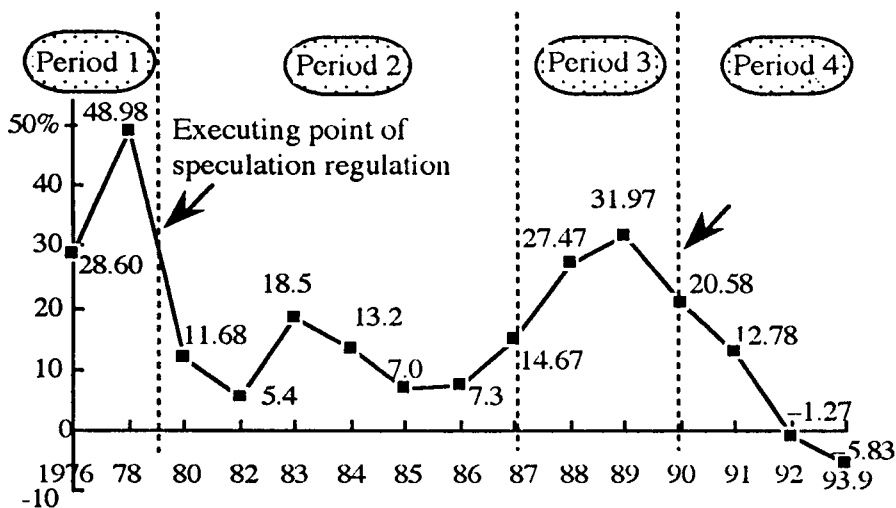


Fig.2 A recent tendency in real estate market
(The source ; Ministry of construction)

It is profitable for citizens to acquire their housing owing to recent housing in stock. However, decrease of housing demand owing to deflation results in decrease of housing supply ability caused by bankruptcy of housing developers.

Accordingly, it may be wondered that government can meet the critical situation with only public side supply method, when housing demand increases rapidly for future. In that case, it is quite within the realms of possibility that they face to crisis more serious than past. There, we need the policy to induce not only decreasing land price but also establishing circulation orders of real estate market, in order to connect the recent housing in stock to acquire ownership.

3) Impacts on administration-finance

The excessive profits tax on lands has big administrative effects. Levy taxes are determined to include in land manage-

ment and regional balanced development special accounts, to use to develop the undeveloped regions(Reference 1, 2, 3). However, it is not determined to use for urban land supply only. Moreover, effects on tax revenue are big, but revenue neutral stance as like exemption of income tax is not set up yet.

Accordingly, it needs a policy making on managing the law under the new government and cooperation system being usable policy making through public information on land policy reform measures and establishment of complete data base. Moreover, the present administrative effects caused by land policy reform measures are encouraging operation of the public side land supply for urban housing.

4) Effects of monetary regulation

The Korean government has declared May 8th Measure. It is popularly believed that large corporations are engaged in, or

worse yet, initiate property speculations using their network of information and easy access to bank loans. In an economy with a perpetual credit shortage, access to large bank loans and loan guarantees is considered a privilege given only to productive investments, and the bank credit regulatory ordinance tried to prevent diversion of fund into property speculation. Banks, however, have not effectively enforced this regulation, as their primary concern is credit stability, not whether the money is used for property speculation or not. Large conglomerates have thus acquired land at will.

In response to mounting mistrust, the government announced on May 8th, 1990 that 49 large conglomerates could not acquire new properties and must sell those with no business purpose, and that the National Tax Bureau would examine property holdings to ensure compliance. Some contents of the decree were on dubious legal grounds, but others simply confirmed existing laws and ordinances. Among the controversies surrounding the decree, the most important one is the dispute on which land is for business purposes and which is not. Considering that statutory codes had long been established on that

issue, it was surprising for such a dispute to arise at all. This revealed that complicated rules on classifying speculative land were beyond day to day administrative capacity.

Monetary regulation has influenced upon increase of land supply, stabilization of urban housing longtimely. However, it is quite within the realms of possibility that it hinders land supply for urban housing. Accordingly, it is necessary to select the subjects of monetary regulation in order not to be reflected negative effects on land supply for urban housing. And we need to devise the diverse financial goods being affordable to the urban middle class, to make exceptions in various kinds of systems for supporting the middle class.

5) Effects on regional development

From the findings of questionnaires about the effects on regional development, well-informed people don't anticipate the effects of regional development, because it doesn't aim to encourage regional development. However, people engaging in market are anticipating the effects of regional development for future even though it is not shown positive effects now (Table 4).

Table 4. Perceptions on the effects of regional development

	Forecast the effects of the law	well-informed people	Real estate agents
Regional development	It is ineffective in regional development.	45	16
	It is effective in construction of infrastructure.	40	21
	It will be effective longtermly.	—	53

Findings are got by plural selection (unit : %).

In view of the results so far achieved, we can anticipate the effects on efficient land use with change of social situation, especially, on encouraging the public side land supply for urban housing by tax increase. Recent land policy reform measures are focused on prevention of influx of funds for disguised demand in land market, so, doesn't considerate fully the publicity of land use based on the law.

6) Effects on people's perception

Consensus on publicity for lands is making, even though we don't put completely confidence in land policy. We are looking forward to the effects of the law under the condition of becoming fixed in people's perception. People don't apprehend come back of speculation, even though it becomes prosperous again. Especially, people

recognize that it is not desirable to possess the real estate as they did in the past, instead they should develop or use the real estate. This is progressive in people's perception on real estate. However, we have

experienced some secondary effects because of substantial limitation of the law. They are insisting revision of the law and planning method, in order to minimize the existing problems (Table 5).

Table 5. Perceptions on countermeasures for the problems by the law

	Countermeasures for the problems	well-informed people	Real estate agents
The existing problems	Reinforcement of the laws	40	17
	Revision of the laws	33	45
	The change of planning method	32	39
	It is no problem in particular	22	18

Findings are got by plural selection (unit : %).

5. Counterproposal on reestablishment of the excessive profits tax on lands

In view of the results so far achieved, it is impossible to anticipate positive effects on land supply, and on efficient land use by the law. However, it is shown improvement direction in order to promote the land supply for urban housing, by analyzing positive effects and negative effects by the law.

On the other hand, the Korean government begins to recognize the negative effects of the law recently. Then, what does enforcement ordinance revised by government influence upon the land supply policy hereafter? We are supposed to confirm the impacts to administration and local government, and to offer the counterproposal to reestablish the land supply for urban housing.

1) Revision of the excessive profits tax on lands by government

The Korean government has revised enforcement ordinance of the law. Especially, government has decided abridgement of tax subject and alleviation of tax standard, in order to minimize tax resistance and to enforce the law smoothly.

According to revised ordinance by government, it is shown that tax subjects be alleviated drastically. However, we can

anticipate the positive effects on land supply for urban housing by curtailment of tax subject, because it taxes on unrealized capital gains. Besides, it is liable to induce discredit on land policy. Therefore, it is necessary to establish taxation system related to lands thoroughly.

2) Revise proposal of the excessive profits tax on lands proposed by administration and local government

The excessive profits tax on lands is forced to solve weakpoints on tax subject and assessment method. Then, we have investigated the perception of the administration and local government who are operating the law, in practical.

According to the findings of questionnaire on tax subject, forty two % out of all are insisting that it is necessary for the agricultural areas in city to be exonerated. On the other hands, twenty four % out of all are insisting that it has to be included lands of all over the country, not but idle lands.

In addition to this, we have investigated perception on assessment method of the law. Half of them are insisting that we have to substitute transfer capital gains tax and comprehensive land tax for the excessive profits tax on lands longtimely, even though the law has to be persisted while the order of land market is estab-

lished. Twenty seven % are insisting that they have to consider assessment method matching real capital gains, because it is

not appropriate to levy for a nationwide increase rates of land price (Table 6).

Table 6. Perceptions on revise proposal of excessive profits tax on lands

	Revise proposal of excessive profits tax on lands	The administrative staff
Tax subject	Exonerate the agricultural areas in city from tax subject.	42
	Include all of the soaring lands, not but idle lands.	25
	Curtail the subjects of exemption	19
	The other.	14
Assessment method	Repeal the laws longtimely.	50
	Devise assessment method matching real capital gains.	27
	First of all, revise the public declaration system.	16
	Assess while holding, levy while disposing	7

In view of the results so far achieved, it is necessary to clarify tax subject and assessment method, in order to make consensus on the effects of the law and to increase the positive effects on land supply for urban housing. Moreover, we have to consider abolition, because we have comprehensive land tax and transfer capital gains tax, and we can't understand the unconstitutionality of the law.

Accordingly, we can summarize that it is good to enforce public side land supply owing to administrative, financial effects of the law. However, the law hinders the private side land supply. Therefore, it is necessary to reestablish land supply policy for urban housing, based on awareness revolution and comprehensive housing policy. This paper can be regarded primary study for urban land supply. Specifically, this paper offers the counterproposal to land supply for urban housing, to minimize the negative impacts, to maximize the positive impacts caused by the excessive profits tax on lands.

6. Concluding remarks and problems to be solved

This paper has analyzed empirically the impacts caused by the excessive profits tax on lands, offered counterproposal to encourage land supply for urban housing. In view of the results so far achieved, we

can have the following conclusion.

Firstly, people have consensus on the purpose of the law, however, they don't have consensus on the effects of the law for its imperfection.

Secondly, the law is timely enforced, which attributes to stabilize land price and to encourage public side land supply owing to positive effects in perception, administration, finance.

Thirdly, it is necessary to revise the excessive profits tax on lands and to change the method of urban land supply being suitable to an advanced society.

Problems to be studied hereafter are as follows. Firstly, we have to study on problems occurred in land use mechanism, because the law is connected with land use mechanism. Secondly, we evaluate the law from the side of Uruai Round negotiation being based on present land and housing supply policy, and propose the planning method for housing supply.

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ABSTRACT

The Korean government has introduced land policy reform measures recently, in order to stabilize the circulating system of land, without a parent law involving effective land use. The measures aim to change the pattern of land market rather than the pattern of land use. Especially, the excessive profits tax on land intends to redistribute the ownership of residential land, and to recapture windfall gains on an accrual basis. However, it may incur secondary gains in macro economics and an unintended reduction of urban land supply in the land market. This paper aims to study empirically the impact caused by the excessive profits tax on land, and to offer an alternative measure in order to promote urban land supply. Ultimately, this paper can be regarded as an interim report on outcome of research projects which aim to propose a method of urban land supply suitable to an advanced society.