

## **Stamp duty and registration fee: Is it time Kerala adopts a modern method of fixing fair value of land?**

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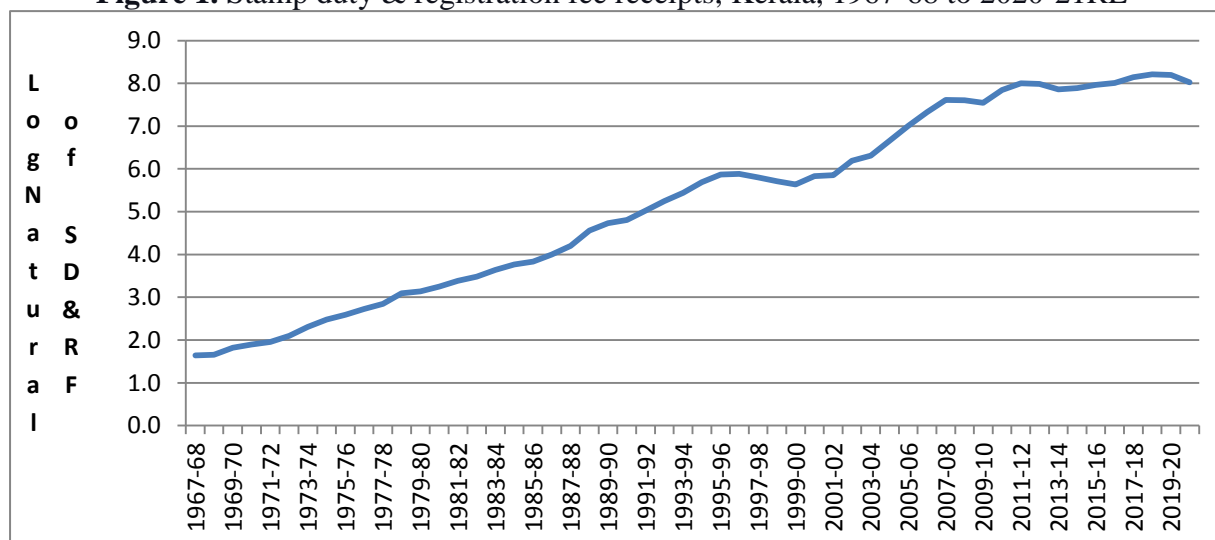
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### **1.Introduction**

Stamp duty and registration fee (SD&RF) was a major source of revenue in Kerala. During the second half of the 2000s, that is 2005-06 to 2009-10, it was next only to Sales tax and VAT contributing more than 12 per cent of the state's own taxes and duties. Its share has steadily fallen since then and it contributes only 6.76 per cent of the own taxes in 2020-21RE trailing to the third place behind taxes on vehicles. A major portion of the receipts from SD&RF in the state is derived from registration of transfer of property effected by way of instruments such as conveyance, gift, settlement, partition etc. As property value is a key subject in any of these registrations, it is well-known that under-valuation of property and evasion of tax was rampant. Fixation of fair value or guidance value is one of the methods adopted by governments to plug this loophole. Kerala too has followed this method during the last twenty-five years. It is important that we take a look at the method adopted to assess whether there is scope for improvement.

### **2. SD&RF trend**

SD&RF receipts over the last 54 years is presented in Figure 1 (in natural log). A careful look at Figure 1 suggests that the period 1967-68 to 2020-21 may be divided into three sub-periods to characterize the changing growth pattern. The three sub-periods are, I: 1967-68 to 1994-95; II: 1995-96 to 2007-08; and III: 2008-09 to 2020-21. Compound Annual Growth Rates (CAGR) of SD&RF for the three sub-periods are 15.91%, 12.39% and 5.18% respectively. It is evident that the growth rates are falling steadily. In the third sub-period the growth has fallen drastically going below the growth rate of Gross State Domestic Product (GSDP) of Kerala in current prices and growth rate of tax revenues leading to the fall of both ratio of SDRF to GSDP as well as SD&RF to State's Own Tax Revenue (SOTR).

**Figure 1.** Stamp duty & registration fee receipts, Kerala, 1967-68 to 2020-21RE

Source: Government of Kerala, Budget in Brief, various years, Finance Department.

### 3. Fair value fixation

It was known for long that considerable undervaluation of land is shown in the documents presented for registration to evade stamp duty. It was felt that a corrective need to be introduced and the insertion of Section 28A by Act 14 of 1988 to amend the Kerala Stamp Act, 1959 was the first step in that direction. This insertion was with regard to the fixation of fair value by the District Collector. The milestones in fair value fixation are well described in Table 7.2 of the C&AG's Report - 8, 2014, Chapter 7 which is reproduced below as Table 1. The description in the Table may be used to arrive at periods when a fair value had to be shown in the document and periods when it need not be. The average annual percentage change in SD&RF receipts during these periods are shown in Table 2.

There was no change in the rates of stamp duty for the major registration instruments during 1991 to 2010. So, we can take the period up to 2010 and examine Table 2 without bothering too much about the influence of rate change on SD&RF. It may be seen that whenever a fair value rule was in operation the receipts showed lower growth and the receipts grew at a much higher rate when the rule was not in operation. Obviously, people were taking advantage of the frequent changes in fair value rule. They were waiting for a relaxation to register the instruments. But from 2010 fair value rule had got firmly established and the poor growth in receipts over the ten years since then needs some careful look.

**Table 1:** Milestones in fixation

| Year | Event   | Remarks  |
|------|---|--|
| 1988 | Introduction of Section 28A and 45A of KS Act, 1959 relating to minimum value of land | Minimum value of land was fixed for the first time by the District Collectors  |
| 1991 | Section 28A and 45A of KS Act, 1959 relating to minimum value of land were withdrawn  | Withdrawn due to discrepancies in the minimum value fixed and reduction in number of documents presented for registration. |
| 1994 | Introduced Section 28A and 45A of KS Act, 1959 relating to fair value                 | New Section was introduced fixing criteria for determination of fair value of lands.                                       |
| 2004 | Fixed the fair value in January 2004 and withdrew the same in February 2004           | The fair value was withdrawn on basis of complaints from public regarding the fixation of fair value.                      |
| 2006 | In Budget 2006 the fixation of fair value was introduced again                        | Land was assigned classification into 15 categories.   |
| 2008 | The draft fair value was published in May 2008  | Seeking suggestions from the public  |
| 2010 | Published the fair value in March 2010  | Implemented with effect from 1 April 2010  |

**Table 2:** Average annual percentage change in SD&RF receipts by periods when fair value rule existed

| Period               | Fair Value Rule Existed | Average Annual Percentage Change |
|----------------------|-------------------------|----------------------------------|
| 1986-87 to 1988-89   | No                      | 27.7                             |
| 1989-90 to 1990-91   | <b>Yes</b>              | 13.2                             |
| 1991-92 to 1994-95   | No                      | 24.8                             |
| 1995-96 to 2003-04   | <b>Yes</b>              | 8.2                              |
| 2004-05 to 2009-10   | No                      | 24.7                             |
| 2010-11 to 2020-21RE | <b>Yes</b>              | 5.3                              |

The period 2010-11 to 2020-21 witnessed the stabilization of the fair value system. The message was clear that the fair value system is going to be there and that the value would see periodic rise. It was increased by 50 per cent in 2014-15 and an annual increase of 10 per cent from 2018-19 onwards (Table 3). The SD rate, however, kept on changing. It came down in 2013-14 only to go up again in 2016-17.

**Table 3:** Change in fair value and stamp duty rate, 2010-11 to 2020-21

| Year        | Fair Value |       | SD&RF Rate |              |             |
|-------------|------------|-------|------------|--------------|-------------|
|             | % Change   | Index | Panchayat  | Municipality | Corporation |
| 2010-11     | 0          | 100   | 7          | 8            | 9           |
| 2011-12     | 0          | 100   | 7          | 8            | 9           |
| 2012-13     | 0          | 100   | 7          | 8            | 9           |
| 2013-14     | 0          | 100   | 5          | 6            | 7           |
| 2014-15     | 50         | 150   | 6          | 6            | 6           |
| 2015-16     | 0          | 150   | 6          | 6            | 6           |
| 2016-17     | 0          | 150   | 8          | 8            | 8           |
| 2017-18     | 0          | 150   | 8          | 8            | 8           |
| 2018-19     | 10         | 165   | 8          | 8            | 8           |
| 2019-20     | 10         | 181.5 | 8          | 8            | 8           |
| 2020-21(RE) | 10         | 200   | 8          | 8            | 8           |

The rising fair value brings another dimension to the growth of the receipts. The growth can then be thought of as consisting of two components: a volume component and a price component. The price effect can be taken out by deflating the revenue receipts by the fair value index as worked out in Table 3. Applying the index on the reported receipts to deflate it and the change in the deflated series can then be viewed as a real increase in revenue. It turns out that the period saw an annual average decrease of 4.5 per cent. On an average, a 10 per cent annual increase in the fair value during this period (column 3, Table 3) has generated only 5 per cent increase in SD&RF receipts suggesting that the volume increase (after taking out the price effect) is less than 5 per cent. This looks a bit surprising, especially considering that GSDP growth has not been too low during the period and remittance flow has been robust. The Sd rate has also gone up. Hence, the question 'is the fair value system implemented in Kerala inadequate to capture the rising prices of land in the state' becomes relevant.

#### **4. C&AG audit findings: System without a base?**

C&AG audit of the fixation of fair value was conducted during May to September 2014 and covered the period April 2009 to March 2014. It was based on a fairly large sample consisting of seven districts, seven Revenue Division Offices, seven Taluks and 21 village offices under the Revenue and Disaster Management Department of the Government of Kerala. The information collected was corroborated with the files and records maintained by the Inspector General of Registration (IGR), Kerala and six Sub Registrar Offices. The soft copy of the database on fair value fixed for land in the State was also analysed.

The objective of fixation of fair value was to prevent the understatement of value of land shown in the documents presented for registration and the consequent evasion of stamp duty. The fair value of land is expected to be close to the market value so that the government does not lose revenue from stamp duty.

The objective was sought to be achieved by classifying the land as those lying in municipal corporations, municipalities and panchayat areas. Within the above further classification is to be done on the basis of a 15-point categorization as under: (i) commercially important plot; (ii) residential plot with NH/PWD road access; (iii) residential plot with Corporation/Municipality/ Panchayath road access; (iv) residential plot with private road access; (v) residential plot without road access; (vi) garden land with road access; (vii) garden land without road access; (viii) coastal belt; (ix) water logged land; (x) rocky land; (xi) waste land (in proximity to crematorium, dump yard etc); (xii) wet land; (xiii) hill tract with road access; (xiv) hill tract without road access; and (xv) government land. Fixation of land value has to be done by a village level committee with the village officer as convenor and forwarded to the Taluk level committee for onward transmission and finalization.

The most important finding of the C&AG is that no comprehensive guidelines clearly specifying the procedure and methodology for fixing the fair value was issued at any time. Further, it was "observed that in the absence of the clear parameters based upon which the market value of land is determined, the Department was not able to fix the fair value of the land as decided by Government" (Audit Report, p.80). It was also found that village level committees or taluk level committees were not constituted in majority of the villages and hence no public consultation was carried out.

C&AG found out that fair value was not fixed for all the survey numbers. Their scrutiny of the database of the selected seven Taluks and under seven RDOs revealed that fair value was not fixed in case of 1,32,991 survey numbers in 89 villages. Thus, the fair value database was incomplete. The incompleteness of the fixation of fair value persists even now. In the year 2020, a parcel of land owned by the author did not have a fair value. To get a certificate from the SRO was a herculean task with the papers moving from the village officer to the SRO many times, each time it moved only when properly greased. Thus, the incompleteness serves an important purpose and it is well known!

C&AG observed three types of irregularities in the fixation of fair value. The first type was that land is not classified according to the actual state or use at the time of fixation of fair value. Their test checks revealed that in a village in Palakkad - I, 18 cases involving 1.07 hectares of land was classified as residential plot or wetland whereas the actual use was commercial purpose as per Kerala Land Utilisation Orders 1967 by the RDO during 2006-08, that is prior to the date of fixation of fair value. Also, commercially important land lying in the heart of the town was classified as residential land.

The second type of anomalies were that value of similar, or comparable plots were very different. C&AG scrutiny showed that in 448 cases in 130 villages of Thiruvananthapuram the variation in fair values was 4 to 88 percent. In Perinthalmanna Taluk, for plots in 28 cases lying on the opposite/ adjacent sides of National Highway and State Highway showed variation from nine to 61 per cent. C&AG attributes these anomalies to "The failure to constitute VLC, absence of joint verification of village boundaries and lack of monitoring at the higher level" (p.84).

The third type of irregularity was fixation of low fair value of land. The draft fair value was published in the website on 5 May 2008. It was decided in June 2009 to fix the fair value at least 50 percent of the market value. C&AG in their test check found that in many cases the fair value fixed was far less than the value declared in the previous documents registered. They concluded that "Even on considering the value shown in the previous documents registered as the market value, the fair value fixed was less than 50 percent of the previous transaction value. Audit noticed that the fair value fixed was only 2.51 to 47.84 percent of the value shown in the previous documents" (PP. 84-5). The System of fixation of fair value was intended to get over the understatement of value of land in the documents presented for registration and if such fair value itself was 3 to 48 percent lower than the value shown in the documents one could imagine the farce of fair value fixation in the State.

In sum, the design of the System to fix fair value in the State suffers from severe infirmities. The most important lacuna is the absence of comprehensive guidelines and procedures for fixing the fair value of land. It is left to the whims and fancies of the village officers with hardly any public consultation or supervision and scrutiny at the higher level. Thus, the fair value fixed is often much lower than the value shown in the previously registered documents which it may be presumed is far below the market value to get over which the fair value System was conceived! Understandably, the System has not yielded the desired benefits.

## 5. Use of remote sensing and GIS in fixing land value

Market value of land is defined as the highest price between an agreeable buyer, who would pay, and an agreeable seller, who would bear, both being fully knowledgeable. This information is known only to the buyer and the seller and the document presented for registration of the sale of the land may not show the market value. The Government loses revenue when the documented value is lower than the market value. The objective of a system of fixation of fair value or guidance value is to get over this problem and increase the SD&RF revenue receipts.

The fixation of fair value is aimed at getting a price close to the market value. One approach to the subject is through the factors determining the market value of land. Value of land is a function of the use to which it is put and land use can vary from agriculture, tourism, residential rural, residential urban, commercial and so on and the factors determining each use may be as shown in Table 4.

**Table 4:** Factors influencing land value

| <b>Land Use</b>   | <b>Factors determining value</b>  |
|-------------------|---|
| Agriculture       | Adjacent vegetation, historic condition, hydrology, land use, soil, and vegetation cover<br>Infrastructure, land form, land texture, land use map, road network, and soil |
| Aquaculture       | Elevation, landforms, major roads, soil type, urban areas, and vegetation cover   |
| Urban Residential | Environment, hospital network, road network, school network, sewer network, and slope   |
| Rural Residential | Environment, land carrying capacity, land use type, landform, and Soil  |
| Urban Commercial  | Road network, transportation systems, sewer network, and slope, Office complexes, population density  |

Determining the land parcel value is based on a number of physical and economic attributes that have to be carefully considered in the land valuation process. Few of the mentioned attributes are inherent to the property, and others are outer ecological factors. Through an objective way, we can determine these factors; however, there will always be a definite level of bias that is hard to measure in the evaluation process. Location impacts are considered to be the most important in asset value, although their inclusion in valuation systems is often indirect. It is often not possible to determine the exact value of a parcel of land, but the valuation of the property is feasible (Balaji Lakshmana Rao et al, 2021). These may be called

location and qualitative attributes. There could also be other macroeconomic factors like income growth, money supply, interest rate and remittances that influence property prices. A strong relationship between GDP growth and house prices has also been observed in many countries. These relationships could be used to arrive at indicators which update the benchmark values to current periods.

These qualitative dimensions could be used to generate land appraisal maps. Vector based cadastral maps can be superimposed on them to determine parcel based real estate valuations. GIS plays an important role in efficiently extracting spatial variables and lesson labor and time inputs. There exist numerous models tried the world over for the fixation of land value. However, the cost of building the database for such model development can be on the higher side. But once developed it could help the government garner more revenue receipts and hence it is worth the effort.

## **6. Summary and recommendations**

The System of fair value fixation in Kerala suffers from many infirmities. Foremost among them is the lack of a scientific base and comprehensive guidelines for the fixation of land value. There was hardly any public consultation or supervision of what was done at the level of the village offices. The result was a system with fair value often significantly lower than the documented value which in turn was much below the market value.

Unlike in the past, now tools are available to develop appraisal value of land drawing on models that estimate the determinants of land value. Well tested models are now found that are used the world for this purpose. Kerala should move ahead and use modern methods, such as Geographic Information System and satellite imagery to institute a comprehensive fair value system so that SD&RF could regain its lost glory and become an important source of revenue again.

## **References:**

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