

# TAXING PROPERTY IN A NEO-DEVELOPMENTAL STATE: THE POLITICS OF URBAN LAND VALUE CAPTURE IN RWANDA AND ETHIOPIA

TOM GOODFELLOW\*

## ABSTRACT

Of the African states experiencing sustained growth and poverty reduction in recent decades, Rwanda and Ethiopia stand out due to the scope of their development visions and relatively effective state-driven transformation, leading them to be compared to the East Asian ‘developmental states’. This article argues that these two states are better conceived as ‘neo-developmental’ due to important differences in the international and national constraints they face compared with the East Asian ‘tigers’. One effect of these differences is the difficulty of attracting investment into manufacturing industry, and the consequent concentration of capital in high-end urban real estate. This underscores the need for effective land value capture and property taxation, which featured strongly in the East Asian cases. Currently, however, both Rwanda and Ethiopia lack effective mechanisms for capturing the value of urban property in a way that is sustainable, redistributive and developmental. The article explores the politics of efforts to introduce property tax in both cases. It argues that property taxation has been obstructed by conflicting imperatives on land reform and tax reform, alongside resistance from vested interests created by the rapid generation of real estate-based wealth in the absence of other sufficiently lucrative investment options.

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FOLLOWING A LONG PHASE OF ‘AFRO-PESSIMISM’ rooted in the sluggish and sometimes negative growth of the 1980s and 1990s, optimism about

\*Tom Goodfellow ([t.goodfellow@sheffield.ac.uk](mailto:t.goodfellow@sheffield.ac.uk)) is a Senior Lecturer at the Department of Urban Studies and Planning, University of Sheffield. I would like to thank John Henneberry, three anonymous reviewers and the journal editors for their very helpful comments on earlier drafts of this paper. I would also like to thank the two anonymous reviewers and Mick Moore for their comments on an earlier working paper on the topic. Most of the research for this paper was conducted with a grant from the International Centre for Tax and Development.

the development potential of a number of 'African lion' states began to intensify in the late 2000s.<sup>1</sup> This optimism is partly predicated on the performance of resource-rich economies benefitting from rising primary commodity prices, such as Nigeria and Angola. Yet it also alludes to the persistent progress of a few smaller, less well-endowed economies that seem to have defied the economic odds. Foremost among these are Ethiopia and Rwanda, whose growth and poverty-reduction performance has been more consistent and concerted than most of the continent. There has been mounting interest not only in the economic achievements of these states but the fact that their progress has been substantially state-driven, deriving partly from unorthodox economic policies, accompanied by restrictive political environments that have drawn substantial criticism.<sup>2</sup> The distinctiveness of these two states is such that a leading Africanist recently claimed that Ethiopia and Rwanda are 'the only two states that can claim to be developmental states in Africa'.<sup>3</sup>

This reference to 'developmental states', now commonplace in discussions of Rwanda and Ethiopia, clearly alludes to the East Asian experience of successful state-driven development.<sup>4</sup> Yet despite important similarities, neither the probability of long-term developmental success in these African countries nor their similarity to the East Asian 'tigers' should be taken for granted. Although their political leaders have looked determinedly towards the East when devising economic strategies, the international environment in which they find themselves has transformed beyond recognition since the time of the East Asian miracle. They are also both highly dependent on foreign aid, and must balance their inclination towards state-directed development with policy imperatives from Washington and Europe, as well as the need to attract international capital in a highly competitive globalized environment. Moreover, they are landlocked, agrarian economies suffering from high transport costs,

1. McKinsey, *Lions on the move: The progress and potential of African economies* (McKinsey Global Institute, 2010). Note that this report should be taken with a pinch of salt, especially as it classifies Ethiopia as a 'coastal' country.

2. Filip Reyntjens, 'Constructing the truth, dealing with dissent, domesticating the world: Governance in post-genocide Rwanda', *African Affairs* 110, 438 (2011), pp. 1–34; Lovise Aalen and Kjetil Tronvoll, 'The end of democracy? Curtailing political and civil rights in Ethiopia', *Review of African Political Economy* 36, 120 (2009), pp. 193–207.

3. Comment made by Christopher Clapham at the workshop 'Developmental States Beyond East Asia', Newcastle University, June 2015.

4. In line with this focus, my use of the term 'development' here refers specifically to economic development, comprising economic growth, structural transformation (particularly away from agriculture), and poverty reduction. The mutually reinforcing achievement of these goals was a distinctive feature of the East Asian cases. This is not to deny the importance of other conceptions of development, including those linked to the expansion of substantive social and political freedoms, which took significantly longer to emerge in these countries. Constraints on freedom are notable features of the two countries under consideration, though there is not space to explore these in depth here.

limited bureaucratic capacity and highly constrained access to far-flung markets.

For these and other reasons, pursuing the internally integrated industrial growth that characterized economic transformation in Japan, South Korea, Taiwan, Singapore, and Hong Kong is very difficult. In their attempts to ‘construct comparative advantage’,<sup>5</sup> political elites committed to developmental transformation in Ethiopia and Rwanda have focused largely on upgrading agricultural productivity, agri-processing, and service sectors. This is starting to change, especially in Ethiopia,<sup>6</sup> but despite some success in securing manufacturing foreign direct investment, many investors perceive larger and quicker profits in large-scale land acquisition for agriculture, or the development of urban real estate. Indeed, the scale of profits that can be made in the latter, in a context of rapid urbanization, economic growth, and the influx of international capital and personnel into major cities, is so substantial as to outweigh a multitude of government incentives to invest in other sectors. It is consequently little surprise that both construction and real estate services are booming in both countries.

This presents an opportunity for governments to raise much-needed revenues. The potential for property taxation to benefit Africa’s development has been highlighted in recent years,<sup>7</sup> and the importance of capturing land value was also central to the development trajectory of the East Asian ‘tigers’, as I will show below. If anything, in contexts where investment in urban real estate is especially appealing due to the limitations of other options, effective urban land value capture is even more important. Yet moves towards effective property taxation have largely failed in both Ethiopia and Rwanda. For different reasons in each case, the political obstacles to property taxation have proven extremely stubborn, partly due to the ways in which property tax interacts (either consciously or contingently) with land reforms. Conflicting imperatives and incentives relating to land and tax reform have set back the cause of sustainable and progressive urban land value capture in both states.

This article highlights two neglected and interlinked aspects of the debate on developmental states in Africa: the role of urban property development in the politics underpinning developmental coalitions, and the

5. Robert Wade, *Governing the market: Economic theory and the role of government in East Asian industrialization* (Princeton University Press, Princeton, NJ, 1990).

6. Arkebe Oqubay, *Made in Africa: Industrial policy in Ethiopia* (Oxford University Press, Oxford, 2015); Cornelia Staritz and Lindsay Whitfield, ‘Made in Ethiopia: The emergence and evolution of the Ethiopian apparel export sector’ (CAE Working Paper 2017: 3, Roskilde University, 2017).

7. Roy Bahl Richard Bird, ‘Subnational taxes in developing countries: The way forward’, *Public Budgeting and Finance* 28, 4 (2008), pp. 1–25; Odd-Helge Fjeldstad and Kari Heggstad, ‘Local government revenue mobilisation in Anglophone Africa’ (Working Paper EP1, Institute for Development Studies, Brighton, 2012); Nara Monkam and Mick Moore, *How property tax would benefit Africa* (Africa Research Institute, London, 2015).

prospects for land value capture to contribute to revenue-raising and redistribution. The article begins by situating Rwanda and Ethiopia vis-à-vis the developmental states concept, exploring key similarities and differences with the ‘classical’ developmental state model, before considering the role of urban land, property, and taxation in this paradigm. It then explores the political economy of efforts to tax property and implement land reform in Kigali and Addis Ababa, presenting an analysis of progress, pitfalls, and obstacles in each case. Despite both exhibiting failures to tax property effectively, other forms of land value capture have been relatively successful in raising revenues in recent years, especially in Ethiopia. These forms of land value capture do not, however, hold the same potential for sustainable and progressive development as property taxation, and may be undermining the prospects for the latter to emerge as a significant revenue instrument. The article concludes by highlighting key aspects of the challenge and its implications for ‘neo-developmental states’ in Africa.

### *Neo-developmental states in Africa*

Amid disillusionment with the ‘Washington Consensus’ and the rising influence of heterodox interpretations of East Asian success, significant attention has been devoted to the prospects for developmental states in Africa.<sup>8</sup> What distinguishes Rwanda and Ethiopia from the other African countries discussed in this literature are certain specific ways in which they are comparable to (and emulate) the East Asian cases, for example with regard to the lack of a substantial natural resource base, high and sustained economic growth rates, and constraints on political freedoms. A growing body of literature alludes to the parallels between these two countries and the East Asian experience.<sup>9</sup> As in East Asia, there are important differences *between* these two African countries, not least regarding the retention of land ownership by the state and greater emphasis on manufacturing in Ethiopia, a stronger market orientation in Rwanda, and the significantly

8. See for example Thandika Mkandawire, ‘Thinking about developmental states in Africa’, *Cambridge Journal of Economics* 25, 3 (2001), pp. 289–314; Omano Edigheji (ed.), *Constructing a democratic developmental state in South Africa: Potentials and challenges* (Human Sciences Research Council, Cape Town, 2010); Ben Fine, ‘Can South Africa be a developmental state?’, in Edigheji (ed.), *Constructing a democratic developmental state in South Africa*, pp. 169–182; Timothy M. Shaw, ‘Africa’s quest for developmental states: ‘Renaissance’ for whom?’, *Third World Quarterly* 33, 5 (2012), pp. 837–851.

9. David Booth and Frederick Golooba-Mutebi, ‘Developmental patrimonialism? The case of Rwanda’, *African Affairs* 111, 444 (2012), pp. 379–403; René Lefort, ‘Free market economy, ‘developmental state’ and party-state hegemony in Ethiopia: The case of the ‘model farmers’’, *The Journal of Modern African Studies* 50, 4 (2012), pp. 681–706; Alex De Waal, ‘The theory and practice of Meles Zenawi’, *African Affairs*, 112, 446 (2013), pp. 148–155; Tim Kelsall, *Business, politics, and the state in Africa: Challenging the orthodoxies on growth and transformation* (Zed Books, London, 2013); Iginio Gagliardone, ‘New media and the developmental state in Ethiopia’, *African Affairs* 113, 451 (2014), pp. 279–299; Oqubay, *Made in Africa*.

different size of their populations and economies. This makes them particularly interesting countries to compare with one another, an endeavor that surprisingly few researchers have yet systematically undertaken. Despite these differences, their common affinity with the East Asian developmental state model is worth highlighting in greater detail.

First, the governing regimes in Ethiopia and Rwanda, in power since 1991 and 1994 respectively, are characterized by a dominant ‘developmental orientation’ among the political elite,<sup>10</sup> linked to the fact that the needs of their political survival are in line with the needs of economic development.<sup>11</sup> Both regimes exhibit the strategic state entrepreneurialism analyzed by Alice Amsden in South Korea, and close-knit relations between state and private sector reminiscent of the ‘authoritarian corporatism’ that Robert Wade observed in Taiwan.<sup>12</sup> Efforts to discipline capital, control finance, and guide foreign investment are evident in both countries, though more markedly in Ethiopia.<sup>13</sup> The use of party- and military-owned firms in both states to make strategic investments is now well known.<sup>14</sup> In both cases, the state also holds majority shares in key banking institutions and retains control over crucial assets, notably land in the case of Ethiopia,<sup>15</sup> highlighting similarities with the approach in the East Asian city-states of Singapore and Hong Kong.<sup>16</sup> As in the East Asian cases, they lack major natural resources for generating export revenues, and are characterized by a persistent sense of regime insecurity due both to the potential for domestic unrest and the presence of hostile armed forces in the wider region.<sup>17</sup> The presence of a political class committed to developmental transformation, and explicitly oriented towards East Asia in its pursuit

10. Chalmers Johnson, *MITI and the Japanese Miracle: The growth of industrial policy, 1925–1975* (Stanford University Press, Stanford, CA, 1982).

11. Wade, *Governing the market*; Adrian Leftwich, *States of development: On the primacy of politics in development* (Polity, Cambridge, 2000).

12. Wade, *Governing the market*; Alice Amsden, *Asia’s next giant: South Korea and late industrialization* (Oxford University Press, Oxford, 1989).

13. Sarah Vaughan and Mesfin Gebremichael, ‘Rethinking business and politics in Ethiopia’, *Africa Power and Politics Programme Research Report 2* (Overseas Development Institute, London, 2011); Toni Weis, ‘Dominant parties and the private sector in Sub-Saharan Africa: A typology of approaches’, *Zeitschrift für Vergleichende Politikwissenschaft* 8, 3–4 (2014), pp. 263–281.

14. Booth and Golooba-Mutebi, ‘Developmental patrimonialism?’; Vaughan and Gebremichael, ‘Rethinking business and politics in Ethiopia’; Pritish Behuria, ‘Between party capitalism and market reforms: Understanding sector differences in Rwanda’, *The Journal of Modern African Studies* 53, 3 (2015), pp. 415–450.

15. John Markakis, *Ethiopia: The last two frontiers* (Boydell and Brewer, Rochester, 2011).

16. Eddie Chi-Man Hui, Vivian Sze-Mun Ho, and David Kim-Hin Ho, ‘Land value capture mechanisms in Hong Kong and Singapore: A comparative analysis’, *Journal of Property Investment and Finance* 22, 1 (2004), pp. 76–100.

17. Richard F. Doner, Bryan K. Ritchie and Dan Slater, ‘Systemic vulnerability and the origins of developmental states: Northeast and Southeast Asia in comparative perspective’, *International Organization* 59, 2 (2005), pp. 327–361.

of this goal, is also a feature of both states, and something written about extensively by the late Ethiopian Prime Minister Meles.<sup>18</sup> Importantly, it is not only the political and economic structures that bear resemblance but also the continued progress on economic and social indicators over an extended period of time,<sup>19</sup> as well as many aspects of the constrained political environment.<sup>20</sup>

Despite these many important similarities, the development trajectories of Rwanda and Ethiopia are different in critical ways from their East Asian predecessors. First, their capacity to discipline firms and guide investment is partially constrained by high dependence on international aid and policy advice from donors generally averse to sustained state intervention. Second, the regional dynamics characteristic of the East Asian experience are lacking, whereby a proximate ‘model’ (such as Japan) could both be emulated and provide a regional market for lower value-added product inputs as it moves up the value chain. Third, they are landlocked and face infrastructure and transport costs on a different scale from the coastal, island, and city-state geographies of the East Asian ‘tigers’, despite major infrastructure projects attempting to mitigate this, especially in Ethiopia. Major land reforms have been undertaken in both countries (although these differ substantially, as shown below) in an effort to reduce the power of landed interests and promote development, something that was crucial for laying the foundations of successful industrialization in East Asia.<sup>21</sup> However, the Rwandan and Ethiopian governments lack the capacity to convert former landlords into an industrial class in the way that was achieved in South Korea and Taiwan.<sup>22</sup>

Consequently, while all the East Asian developers were dependent on exporting manufactured goods, there is a less concerted focus on industrialization in Ethiopia and Rwanda—especially in the latter, which has largely geared itself towards transforming agriculture and developing service sectors including ICT, logistics, finance, and tourism. This is partly strategic given that under current global conditions, countries are running out of industrialization opportunities sooner and at much lower-income

18. Meles Zenawi, ‘States and markets: Neoliberal limitations and the case for a developmental state’, in Akbar Noman, Kwesi Botchwey, Howard Stein, and Joseph E. Stiglitz (eds), *Good growth and governance in Africa: Rethinking development strategies* (Oxford University Press, Oxford, 2012), pp. 140–174.

19. See for example *Africa’s Pulse*, Volume 7, April 2013, <[http://www.worldbank.org/content/dam/Worldbank/document/Africa/Report/Africas-Pulse-brochure\\_Vol7.pdf](http://www.worldbank.org/content/dam/Worldbank/document/Africa/Report/Africas-Pulse-brochure_Vol7.pdf)> (13 May 2016).

20. Hilary Matfess, ‘Rwanda and Ethiopia: Developmental authoritarianism and the new politics of African strong men’, *African Studies Review* 58, 2 (2015), pp. 181–204.

21. Cristóbal Kay, ‘Why East Asia overtook Latin America: Agrarian reform, industrialisation and development’, *Third World Quarterly* 23, 6 (2002), pp. 1073–1102.

22. Manuel Castells, ‘Four Asian tigers with a dragon’s head’, in Richard P. Appelbaum and Jeffrey William Henderson (eds), *States and development in the Asian Pacific Rim* (Sage Publications, Newbury Park, CA, 1992), pp 33–70.

levels than their forebears,<sup>23</sup> notwithstanding some efforts to integrate into global value chains. While contemporary developing countries may be able to look to services-led growth strategies instead, services are typically skill-intensive and do not have the same capacity as manufacturing to absorb the kind of large-scale low-skilled labor in which many African countries are so abundant.<sup>24</sup>

For all these reasons, we can consider Rwanda and Ethiopia ‘neo-developmental states’: states led by regimes with the intensity of developmental orientation possessed by their East Asian forerunners, which is translating into sustained growth and poverty-reduction, but which are globally and regionally anchored by different sets of incentives and constraints. While there are parallels between the concept of ‘neo-developmental states’ and the idea of ‘developmental patrimonialism’, the latter is specifically concerned with dynamics of centralized rent-management over particular time horizons. The concern here is rather with the strategic role of the state in harnessing domestic and international forces towards national economic interests, including the politics of securing investment into key economic sectors over others.<sup>25</sup>

#### *The role of property and land value capture in developmental states*

Despite their focus on industrialization, strategic urban property development and the capture of value from land and property played a central role in the strategies of several of the East Asian ‘tigers’. Land value capture is used here in a broad sense to refer to the range of instruments used by governments to derive revenue from the value of land and structures build upon it.<sup>26</sup> This may include leasing or sale of publicly owned land, land acquisition and resale, recurrent (e.g. annual) property taxes, capital gains taxes, and betterment levies based on imputed increases in property value due to public investment or changes in property rights.

The city-states of Singapore and Hong Kong have been termed ‘property states’ due to deliberate state-led property development and the central role of land and buildings in national wealth.<sup>27</sup> From an early stage, there was an effort in both Singapore and Hong Kong to drive the

23. Dani Rodrik, ‘Premature deindustrialization’, *NBER Working Paper No. 20935* (Cambridge, MA: National Bureau of Economic Research, 2015), p. I; Oqubay, *Made in Africa*, p. 10.

24. Rodrik, ‘Premature deindustrialization’, p. 24.

25. Amsden, *Asia’s next giant*; Ziya Öniş, ‘The logic of the developmental state’, *Comparative Politics* 24, 1 (1991), pp. 109–126.

26. This follows Chi-Man Hui *et al.*, ‘Land value capture mechanisms’, p. 77. There are also more specific definitions that define land value capture as when governments trigger increases in land values via regulatory decisions or infrastructure investments and then redistribute this land value increment, see Ian Palmer and Stephen Berrisford, ‘Urban infrastructure in sub-Saharan African cities’ (African Centre for Cities, Cape Town, 2015).

27. Anne Haila, ‘Real estate in global cities: Singapore and Hong Kong as property states’, *Urban Studies* 37, 12 (2000), pp. 2241–2256.



economy through property while also recapturing some of that value for public investment, limiting speculative investments in the real estate sector to incentivize investments in manufacturing.<sup>28</sup> In both of these cases, most land is publicly owned, allowing the government not only to subsidize certain land uses like housing and industry by providing free or cheap land but also to capture the value of land leased for private development and prevent speculation. Land value was captured through auctioning land leases but also various forms of progressive property-related taxes, including annual taxes on real property, rental income tax, betterment levies, and taxes on capital gains.<sup>29</sup> These instruments resulted in substantial government revenues. Annual property taxes alone account for around 8 percent of the total tax collected nationally by Singapore's inland revenue,<sup>30</sup> almost double the high-income country average of 4.5 percent.<sup>31</sup> Alongside its property-led strategy, Singapore used its fiscal structure to help encourage investment into industry from an early stage, drawing on a relatively educated population and well-developed infrastructure.<sup>32</sup>

Urban property development features less strongly in growth narratives of South Korea, a largely rural society with less than 30 percent of the population living in cities in 1960 when its economic transformation started in earnest. However, urbanization was extremely rapid: the urban population rose to almost 50 percent by 1975 and 75 percent by 1990. There were precipitous rises in land prices in the 1970s and 1980s, such that between 1974 and 1996, land values in Seoul increased 33-fold.<sup>33</sup> Significantly, however, progressive property taxes were adopted from the 1970s to prevent excessive speculation and to facilitate redistribution.<sup>34</sup> It was only from the mid-1980s, when returns from surplus capital in the industrial sector were diminishing, that speculative urban property development took off and property developers became a more politically salient sector.<sup>35</sup> Yet the taxes were already in place, and at the turn of the millennium, property-related taxes comprised a higher percentage of tax revenue in Korea than in any other country in the OECD.<sup>36</sup>

28. Haila, 'Real estate in global cities', p. 2247.

29. Chi-Man Hui *et al.*, 'Land value capture mechanisms'.

30. Haila, 'Real estate in global cities'.

31. John Norregaard, 'Taxing immovable property: Revenue potential and implementation challenges' (International Monetary Fund report, Washington D.C., May 2013), p. 40.

32. Castells, 'Four Asian tigers with a dragon's head'.

33. Hae Un Rii and Jae-Seob Ahn, 'Urbanization and its impact on Seoul, Korea', in *Forum on Urbanizing World and UN Human Habitat II* (Columbia University, New York, 2002), pp. 83–100.

34. Thomas Dalsgaard, 'The tax system in Korea: More fairness and less complexity required', OECD Economics Department Working Paper No. 271 (OECD Publishing, Paris, 2000).

35. Hyun Bang Shin, 'Property-based redevelopment and gentrification: The case of Seoul, South Korea', *Geoforum* 40, 5 (2009), pp. 906–917.

36. Dalsgaard, 'The tax system in Korea'.



Property-related taxes also played a key role in local revenue mobilization in Taiwan. In 1985, when the territory was mid-way through its extraordinary growth, ‘house taxes’ and ‘land value increment tax’ (a form of capital gains tax) collectively comprised over 70 percent of local government revenues.<sup>37</sup> As shown below, this percentage is far higher than is common for developing countries today. Moreover, the policy of capturing land value dates back to as early as 1912, and was made concrete in a 1954 statute that explicitly aimed to use property taxation to ensure ‘public enjoyment of future land increment’.<sup>38</sup>

This focus on capturing property values does not mean that unusually *high levels* of taxation were central to the East Asian success; in fact, the tax/GDP ratios were not much higher than the average for countries in Africa.<sup>39</sup> Rather, the composition of taxes differed significantly, with East Asian countries having relatively high levels of direct taxation including property-related taxes.<sup>40</sup> Given these aspects of the East Asian story, the degree to which East Africa’s aspiring neo-developmental states are emulating this focus on capturing land and property values is an important concern. This concern is underscored by the absence of a clear route towards industrialization in many African states, meaning that economic elites are especially inclined to maximize profits from land itself, including in the form of urban real estate.

The role of the urban in the development trajectories of contemporary African states varies significantly, but rarely resembles the ‘urban bias’ lamented by Robert Bates and others in the 1970s and 1980s, whereby political elites were seen as pandering to urban industrial classes.<sup>41</sup> Rather, we see an ascendant class of urban property owners alongside ‘urban fantasies’ based on ‘speculative urbanism’ and images of iconic real estate from Dubai to Singapore.<sup>42</sup> Moreover, in Rwanda and Ethiopia specifically, there is a substantial class of returnee elites, often bringing significant capital with them, for whom urban land offers especially attractive investment opportunities. The sectors of the economy linked to urban real estate are consequently booming. In Rwanda, the compound annual growth rate for construction in the period 2006–2013

37. Alvin H. S. Lam, ‘Republic of China (Taiwan)’, in W. Samuels (ed.) *Land value taxation around the world*, Special Issue of the *American Journal of Economics and Sociology* 59, 5 (2000), p. 330.

38. *Ibid.*, p. 328.

39. Alice Sindzingre, ‘Financing the developmental state: Tax and revenue issues’, *Development Policy Review* 25, 5 (2007), pp. 615–632.

40. Atul Kohli, *State-directed development: Political power and industrialization in the global periphery* (Cambridge University Press, Cambridge, 2004).

41. Robert Bates, *Markets and states in tropical Africa* (University of California Press, Berkeley, 1981).

42. Vanessa Watson, ‘African urban fantasies: Dreams or nightmares?’, *Environment and Urbanization* 26, 1 (2014), pp.1–17.

was 19.66 percent, dwarfing all other sectors of the economy. Real estate services also grew at 6 percent, while the compound annual growth rate of manufacturing over the same period was just 3.26 percent.<sup>43</sup> Meanwhile, in Ethiopia, the real estate sector grew by an annual average of 14.1 percent in the second half of the 2000s, which is significantly above the overall GDP growth rate.<sup>44</sup>

The high degree of urban concentration and limited transport infrastructure characteristic of many African states means that the capital city tends to become ever more magnetic for real estate investment. In Kigali, government policy embraces the development of luxury housing and commercial real estate by private developers. The national social security fund has invested in major high-end housing projects, while the Kigali Master Plan envisages a gleaming futuristic city, and the Rwandan development board has allowed generous incentives in the construction sector. Partly due to the influx of international personnel and capital after the genocide,<sup>45</sup> rental incomes in Kigali reached ‘US prices’ by the end of the 2000s, with houses commonly being rented to expatriates for US\$3,000 per month or more.<sup>46</sup> Given the great potential for profits, it is not surprising that 73 percent of investment from the top 10 domestic investors between 2006 and 2010 was in real estate or construction.<sup>47</sup>

In Ethiopia, urban real estate is equally if not more lucrative, although not explicitly favored. It is very hard to get loans for real estate development, so for those who already have capital to invest, building houses is all the more profitable given the high demand relative to supply. Profits of 100 percent are commonplace in Addis Ababa for those with the finance to build and sell, and house prices commonly double every 5 years.<sup>48</sup> Moreover, the Ethiopian diaspora, who bring substantial resources to invest in the country, are prohibited from investing in the five key sectors of banking, telecommunications, media, insurance, and transport, which the government considers strategically important to keep within the domestic sphere.<sup>49</sup> Consequently, much of the investment from the diaspora community is in real estate, often in the form of commercial

43. Figures acquired from the Rwandan Ministry of Finance and Economic Development, June 2014.

44. Access Capital, ‘Sector report—Real estate’ (Access Capital, Addis Ababa, 2010).

45. For a discussion, see Tom Goodfellow and Alyson Smith, ‘From urban catastrophe to ‘model’ city? Politics, security and development in post-conflict Kigali’, *Urban Studies* 50, 15 (2013), pp. 3185–202.

46. Interview, taxation adviser, Kigali, 1 December 2009.

47. Tom Goodfellow, ‘Rwanda’s political settlement and the urban transition: Expropriation, construction and taxation in Kigali’, *Journal of Eastern African Studies* 8, 2 (2014), pp. 311–329.

48. Interview, property developer, Addis Ababa, 30 September 2014.

49. Interview, Ethiopian Investment Authority, Addis Ababa, 1 October 2014.

buildings for rental.<sup>50</sup> Indeed, 60 percent of all investment by diaspora in the period between 1994 and 2014 was in real estate and related services. They invested *four times more* in this sector than in manufacturing, despite numerous official incentives in place for the latter, and 91 percent of all diaspora investment was in Addis Ababa. Over the same period, domestic investors also invested more in real estate than in any other sector, including manufacturing.<sup>51</sup>

This dominance of property in both cases as a sphere for domestic and diaspora investment raises important questions about whether and how the value that accrues to real estate assets is being captured by the public purse for broader development goals, as it was to a significant degree in the East Asian ‘tigers’. Rwanda and Ethiopia differ in critical ways from these states, as has already been noted. Yet there are reasons to believe that these differences make effective land value capture mechanisms *more* rather than less important. Although not city-states like Singapore or Hong Kong, Ethiopia, and especially Rwanda are relatively densely populated and can ill afford for land to be used in suboptimal ways. Moreover, having large, mostly poor rural populations as well as growing and relatively unskilled urban populations, the need to drive investment into sectors that can absorb labor is urgent, even if global conditions make finding such investment challenging. Ethiopian diaspora investment data indicate that investments in manufacturing create more jobs than investments in real estate by a ratio of four to one,<sup>52</sup> yet the latter is where many investors are channeling their capital.

This developmental imperative to generate jobs and transform the economy, alongside the need to raise government revenues to fund basic infrastructure, bolsters the need for effective land value capture mechanisms. Given their institutional and infrastructural constraints and very low average incomes, we would not expect Rwanda or Ethiopia to adopt the same mix of land value capture instruments as Singapore. There is, however, little evidence that the reforms thus far adopted to capture land and property values in either are well suited to their own development requirements. Rather, the progressive, anti-speculative, and developmental property taxation they need has been actively blocked or more passively resisted, with worrying long-term consequences.

### *Kigali: confusion and passive resistance*

The government led by the Rwandan Patriotic Front (RPF), which took power in 1994, introduced a decentralization policy from 2000 through

50. Ibid.

51. Figures acquired from the Ethiopian Investment Authority, October 2014.

52. Ibid.

which substantial resources and responsibilities were devolved to local governments. The Law No. 17/2002 institutionalized various types of central-local transfer and decentralized three taxes previously collected centrally: a recurrent property tax, trading licence tax, and rental income tax. These were supposed to form the bedrock of local revenue for districts, alongside various fees for specific services and rent paid on plots of leasehold land (discussed below). All property owners with freehold titles were obliged to pay property tax, barring various exemptions. Some of the city's older properties were already on government registers (though often valuations were from as long ago as the 1960s), with owners required to pay 0.2 percent of the registered value annually in tax.<sup>53</sup> Owners of new properties were supposed to have their properties valued for taxation, with assessments based on square meters of land and buildings.

A new local taxation law at the end of 2011 (Law No. 59/2011) introduced significant changes.<sup>54</sup> In contrast to the previous approach to property taxation, this law aimed to introduce a tax based on market (capital) value rather than floor area. The law specifies that market values should be determined on the basis of self-reported value, but outlines only in very general terms how market values should be assessed, which in the words of one local tax expert is 'asking for trouble'.<sup>55</sup> Perhaps even more problematic is that the new law set the tax rate at 0.1 percent of the assessed value for all properties, whether commercial, residential, or industrial. The 0.2 percent levied previously was already remarkably low by international standards.<sup>56</sup>

Both before and after these changes, the performance of property tax as a revenue instrument was extremely weak. In the late 2000s, property tax comprised at most 4 percent of locally collected revenue.<sup>57</sup> In many developed countries it commonly accounts for over 50 percent of locally collected revenues and, in some cases, 100 percent.<sup>58</sup> Even in neighboring Uganda, it accounts for over a third.<sup>59</sup> Instead, most of Rwanda's locally generated revenue is composed of various forms of fees. In 2012,

53. Interview, government decentralization official, Kigali, 4 February 2010. For further details on this and other aspects of property taxation and land leasing in Kigali, see Tom Goodfellow, 'Taxing the urban boom: Property taxation and land leasing in Kigali and Addis Ababa' (Working Paper Working Paper 38, International Centre for Tax and Development, Institute for Development Studies, 2015).

54. In this law, property tax is referred to as 'Fixed Asset Tax'. I will, however, retain the use of the term 'property tax' throughout this paper for consistency and to avoid confusion.

55. Personal communication, 5 November 2014.

56. Interviews, various taxation experts, Kigali, 2009–2015.

57. Musharraf R. Cyan, Canisius Karuranga, and François Vaillancourt, 'Local government revenue potential in Rwanda' (report by Georgia State University, Andrew Young School of Policy Studies, 2013).

58. Norregaard, 'Taxing immovable property'.

59. Tom Goodfellow, *State effectiveness and the politics of urban development in East Africa* (PhD Thesis, London School of Economics and Political Science, 2012).

property tax brought in less than a third of the amount generated by market fees or fees for public cleaning services, for example. It was also stagnant. Despite the problems involved in interpreting property tax revenue over time, evidence suggests that property tax reported zero growth in 2011–12 in 2011–12,<sup>60</sup> and even declined in 2012–13 after the tax rate was lowered.<sup>61</sup> This picture contrasts sharply with what was unfolding in the real estate sector. The property development taking place in Kigali over the past two decades led one expert to suggest in 2009 that in Rwanda property taxation could, hypothetically speaking, amount to as much as 5 percent of GDP.<sup>62</sup> In 2013, the amount of property tax collected nationally was just 0.018 percent of GDP.<sup>63</sup> This is extraordinarily low even by the standards of developing countries, a selection of which was found to average at 0.6 percent,<sup>64</sup> and African countries, for which the overall average is estimated at 0.5 percent.<sup>65</sup>

It is puzzling as to why such a development-oriented state, lauded for its tax reforms more generally,<sup>66</sup> has failed to significantly improve its system for property taxation. Accounting for this requires situating the property tax problematic in relation to the land lease system that was introduced in the context of Rwanda's land reform in 2004–5. The 2005 Organic Land Law denationalized land and introduced a two-tiered system, under which investors in urban land meeting certain specifications are entitled to freehold titles. Meanwhile all other landholders are granted an 'Emphyteutic lease' of 20–99 years, depending on land use, in exchange for paying a lease contract fee (based on plot size and location, and payable in annual installments) and committing to develop the land according to relevant land use conditions.<sup>67</sup> Leaseholders may convert their leases into freehold titles if they meet these conditions and pay the fee in full.<sup>68</sup> The crucial point here is that those with leasehold titles pay

60. Cyan *et al.*, 'Local government revenue potential in Rwanda', p. 54.

61. Interview, researcher, Kigali, 9 June 2014.

62. Interview, taxation adviser, Kigali, 26 November 2009. This is would be even higher than is typical for OECD countries, which average at around 2.1 percent of GDP (OECD library, data available at: [http://www.oecd-ilibrary.org/taxation/taxes-on-property\\_20758510-table7](http://www.oecd-ilibrary.org/taxation/taxes-on-property_20758510-table7), accessed 20 April 2015). Some countries do have significantly higher proportions, however, with the UK ranking the highest at 4.3 percent (*ibid*).

63. This is based on the amount of property tax collected in 2013 as a proportion of the 2013 GDP according to World Bank figures (available at: <http://data.worldbank.org/indicator/NY.GDP.MKTP.PP.CD>, accessed 20 April 2015).

64. Norregaard, 'Taxing immovable property'.

65. Fjeldstad and Heggstad, 'Local government revenue mobilisation'.

66. Odd-Helge Fjeldstad and Mick Moore, 'Revenue authorities and public authority in sub-Saharan Africa', *The Journal of Modern African Studies* 47, 1 (2009), pp. 1–18.

67. The state retains ultimate title on leasehold land.

68. Interview, government decentralization official, Kigali, 4 February 2010; Interview, land official, Kigali, 9 December 2011.

land lease fees, while holders of freehold properties, which constitute only 3 percent of land parcels in the country, pay property tax; the latter replaces the former once you have a freehold title.

This dual system was intended as a way of spurring planned development of every plot, while also ensuring a steady flow of revenue from land based on simple square-meter calculations, and increasing the number of landholders paying property tax over time. However, the system rests on the perception that freehold ownership is something desirable that people should (and do) aspire to. Enthusiasm among donors and foreign advisors for Hernando de Soto's ideas on formal property titling looms large here: the assumption is that people will want full title for the security it provides them over their land, and this will spur both development and the broadening of the property tax base.<sup>69</sup>

The experience so far in Kigali is not bearing this out. Land and housing officials in the city affirm that even those eligible to pick up freehold titles have often not done so, partly because if they did they would have to pay property tax, which may be significantly more than what they are paying in lease fees.<sup>70</sup> This was affirmed by other sources, including real estate brokers and a lawyer.<sup>71</sup> The result was a fiscal situation in which two identical properties could be paying very different amounts simply based on whether the landholder has or has not picked up a freehold title, with the latter paying a lease fee that effectively exempts structures on the land from any taxation whatsoever. Calculations suggest that many leaseholders are paying around a *fifth* in land lease fees of what a freeholder would pay in property tax on an identical plot, even with the very low property tax rate.<sup>72</sup> One observer commented that 'more or less only the people who are stupid enough to pay [property tax] pay'.<sup>73</sup> The supposed benefits of freehold ownership were not sufficient to incentivize most people to upgrade to freehold.

The benefits of freehold ownership are also not being articulated in a way that resonates locally. Part of the problem is that both the concepts of freehold and leasehold, and the supposedly significant distinction between them, are essentially foreign to the Rwandan context and contribute to the lack of public understanding about the differences between various local taxes and fees.<sup>74</sup> One long-term advisor on decentralized revenue confirmed that 'there is huge confusion over what is property tax and

69. Hernando De Soto, *The mystery of capital: Why capitalism triumphs in the West and fails everywhere else* (Basic Books, New York, 2000).

70. Interview, official, Kigali, 4 June 2014.

71. Interview, lawyer, Kigali, 2 June 2014; interview, property broker, Kigali, 5 June 2014.

72. Interview, RRA officials, Kigali, 4 June 2014.

73. Interview, taxation adviser, Kigali, 8 June 2014.

74. Interview, land and housing official, Kigali, 8 June 2014; interview, researcher, Kigali, 9 June 2014.

what is *Location Parcelle* [the land lease fee]'.<sup>75</sup> There are also widely diverging understandings of property tax among those who are supposed to administer it. In the words of one observer, 'not even the districts can tell the difference between property tax and [land lease fees] most of the time'.<sup>76</sup> Meanwhile, there is a common belief that leaseholders pay land lease fees, and freeholders who rent out should only pay rental income tax—another category of tax altogether based on actual rent received. In fact, all freeholders are supposed to pay property tax *regardless* of whether they rent the property out and also pay rental income tax. As far as many actors are concerned, property tax simply does not exist, despite apparently being central to the government's decentralization policy 15 years ago.

In addition to this confusion, there were missed opportunities with regard to how the DFID-funded Land Tenure Regularization Programme (LTRP) was conducted. From 2009, the LTRP process provided a window of opportunity to register properties for taxation: allocating land titles could be combined with identification of buildings on the land and even the gathering of data for the purposes of valuation.<sup>77</sup> The government, however, was concerned that people might be discouraged from participating in the LTRP if they knew it could lead to taxation,<sup>78</sup> so this did not happen. Consequently, the land registry contains no information on what is built on land; there was no cadastre of real property developed through the process that would facilitate 'switching on' a property tax at a later stage.<sup>79</sup> Rwanda is, therefore, in a situation where the majority of people pay lease fees based on square meters, which reflect nothing of the market value of land, cannot capture any value increment over time, and are finite, being payable in one lump sum or installments over 10 years. The irony is that once the plots are fully developed and of higher market value, owners can become freeholders and switch from a lease fee system to a property tax system that not only has extremely low rates but is effectively optional because enforcement is weak.

Many of these problems are resolvable, and the Rwanda Revenue Authority 'know they've dropped the ball on property tax',<sup>80</sup> recently bringing in the IMF and other experts to report on the situation. A clear priority is to expand the property tax base beyond freeholders, who are likely to remain a small minority. The question is whether political constraints will prevent this from being implemented, given the rapid accruing of real estate wealth in Rwanda that has thus far largely remained

75. Interview, former taxation official, 4 June 2014.

76. Interview, researcher, Kigali, 9 June 2014.

77. Interview, taxation adviser, Kigali, 26 November 2009.

78. Interview, government advisers, Kigali, 23 November 2009; interview, officials at the National Land Centre, Kigali, 3 December 2009.

79. Interview, city official, Kigali, 5 June 2014.

80. Interview, architect, Kigali, 3 June 2014.



untaxed, creating a powerful vested interest. The current system is regressive because while many large property owners pay virtually nothing, much of the revenue from land lease fees is garnered from small plots that would actually be exempt under an expanded property tax, being of little market value. The RPF government is very effective in raising revenues from the lower-income groups in society;<sup>81</sup> shifting over to a property tax for all urban plots would be a radical progressive move that partially reverses this trend, as it would mean high-value real estate paying far more tax while many ordinary city-dwellers might find themselves legitimately paying nothing. In Rwandan politics, where the elite coalition underpinning the RPF is fragile,<sup>82</sup> this could be a very risky move.

An aversion to disrupting what has thus far been a relatively untouched sphere of elite capital accumulation helps to explain the long history of 'passive resistance' to meaningful property tax in Rwanda,<sup>83</sup> which now dates back two decades. One advisor claimed he had first talked to the government about developing a functional system in 1997, and despite ministerial enthusiasm found no progress at all on the issue by 2003, and hardly any more by 2009.<sup>84</sup> Such inertia is uncharacteristic of Rwanda, which generally implements reforms fast. While the 2011 law could have been a turning point, it proved a false start for three reasons. First, instituting a market values-based system in a country with a nascent real estate profession, lacking in transparent transactions to form a basis for valuation, is highly problematic. In the words of one observer, 'nobody has any clue about market values'.<sup>85</sup> Second, the 2011 law did nothing to resolve the dichotomy between different kinds of payments on freehold and leasehold properties, which has severely constrained the tax base.

Third and most glaring was the slashing of the tax rate to 0.1 percent. According to close observers of developments in taxation, the draft version of the 2011 law had set the property tax rate at 0.5 percent, reflecting international norms, *and* had addressed the freehold/leasehold issue by making leasehold properties subject to property taxation.<sup>86</sup> Politicians in parliament revised both of these clauses before the law was passed, which if anything suggests a shift from 'passive' to more active resistance.

81. See Goodfellow, 'State effectiveness'.

82. For a discussion, see Pritish Behuria, 'Centralising rents and dispersing power while pursuing development? Exploring the strategic uses of military firms in Rwanda', *Review of African Political Economy* 43, 150 (2016), pp. 630–647.

83. Interview, taxation adviser, Kigali, 1 December 2009.

84. Interview, taxation adviser, Kigali, 26 November 2009.

85. Interview, construction sector specialist, Kigali, 15 January 2015.

86. Interviews, taxation specialists, Kigali, 6 and 8 June 2014. For further details on this and other aspects of property taxation and land leasing in Addis Ababa, see Goodfellow, 'Taxing the urban boom'.

Indeed, the fact that ‘property owners are often lawmakers’ is self-evident.<sup>87</sup> The interests in urban land, and degree to which this has caused large-scale expropriation of the urban poor, have been discussed elsewhere.<sup>88</sup> It seems clear that there is an enormous political hurdle to be overcome in Rwanda if the situation with regard to property taxation is to substantially improve.

*Addis Ababa: ‘people are already feeling taxed’*

Since the Ethiopian People’s Revolutionary Democratic Front (EPRDF) took power in 1991, Ethiopia has instituted a radical system of ‘ethnic federalism’, whereby the country is divided into nine federal states and two separately administered cities, Addis Ababa and Dire Dawa. This has important fiscal implications, set out in the 1994 Constitution. The governments of federal regions and cities possess powers to tax the incomes of employees within their regional state, as well as the profits of enterprises located within them and various other revenue sources usually collected centrally, including VAT. Thus, there are no transfers of revenue to Addis Ababa, unlike cities in decentralized systems or indeed most urban areas in Ethiopia, which acquire 70 percent of their resources in transfers from the regional states in which they are located. Addis Ababa collects all its own taxes.<sup>89</sup>

In addition to the taxes outlined above (known as ‘state taxes’), there are a series of municipal revenues collected locally. State taxes are collected by regional branches of the Ethiopian Revenue and Customs Authority, while municipal revenues are collected by the lowest rungs of local government (*woredas* or *kebeles*) as well as, in the cities, an intermediate tier of ‘sub-city’ government offices. Among these is a municipal tax known variously as ‘roof tax’ and ‘city house tax’—the equivalent of property tax.<sup>90</sup> This relates to buildings only. There is no single revenue instrument based on the combined value of land and buildings, but there was in the past. Property taxation in Ethiopia dates back to 1937 under the Italian occupation, and was based on annual market value (i.e. the amount that a property could yield in rent each year) rather than capital value.<sup>91</sup> After the socialist revolution in 1974, when land was nationalized,

87. Interview, Kigali, 3 June 2014.

88. Vincent Manirakiza, and An Ansoms, ‘Modernizing Kigali: The struggle for space in the Rwandan urban context’ in An Ansoms and Thea Hilhorst (eds), *Everyday forms of land grabbing in the Great Lakes region of Africa* (James Currey, Oxford, 2014); Goodfellow, ‘Rwanda’s political settlement and the urban transition’.

89. In 2014, the federal revenue authority was actually collecting taxes on behalf of the city authority, but this was supposed to be temporary and is beyond the scope of this article.

90. Hereafter where the term ‘property tax’ is used, this refers to the ‘roof tax’/‘city house tax’.

91. Interview, property taxation expert, Addis Ababa, 26 September 2014.

a new law split property tax into roof tax and land rent, as land itself was no longer taxable property but something rented from the state. In theory, the roof tax was still based on annual rental value, with rates ranging from 1 percent to 4.5 percent of annual value depending on a range of criteria.<sup>92</sup>

Soon after the EPRDF displaced the socialist Derg regime in 1991, they realized that the property valuation rolls being used for taxation were extremely out of date and only captured a fraction of the city's fast-growing housing stock. Consequently, a major census of properties in Addis Ababa was undertaken in 1996, using a computerized system and a team of 3,000 enumerators. Through this exercise, all properties (including informal structures) were identified and valued. This resulted in a new tax bill being presented to all property owners, indicating that they were currently paying only around a quarter of what they should be in property tax according to the recalculated values. This prompted such an outcry that the city government instructed the valuation team to slash the values to a quarter of what had been painstakingly calculated, rendering the whole exercise essentially pointless for properties already on the register.<sup>93</sup>

Since 1996, there has been no revaluation of properties in the city. Meanwhile, the population of Addis Ababa almost doubled from 1.8 million in 1990 to 3.2 million in 2014.<sup>94</sup> Even for houses on the register, severe undervaluation is the norm. One 2006 study of Lideta sub-city examined cases where properties listed on government valuation rolls had also been valued by banks, and found that on average the banks' valuations were 300 percent higher. For some properties, the banks' valuations differed by thousands of percent.<sup>95</sup> This disparity is likely to be even higher today. When new structures are built, property owners can get someone to come and value the property 'if they want to pay the tax'.<sup>96</sup> Evidently (and unsurprisingly) very few do. The general consensus was that most owners of privately owned houses 'pay nothing, because the government does not know them'.<sup>97</sup>

As a proportion of total city revenue (including all state revenue and municipal revenue), the contribution of the roof tax is just 0.1 percent. Even if we look at 'municipal revenues' only, which cumulatively

92. Ibid.

93. Ibid.

94. UN population division data, available at: <[http://esa.un.org/unpd/wup/wallcharts/WUP\\_2014\\_percent\\_percent20Urban\\_percent\\_percent20Agglomerations\\_percent\\_percent20Wallchart.pdf](http://esa.un.org/unpd/wup/wallcharts/WUP_2014_percent_percent20Urban_percent_percent20Agglomerations_percent_percent20Wallchart.pdf)> (13 May 2016).

95. Bacry Yusuf, Sileshi Tefera, and Admit Zerihun, *Land lease policy in Addis Ababa* (Private Sector Development Hub, Addis Ababa Chamber of Commerce, 2009), p. 60.

96. Interview, property taxation expert, Addis Ababa, 26 September 2014.

97. Interview, local researcher, Addis Ababa, 26 September 2014.

constitute only 5 percent of the city's budget (the vast majority being from 'state taxes'), the roof tax comprises just 1.65 percent of this.<sup>98</sup> Property tax is, therefore, a minuscule proportion of city revenue by any standards. Addis Ababa collects more revenue from 'engineering and asset estimation service fees' or 'fees for medical examinations' than it does from property taxation. The situation in the capital is also significantly worse than in some other federal regions, where regional governments have used their devolved powers to substantially increase roof tax rates. One source pointed out that 'I pay four times more property tax in Adama for a small house than I pay for my big house in Addis Ababa'.<sup>99</sup>

In short, despite the thorough efforts in the 1990s to register and revalue properties, property tax in Addis Ababa has been rendered 'almost non-existent' by interventions to deliberately undervalue properties, the lack of revaluation over time, and the failure to register properties constructed in the past two decades.<sup>100</sup> As well as privately built houses, this includes the mushrooming high-rise commercial developments throughout the city and over 100,000 condominium apartments built by the government over the past decade, which have proved lucrative revenue sources for many owners but have not been registered, let alone valued, as taxable assets.<sup>101</sup> The value created by the state's own property entrepreneurship is thus not being recaptured fiscally as it was in East Asia. In the words of one government official, the problem of property taxation in the city 'is untouched'.<sup>102</sup>

As in Rwanda, understanding how this relates to the land question is critical. Although relinquishing national ownership of land was unthinkable for the EPRDF when they came to power,<sup>103</sup> the regime found itself faced with a land use system that neither yielded much revenue nor provided the foundations for the rapid development it was determined to promote. Existing land use was governed by a permit system, in which the government would issue permits for people or organizations to use particular plots for indefinite periods in exchange for rent, which bore no relation to market value.<sup>104</sup> There was no formal mechanism for capturing the value of land. The new regime wanted to combine continued state land ownership with market-driven development, and soon began investigating the possibilities for a system of land leasing along the lines of what was happening in other countries transitioning from socialism.<sup>105</sup>

98. Figures acquired from various government agencies in Addis Ababa, September–October 2014.

99. Interview, official in international agency, Addis Ababa, 24 September 2014.

100. Interview, local researcher, Addis Ababa, 23 September 2014.

101. Interview, housing expert, Addis Ababa, 1 October 2014.

102. Interview, tax official, Addis Ababa, 23 September 2014.

103. Markakis, *Ethiopia*.

104. Interview, land expert, Addis Ababa, 4 October 2014.

105. *Ibid.*

Based on a series of study visits including several to China, a system was developed which provided for government to transfer rights over land for specified periods of time while retaining the ultimate title. Minimum benchmark prices per square meter of land were set, which would apply to certain kinds of favored development such as schools, manufacturing industry and the condominiums. Commercial developments would be expected to pay significantly more. Initially, the modality for establishing prices for commercial developments was exclusively through auction, with the benchmark as the starting price. Again following the example of China, however, a modality of ‘negotiation’ was introduced in 2002 alongside auctioning, though the basis for such negotiation was never entirely clear.<sup>106</sup>

Having to purchase leases resulted in radically increased costs for usage of urban land, which inevitably generated resistance to the new system. To ease its passage, the old permit system was maintained alongside the leasing framework; people already holding permits could continue to use their land in exchange for minimal rent, while the government worked towards conceiving a way to incorporate *all* land into the leasehold system. Meanwhile, the land leasing system resulted in highly erratic pricing. A study of 1,000 land transactions from 2002 to 2009 found that 96 percent of plots were leased through ‘negotiation’, with the remaining 4 percent split between allotment at benchmark prices and auctioning. According to the same report, land lease prices followed ‘neither logic nor theory, neither policy priorities nor grades, neither floor prices nor size of plots’.<sup>107</sup> The price per square meter for one plot of land within a given sub-city of Addis Ababa might be as much as 50 times higher than another plot in the same area. By this time, land leasing was already generating more than 20 times more revenue than property tax or any other fees relating to property.<sup>108</sup>

In 2011, a new government proclamation took the leasing system a step further through a controversial measure to incrementally incorporate all land into the leasing system.<sup>109</sup> This meant that whenever a plot held under the old permit system was sold, instead of the permit transferring as part of the sale (as had happened previously), the new landholder was required to take out a lease from the government at the benchmark price, which is updated every 2 years.<sup>110</sup> These measures contributed to an ongoing increase in local revenue garnered through land leasing. The

106. Yusuf *et al.*, *Land lease policy in Addis Ababa*.

107. *Ibid.*, pp. 105–106.

108. Figures acquired from various government agencies in Addis Ababa, September–October 2014.

109. Federal Democratic Republic of Ethiopia, *Land Lease Holding Proclamation* (No. 721/2011).

110. Leases in Addis Ababa are 99 years for residential housing, science and technology, research and study, government offices, charities; 70 years for industry; 60 years for commerce; and 15 years for urban agriculture (Article 18).

2011 proclamation also abolished the opaque modality of negotiation, making all commercial land leasing dependent on auction. The average price of leases sold through auction was always significantly higher than those sold through negotiation, so subjecting all commercial land purchases to compulsory bidding in monthly auctions paved the way for prices to rapidly escalate. By late 2014, some plots of land were selling for 65,000 Ethiopian Birr (ETB) in parts of the city,<sup>111</sup> and on 5 December, a plot of land in Addis Ketema sub-city was auctioned for ETB 307,000 per square meter—around \$15,500. This is higher than the average price for *developed real estate* in Geneva (\$15,250), the fifth most expensive city in the world for property.<sup>112</sup>

These soaring prices are clearly contributing to increased revenue for the city administration. They do, however, raise questions about the stability and sustainability of urban revenue over time, quite aside from the effects that this kind of land-based financing might have on displacement of the urban poor, the path to which is eased by new rules on government powers to ‘clear’ land in the 2011 Land Proclamation. As sources of government revenue, leases are fixed sums of money rather than continuous payments like taxes. They are also determined at a specific point in time and, therefore, do not change over time with market values of the land. In terms of revenue stability, sales may vary hugely from one year to the next, and urban land is ultimately finite. Moreover, land lease fees will not recapture any of the value of structures built on the land; for this, a real property tax is required.

As noted previously, despite clear evidence that the urban property market and construction sector are booming, the existing property tax (‘roof tax’) has remained stagnant. As in Rwanda, there are moves to address this issue and a growing awareness of the potential for property taxation. A major four-year study and pilot project supported by the Gates Foundation and the German development corporation, GIZ, is underway. Significantly, however, a strategic decision was made not to conduct the pilot in Addis Ababa, where it was felt that there was ‘too much politics, the land leasing system had just come in [and there would be] too much mayhem’.<sup>113</sup> The property tax project being developed is, therefore, going to be piloted instead in three secondary cities: Dire Dawa, Bahir Dar, and Mekelle.

While the thought and strategic planning going into this project are evident, the question is whether the government will actually ‘pull the

111. Various interviews, Addis Ababa, September–October 2014.

112. *Capital* (Ethiopia) ‘It’s official: Addis, one of the most expensive cities in the world’, 8 December 2014, <<http://capitalethiopia.com/2014/12/08/its-official-addis-one-of-the-most-expensive-cities-in-the-world/#.WSNialKZN0s>> (13 May 2016).

113. Interview, project adviser, Addis Ababa, 30 September 2014.

trigger' by rolling the project out after the pilot exercise, which ultimately means bringing it to Addis Ababa.<sup>114</sup> There are major political obstacles to doing so when, in the words of one source, people are 'already feeling taxed, due to the new land lease system'.<sup>115</sup> All who acquire new property find themselves now paying lease fees substantially higher than any nominal land rent they had paid previously, which makes the introduction of an effective property tax highly politically challenging. Moreover, when the lease fee system was introduced, explicit public announcements were made as part of the 'hard sell' that people *would not be taxed* on their property once they had paid for the lease.

There are reasons to think that the EPRDF may be more willing to follow through on reform than the RPF in Rwanda. Although massive real estate wealth has accrued in Addis, which is partly why the pilot exercise is avoiding the capital, the government has demonstrated its willingness to face down this sector by constraining access to finance and land for real estate, in contrast to the situation in Kigali. However, the politics of governing Addis Ababa is also colored by the history of sustained opposition to the EPRDF in the Ethiopian capital and the fear of urban uprising,<sup>116</sup> exacerbated since the state of emergency declared in 2016–17. While elite resistance is the most substantial obstacle in Kigali, in Addis there is also the question of how the wider population will respond to the imposition of a real property tax when many are used to paying miniscule amounts of roof tax. Such reforms would impact substantially on the growing urban middle classes living in housing a tier above the low-income and shack accommodation that would mostly be exempt. Unlike in Rwanda, courting the urban middle classes has been an important priority for the EPRDF, which is a driving factor behind major public projects such as the condominium housing and the Chinese-funded Addis Ababa light railway. Property tax would also impact very significantly on domestic and diaspora investors currently channeling capital into real estate. The latter category in particular already have a fractious relationship with government, and are too numerous and wealthy to ignore.<sup>117</sup>

### *Conclusion*

The failure of both Rwanda and Ethiopia to institute effective and progressive property taxes is linked to some of the crucial differences between these 'neo-developmental' states and their East Asian forebears. In the

114. Ibid.

115. Interview, taxation adviser, Addis Ababa, 30 September 2014.

116. See Aalen and Tronvoll, 'The end of democracy?'

117. Terrence Lyons, 'Conflict-generated diasporas and transnational politics in Ethiopia: Analysis', *Conflict, Security and Development* 7, 4 (2007), pp. 529–549.



East Asian cases, there was either no established landlord class to begin with (as in the city-states of Hong Kong and Singapore), or this class was crushed and turned into an industrialist class capable of driving forward structural transformation of the country.<sup>118</sup> Ethiopia and Rwanda share similar preconditions in that pre-existing landholding classes were largely destroyed through socialist revolution and post-genocide transition, respectively. Yet notwithstanding some progress in manufacturing in Ethiopia, the obstacles to transforming into industrial powerhouses are formidable, due to intense and ongoing competition from established low-wage manufacturing hubs in Asia as well as donor imperatives to liberalize their economies. This leads many elites towards the relatively much easier and more lucrative profits available in real estate, bolstered by the lack of effective taxes on property. Thus, a powerful class concerned to protect property rents now holds disproportionate influence relative to their forebears in East Asia at a similar stage of development, where the ascent of manufacturing provided broader scope for profitable investment and where robust land value capture mechanisms were already in place.

The precise nature of the problem differs significantly in the two countries. In Rwanda, the problematic freehold/leasehold divide in terms of property taxation may be on the way out, judging by a draft law at the time of writing. However, even if the removal of this distinction radically expands the tax base, the extremely low tax rate will be politically difficult to raise, and the administrative challenges remain overwhelming. In Ethiopia, there is a more solid technical base to build upon, but government ownership of land and the public relations challenge of introducing the tax on top of controversial lease fees remain major obstacles, in Addis Ababa particularly. In the meantime, the capital is transforming fast. Instituting real property taxation needs to happen before land for leasing (and the revenue that accompanies this) starts to run out, leading government to expropriate more land in potentially very socially regressive and politically explosive ways.

In both cases, land leasing is proving a much bigger revenue stream than property tax. But land leasing alone is not enough for states that need urgently to build viable urban economies and sustainable local government revenues, as it leaves untouched the structures built on properties and does not capture increments to value over time. It is also increasingly associated with the displacement of low-income communities and selling off of rights to the highest bidder, rather than generating revenue to provide services in the interests of the majority. Furthermore, it

118. Kay, 'Why East Asia overtook Latin America'; Castells, 'Four Asian tigers with a dragon's head'.

provides no disincentive to speculative property development that might also help to spur more productive investment elsewhere. The East Asian developmental states implemented a range of solid property-related taxes as well as land leasing. Their African aspiring counterparts would do well to take this lesson very seriously.