

# Calculating the Collection Efficiency and Cost to Collection Ratio



IMPROVING REAL PROPERTY TAX SYSTEM PERFORMANCE

Notes 3

Local Finance



*Knowing real property tax collection efficiency and the cost-to-collection ratio allows the LGU to formulate measures that will increase revenue collection and make RPT a major factor in LGU revenue generation.*

## Making Real Property Taxes Count

Real property tax is the single most important local source of provincial and municipal revenues. However, its income potential has not been fully exploited by local government units (LGU). One reason for this is that revenue targets are usually set as a fixed percentage of previous year's collections rather than setting targets based on the total potentially collectible taxes.

Many LGUs also fail to monitor uncollected taxes which have accumulated over time.

By looking at the collection efficiency ratio, they would have known the proportion of collected taxes to collectibles during the year, based on taxable assessed values of the LGU. It also gives the percentage of uncollected realty taxes during the year.

LGUs are also unaware how much is spent for every peso collected. LGUs in lower income classifications actually subsidize the cost of collecting taxes, sacrificing other priority projects like basic service delivery and infrastructure. If the situation persists, LGUs are better off not collecting real property tax.

Real property tax can make a great impact in increasing LGU revenues. Calculating collection efficiency and cost-to-collection ratios is the first step. Monitoring these ratios over time will give LGU officials the necessary information on the performance of real property tax collection in their LGUs. This information could then be used to formulate strategic and doable measures to increase revenue collection and enable LGUs to finance more projects that benefit the constituents.

*The Local Governance Technical Notes series is a publication of the Governance and Local Democracy (GOLD) Project made possible through support of the United States Agency for International Development (USAID) under the terms of the GOLD Project Contract No. 492-0471-C-00-5089-00. The series provides information on key processes and tools in local government management, service delivery, citizen participation, and policy issues. The opinions expressed herein do not necessarily reflect the views of USAID.*

Published in January 2001



# Technology

## Collection Efficiency Ratio

All other factors being equal, the collection efficiency (CE) ratio is one parameter LGUs may use to evaluate their tax administration and enforcement programs. As a performance indicator, it compares actual collections with what is supposed to be collected by LGUs.

Previously, LGUs computed their collection efficiency (CE<sub>1</sub>) by getting the ratio of actual total collections (current and previous years' taxes) and the BLGF-prescribed collection targets (see Formula 1.1). Under this formula, the ratio could range from zero to more than 100%, which many LGU officials find difficult to understand. In one of the sharing sessions of the League of Provinces, the BLGF agreed with the provincial governors

to use a new formula (see Formula 1.2) comparing current year tax collections vis-à-vis the potential current year tax collectible based on the total taxable assessed values of all properties in a particular taxing jurisdiction. (In addition, the BLGF has set a separate collection target for

delinquent taxes.) This would be used in lieu of the pre-determined collection target mandated by BLGF. The CE<sub>2</sub> ratio indicated in Formula 1.2 would range from zero to 100%. A ratio closer to 100% means better tax administration and enforcement performance by the LGU.

### Formula 1.1

$$CE_1 = \frac{\text{Actual Total Collections (Current and previous years' taxes including penalties)}}{\text{Total Target Collections (As determined by BLGF)}} \times 100$$

### Formula 1.2

$$CE_2 = \frac{\text{Actual Current Year Collections (Basic, SEF, plus discounts)}}{\text{Current Year Potential Collectibles (Based on total taxable assessed values)}} \times 100$$

## Cost-To-Collection Ratio

Another performance indicator is the cost-to-collection ratio (CCR). It measures how much the LGU spends for every peso of real property tax that goes to its coffers. If the ratio is more than one, the LGU is spending more than what it is getting as revenue from the real property tax. If the ratio is equal to one (1), it means that the LGU operation is break-even. With a ratio less than one (1), the real property tax is contributing to the revenue coffers of the LGU to augment the fi-

ancing of the cost of delivery of basic services and other local development projects.

To compute the municipal CCR, get the ratio of the Municipal Assessor's Office (MASSO) expenditures plus 20% of the Municipal Treasurer's Office (MTO) expenditures and the 40% share of the municipality from the basic real property tax collections (current and previous years' taxes including penalties). The same formula can be applied to compute the provincial

CCR using the expenditures of the Provincial Assessor's Office plus 20% of the Provincial Treasurer's Office expenditures and the 35% share of the province from the basic real property tax collections.

Several of the assumptions included in this formula are:

- Assessment cost covers the total expenditures of the Provincial or Municipal Assessor's Office. Only 20% of the expenditures of the Provincial or Municipal Treasurer's Office are conservatively allocated as collection cost of the real property tax. It represents the proportionate time or effort by the personnel of said offices to collect the said tax. The other 80% expenditures represent the cost of their other activities.
- The amount of basic tax collection in the denominator represents the amount that actually accrues to the coffers of the LGU concerned, i.e. 40% to the municipality and 35% to the province of the total basic tax collections (current year, previous years', and penalties).

### Formula for the Province

$$CCR = \frac{\text{Total Budgetary Cost of PASSO + 20\% of PTO expenditures}}{\text{35\% of Basic Tax Actual Collections (current, previous taxes, and penalties)}}$$

- PASSO – Provincial Assessor's Office; PTO – Provincial Treasurer's Office

### Formula for the Municipality

$$CCR = \frac{\text{Total Budgetary Cost of MASSO + 20\% of MTO expenditures}}{\text{40\% of Basic Tax Actual Collections (current, previous taxes, and penalties)}}$$

- MASSO – Municipal Assessor's Office; MTO – Municipal Treasurer's Office



# Policy and Practice

## Enabling Framework

The Local Government Code of 1991 (RA 7160) provides the overall framework for the administration, imposition, and collection of real property tax. Section 247 states that “the collection of real property tax with interest thereon... and the enforcement remedies provided shall be the responsibility of the city or municipal treasurers concerned.” To support its collection efforts, Title Five, art. 2 (5) of the Code mandates local treasurers to maintain and update the LGU tax information system.

Executive Order No. 127 dated October 1, 1987 of the Office of the President underscores the role of BLGF in

local financial management. Section 43 states that the DOF through the BLGF shall exercise administrative and technical supervision and coordination over the treasury and assessment operations of local governments. Further, the BLGF shall develop and promote plans and programs for the improvement of resource management systems and collection enforcement mechanisms at the local level. It will also provide “consultative services and technical assistance to LGUs on local taxation and real property assessment.”

In 1998, the Province of Nueva Vizcaya presented to other provinces

its RPTA experience under the GOLD Project during the sharing session of the League of Provinces in Clark, Pampanga. The ensuing discussion centered on the use of potential tax collectibles based on total taxable assessed values as a factor in the measurement of collection efficiency and to determine the LGU revenue target. In the end, the BLGF agreed to the proposal of the Provincial Governors to use the current potential tax collectibles instead of the BLGF-mandated collection target as basis for computing the collection efficiency.

## Practices That Are Working

The Province of Nueva Vizcaya was among the first LGUs to adopt the new formula to calculate collection efficiency using potential tax collectibles based on the total taxable assessed values in the province. The province and the six pilot municipalities computed their collection efficiency using both formulae— $CE_1$  and  $CE_2$ —and the results are shown in Table 1. As can be gleaned in Table 1, the province’ collection performance in 1997 was 131.46% using the BLGF-mandated  $CE_1$  formula. On the other hand, the  $CE_2$  formula indicated a more realistic figure at 45.24%. The same pattern can be observed in the 6 municipalities.

Calculating how much the municipality or the province spends for each peso of tax collected is not a usual practice for most LGUs. The Province of Nueva Vizcaya, however, wanted to know the cost-effectiveness of the real property tax system in the province and, initially, in the six pilot municipalities. As indicated in Table 2, the province spent P 1.34 to collect every peso of real property tax. The case of the six municipalities was even worse. The cost of collecting a peso ranged from P 2.19 for Bayombong to a high of P 10.29 for Kasibu.

Upon learning the true state of the real property tax system in their lo-

Table 2 Cost-to-Collection ratios, Nueva Vizcaya, 1997

LGU	CCR
Bambang	2.54
Bayombong	2.19
Diadi	5.86
Dupax del Sur	8.98
Kasibu	10.29
Solano	2.47
Province	1.34

Source: Nueva Vizcaya PTWG Report, 1998

cality as indicated in the above CE and CCR figures, provincial and municipal officials immediately undertook decisive actions to increase tax collection and reduce costs. These actions included mobilizing barangay officials, teachers, and DECS officials to assist in tax administration; increasing fair market values; and sending notices of delinquency to taxpayers. The province also delegated assessment functions to the six municipal assessors, reorganized the Provincial Assessor’s Office, and reduced the number of assessment forms used from nine to four.

Table 1 Comparative collection efficiency figures, Nueva Vizcaya

LGU	CE Ratio <sub>1</sub>	CE Ratio <sub>2</sub>
Bambang	118.09%	44.41%
Bayombong	125.38%	50.27%
Diadi	130.24%	43.38%
Dupax del Sur	140.02%	41.12%
Kasibu	108.86%	29.51%
Solano	170.54%	54.43%
Province	131.46%	45.24%

Source: Nueva Vizcaya PTWG Report, 1998



# LGU Action Agenda

## Other Initiatives

Aside from the province of Nueva Vizcaya, these formulae for collection efficiency and cost-to-collection ratios were also tested and used in the provinces of Capiz, Cotabato, Palawan, and Negros Oriental. LGUs who used to achieve over one hundred percent efficiency in collection were surprised to realize how low their actual efficiency was. In 1996, the province of Palawan had a collection efficiency of 190.77% based on BLGF-given targets. Using current year collectibles as basis for their calculation, they discovered that CE was only 54.70%. The Province of Capiz reported a collection efficiency of 76.07% in 1996 based on DOF targets. Based on actual current collectibles, however, the province achieved only 28.19% efficiency that showed a 47.88% difference.

The Province of Cotabato used to apply only the current year collection as the denominator for the provincial CCR calculations. From 1991 to 1996, the province was apparently failing in RPT administration since the formula showed that they spent an average of P 1.15 for every peso of realty tax collected. Using total collection that included the back taxes and penalties as the CCR denominator, the province reported an average CCR of 0.65 for the same year period. This meant that they earned P 0.35 per peso of realty tax collected in the entire province.

## What You Can Do

The collection efficiency (CE) and cost-to-collection ratio (CCR) measures LGU performance in administering and collecting its real property tax. In so doing, LGUs are given the idea of how much they spend for each peso collected and the level of their tax collection efficiency. Moreover, the exercise will also give LGUs the idea on how effective their tax collection strategies and tax information campaigns are. To do this, the following steps are useful.

1. Gather all the necessary data for the computation of CE and CCR. To compute the CE of the province or of the municipality, you will need the:
  - current year actual collections from basic tax and Special Education Fund Tax including discounts,
  - collectible taxes based on the previous year total assessed value.
2. In computing the CCR for a municipality you will need:
  - total budgetary cost of the Municipal Assessor's Office,
  - twenty percent of budgetary cost of the Municipal Treasurer's Office,
  - total collections (including penalties and previous years' collections).
3. For Cost-to-Collection Ratio in the province you will need:
  - total budgetary cost of the Provincial Assessors Office,
  - twenty percent of budgetary cost of Provincial Treasurer's Office,
  - total provincial collections (including penalties & previous years' collection).
4. Using the data gathered, calculate the CE and CCR.
5. Assess the results of the computation. If the results are not satisfying, or there is a noted decrease in the collection efficiency and increase in the cost-to-collection ratio, identify possible problems or bottlenecks.
6. Having identified possible problems, decide on the doable practical actions to be implemented to address the problems identified.
7. Given the level of spending, tax collection efficiency, the possible reasons and the doable measures or actions, LGUs are ready and now able to set realistic targets based on its current collectibles.
8. It is suggested that this activity be done regularly to monitor the performance of the real property tax system. An increase in collection efficiency or a decrease in cost-to-collection ratio means an improvement in performance.

## Resources and References

The provinces of Capiz, Cotabato, Nueva Vizcaya, Negros Oriental, Palawan and to some extent, Bulacan, are a few of the first LGUs that have used collection efficiency and cost -to-collection ratio as a measure to monitor the effectiveness of their real property tax administration. LGUs who wish to adopt the same approach may contact or solicit technical assistance from the following:

- Mr. Roque Barrios, Provincial Assessor's Office, Capiz, Tel. (036) 621-0033
- Mr. Corpuz Limpot, Provincial Assessor's Office, Amas, Kidapawan, Cotabato, Tel. (064) 288-1799
- Ms. Flory Sonjaco, Provincial Treasurer's Office, Dumaguete, Negros Oriental, Tel. (035) 225-1723
- Mr. Mario Creag, Provincial Assessor's Office, Puerto Princesa, Palawan, Tel. (048) 433-2571
- Mr. Manuel Reyes, Provincial Assessor's Office, Bayombong, Nueva Vizcaya, Tel. (078) 321-2713

The experience of Capiz, Cotabato, Nueva Vizcaya, and Palawan is documented in detail in the Technical Working Group (TWG) Reports available at the Provincial Treasurer's or Assessor's Office of these provinces.