St. Catharines | **Corporate Report**
**Budget Standing Committee**

**Report from** Financial Management Services, Billing

**Date of Report:** May 17,2018 **Date of Meeting:** May 23, 2018

**Report Number:** FMS-B025-2018 **File:** 10.57.1

**Subject:** Non-Residential Tax Capping Policy – Additional Information

# Recommendation

That the Budget Standing Committee (BSC) receives this report for consideration; and

That in the event BSC determines that tax capping policy in the Niagara Region requires further review for the 2019 taxation year; and

That BSC refer this report to City Council in order for a referral to Niagara Region Council for inclusion and consideration with the 2019 tax policy.

# Summary

MTE prepared a summarized policy review of the tax changes and tax mitigation strategies in relation the City's Downtown Business Improvement Area (DTBIA) properties. Their report "Qualitative Policy Review Mitigation of Reassessment Related Property Tax Shifts" is attached as Appendix 1.

In terms of layering mitigation programs, there are really no options that the City can utilize for 2018. Prevailing legislation does not permit City Council to alter the business tax capping program or implement a tax phase-in plan. Tax Policy (including tax capping) is the responsibility of the upper tier and would need to be addressed by Regional Council as part of the 2019 tax policy.

# Background

The BSC directed staff to prepare a report on the model adopted by Toronto that created a 10% cap on annual tax increases resulting from assessment increases and feasibility of implementing a similar system for downtown St. Catharines for 2019.

At the BSC meeting of April 16, 2018, the Mayor asked that report FMS-B012-2018 attached as Appendix 2, be referred back to staff for more information and to come back to the next BSC meeting of May 23, 2018.

# Report

City staff engaged Municipal Tax Equity Consultants (MTE) who work closely with municipal and provincial governments, to ensure that we are able to operate in a compliant manner within today's complex property tax and municipal finance environment to provide us with the legislative options necessary to identify and meet local tax policy.

It is documented that very limited impact would be realized if capping were to be re-introduced. In fact, that this would increase taxes for a number of DTBIA properties as a result of the claw-back portion of tax capping policy. Tax capping refers to limitations on annual property tax increases for certain commercial, industrial and multi-residential properties. Properties that have been subject to capping protection (meaning they have paid less than their CVA property taxes) will see an eventual loss on their capping protection. On the other hand, property owners that have been subject to a claw back of tax reductions (therefore paying more than CVA taxes or withholding part of a property's decrease due to reassessment) will realize these reductions and eventually pay their CVA property taxes.

MTE has included distribution/frequency tables showing the number of increasing and decreasing properties that demonstrate the incidence of high $ and/or high % increases is actually fairly limited.

Table 3 of Appendix 1 reports on the distribution of tax shift experienced in the DTBIA for 2018. As it can be seen in Table 3, only a small minority of properties are experiencing reassessment related tax changes in excess of 10% and the majority of these are expected to change at a rate of less than 15%.

The taxes for all commercial properties in the City of St Catharines would be approximately 0.35% higher in 2018, if the Region had not decreased the commercial tax ratio for 2018. The change shifted taxes off all the commercial properties and onto the remaining tax classes with residential carrying the majority of the shift.

# Financial Implications

There are no direct costs to the City as the capping protection for a property class is funded through a clawing back of tax reductions with the same class. There are tax payer impacts as a result of tax shifts between property classes due to assessment phase-in, assessment growth and tax ratios due to tax policy. The current tax capping system is administered by OPTA. If the Region of Niagara opts back into capping there would be system infrastructure and staffing requirements to manage the re-implemented capping program, as OPTA currently only administers the province wide capping program.

# Relationship to Strategic Plan

**GOAL:**

1. Be an affordable city for all.

Actions:

1.1 Update financial controls and the debt management strategy to better manage escalating costs of City operations and services

# Conclusion

With tax policy being the responsibility of the upper tier in a two-tier system, the City has no authority over its local capping program. Region of Niagara manages the tax capping program for the Region. For future years, the City could request Regional Council to re-implement a capping program for commercial properties, which would be a complete reversal of the policy direction taken by the Region over the past decade. The current approach will see capping eliminated entirely and strongly supported by the municipalities across the Region. Any other any mitigation options would require special legislation being pursued, which would take a long time and would likely come at a high cost. Any changes are not likely to be in time for current reassessment cycle.

# Notification

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# QUALITATIVE POLICY REVIEW
# MITIGATION OF REASSESSMENT RELATED PROPERTY TAX SHIFTS

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*Published On:*
**WEDNESDAY, MAY 16TH, 2018**

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The discussion and commentary contained in this report do not constitute legal advice or the provision of legal services as defined by the *Law Society Act,* any other Act, or Regulation. If legal advice is required or if legal rights are, or may be an issue, the reader must obtain an independent legal opinion.

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MTE is not responsible to the municipality, nor to any other party for damages arising based on incorrect data or due to the misuse of the information contained in this study, including without limitation, any related, indirect, special or consequential damages.

The results contained in this report should not be relied upon to make final tax policy or budgetary decisions for 2018 taxation. The assessment and taxation details contained herein must not be used as part of any aggregate, or property specific tax calculations for any taxation year.

Analysis contained in this report is based on the use of tax rates for general local municipal purposes only. Education tax rates have not been employed, and education levies are not included in any of the results.

## INTRODUCTION AND PURPOSE

Within the context of reviewing and managing the impacts related to the most recent reassessment, the City of St. Catharines has had reason to look closely at the changes being experienced by commercial properties within its Downtown Business Improvement Area (BIA). The interest in this specific sector of the assessment and tax base has been driven by the general perception that these properties experienced higher than typical rates of reassessment change and were facing higher than average reassessment related tax shifts.

The assistance of Municipal Tax Equity (MTE) Consultants Inc. has been enlisted to supplement the information available to staff and decision makers within the context of these discussions. Specifically, City Staff requested that we review the assessment and tax change circumstances of these properties and that we provide policy insight in regards to existing, optional and potential tax mitigation programs that have been discussed or suggested to date. This report has been prepared to satisfy this request and summarize our enquiry into this issue.

In approaching this mandate our efforts were organized into a number of distinct lines of enquiry and comments related to our preliminary findings and conclusions are set out along these lines below.

As an immediate first step we have considered the actual tax shifts related to the subject properties. We have also analysed the level of tax mitigation currently being provided by the assessment phase-in program, which is the primary reassessment stabilization mechanism under Ontario's current system.

This accomplished, we move on to a discussion and overview of the business tax capping system, its history and how it functions in general. We further look at how the Downtown BIA properties might be impacted under a modified capping program. We also provide a discussion related to the tax phase-in program set out under the *Municipal Act, 2001 (The Act),* which is an alternative to capping that is currently only available to implement at the upper-tier level.

In the last section of the report we discuss some subjective considerations and thoughts that the authors suggest are important in any discussion regarding the introduction or expansion of tax mitigation programs in general.

When considering this material it is important for the reader to be aware that the exercise at hand was intentionally set out to be a high-level review and consideration of tax policy and concepts, no efforts were made to consider the accuracy or appropriateness of any property specific assessments.

Finally, the following commentary should be taken as general in nature and nothing in this report is intended to be, or should be read as a legal opinion. This material is intended to support the discussion and consideration of the issues at hand and should be read and considered with this simple objective in mind.

## DOWNTOWN BIA COMMERCIAL PROPERTY TAX CHANGE PATTERNS

As noted above, general concerns have been identified in respect to the reassessment related tax shifts being experienced by some commercial properties within the Downtown BIA. Before discussing any the specific policy options or considerations surrounding tax mitigation schemes, it is important to establish a robust picture of the actual rates and incidence of the tax shifts being experienced. This is a critical step for a host of reasons but most importantly, we want to ensure that the discussion is informed by the actual circumstances. There is always a risk that a limited number of outlier circumstances are understood to be a broader, more common pattern than they actually are. That is, we want to know if there is actually a broad trend of extreme tax shifts, or are these more isolated, property specific occurrences.

In addition, it is also important to consider the nature of protection properties are already receiving via the assessment phase-in program, which is the default system that protects taxpayers from the volatility of reassessment and does act as an effective tax phase-in program.

### *Downtown BIA Tax Change*

There are approximately 240 properties (roll numbers) within the Downtown BIA that have assessment in the commercial tax class. These properties vary widely in size, value and nature with CVAs ranging from less than 50,000 to in excess of 30 million. The property tax they attract ranges from a few hundred dollars to over $500,000. Table 1 summarizes the distribution (frequency) of these properties across the assessment spectrum. These value ranges are based on full, non-phase adjusted CVA in order to facilitate a consistent basis for comparison.

**Table 1**
**Downtown BIA Commercial Property CVA Distribution**

| Full / Non Phased CVA | Frequency |
|---|---:|
| < 100,000 | 18 |
| 100,000 - 249,999 | 82 |
| 250,000 - 499,999 | 74 |
| 500,000 - 999,999 | 43 |
| 1,000,000 - 2,499,999 | 15 |
| 2,500,000 - 9,999,999 | 6 |
| 10,000,000 - 20,000,000 | 2 |
| > 20,000,000 | 1 |
| **Total Commercial BIA Rolls** | **241** |

What is clear in reviewing Table 1 is that the commercial property class within the Downtown BIA is not a homogeneous collection of properties. While the majority of properties range in assessed value from 100,000 to 1,000,000 this is a fairly large range itself and the outliers are quite spread out.

As the key factor here is not the property assessments, but the property tax and the rate, or magnitude of reassessment related shifts being experienced, we also looked at how the taxes for these properties are changing. In order to isolate the pure impact of reassessment change, independent from City or Regional levy changes, which are applied equally to all properties, we calculated the 2017 year-end general levies for City and Regional purposes as well as the

Provincial Education levy for each property. These year-end tax values were then compared to the 2018 revenue neutral levy amounts[1].

Table 2 shows the distribution of tax shifts in general municipal levy and education tax dollars, Table 3 reports on the distribution of percentage tax shift experienced by the commercial class properties in the Downtown BIA for 2018.

**Table 2**
**Distribution of Tax Shifts Measured in Revenue Neutral General Levy and Education Dollars**

| Tax Shift $ Ranges | | Frequency |
|---|---|---|
| Tax Decreases | > $2,500 | 1 |
| | $1,000 - $2,499 | 3 |
| | $500 - $999 | 4 |
| | $100 - $499 | 32 |
| | $0 - $99 | 37 |
| Tax Increases | $1 - $99 | 41 |
| | $100 - $499 | 75 |
| | $500 - $999 | 23 |
| | $1,000 - $2,499 | 14 |
| | $2,500 - $4,999 | 8 |
| | $5,000 - $9,999 | 2 |
| | > $10,000 | 1 |
| **Total Commercial BIA Rolls** | | **241** |

**Table 3**
**Distribution of Tax Shifts Measured in Percentage Change of Revenue Neutral General Levy and Education Tax**

| Tax Shift % Ranges | | Frequency |
|---|---|---|
| Tax Decreases | > 2.5% | 31 |
| | 1.00% - 2.49% | 20 |
| | 0% - 0.99% | 25 |
| Tax Increases | 0.01% - 0.99% | 29 |
| | 1.00% - 2.49% | 42 |
| | 2.50% - 4.99% | 37 |
| | 5.00% - 9.99% | 9 |
| | 10.00% - 14.99% | 32 |
| | 15.00% - 19.99% | 12 |
| | 20.00% - 24.99% | 2 |
| | > 25.00% | 2 |
| **Total Commercial BIA Rolls** | | **241** |

[1] The City's Urban Service Area rate, Regional waste rate nor any 2018 levy increases were utilized in this exercise.

As can be seen in Table 3, only a small minority of properties are experiencing reassessment related tax change in excess of 10% and the majority of these are expected to change at a rate of less than 15%.

It is also important for the reader to note that the taxes for all commercial properties in the City of St. Catharines would be approximately 0.35% higher than currently anticipated if the Region had not decreased the commercial tax ratio for 2018. This change shifted taxes off of all commercial properties and onto the remaining tax classes; residential carrying the majority of this shift.

***Assessment Phase-In Tax Mitigation***

Before looking at any supplementary tax mitigation schemes to deal with reassessment related tax change, it is critical to gain an understanding as to the outcomes of the mitigation program, namely the phase-in of assessment increases.

Where an increase in market value has materialized, the increase is added to the property's "Phased" CVA in twenty-five percent (25%) increments each year over the four-year period. As such, effected taxpayers will not be taxed on their new full market value until 2020, which is the last year of the new assessment cycle.

Assessment decreases are <u>not</u> phased-in. Where a property's CVA has been reduced as a result of reassessment, the new, lower CVA has been set as the property's phased or effective CVA for the duration of the four-year assessment cycle.

The phase-in is calculated and administered at the property portion, or RTC/RTQ level, which means that a property with multiple portions could have some portions that are increasing and some that are decreasing. The following has been prepared to illustrate how this works at the property and portion level.

| | | Market Value Update | | | Eligible Phase-In Amount | Phase-Adjusted Assessment | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | **1/1/2012** | | **1/1/2016** | | **2017** | **2018** | **2019** | **2020** |
| Property A | RT | 100,000 | ↑ | 140,000 | 40,000 | 110,000 | 120,000 | 130,000 | 140,000 |
| Property A | CT | 100,000 | ↓ | 80,000 | 0 | 80,000 | 80,000 | 80,000 | 80,000 |
| Property B | RT | 100,000 | → | 100,000 | 0 | 100,000 | 100,000 | 100,000 | 100,000 |

Although the assessment phase-in program does not place any specific limitations on the year-over-year tax change for individual properties, it does necessarily have consequences for final tax outcomes. The most obvious tax impact of the phase-in program is the benefit to increasing properties, which will not be taxed on their full CVA values until 2020. The tax implications for decreasing properties are not quite as direct, but they are material and measurable.

While there is no delay or phase-in of assessment decreases, the reduced availability of CVA against which to levy taxes in the first three years of a cycle results in the tax rates for those years being higher than would otherwise be the case if the phase-in did not exist. That is, if the full CVA for all properties were made available for 2018 taxation, and revenue requirements were held constant, the tax rates set would be lower.

Of the 241 commercial properties within the Downtown BIA, 52 will pay approximately $15,000 more tax in 2018 than they would if the assessment phase-in program did not exist and the remainder share in protection of over $165,000 on the general City and Regional levies alone.

The 11 properties identified with tax shifts in excess of $2,500 in Table 2 will realize a combined tax change protection of almost $80,000 this year. All tax protection amounts are funded by properties that experienced CVA decreases, or no change at all as a result of the latest reassessment. This funding is operationalized by the application of tax rates that are higher than they would otherwise be if increases were not being phased-in.

### BUSINESS TAX CAPPING

Central to this enquiry is the City's interest in understanding whether the re-introduction of business tax capping could be viable option for providing additional protection against reassessment related tax change for commercial properties. Specifically those perceived to be subject to higher than average rates of assessment change and tax shift. Before considering this on any level, the reader must be aware that the City has no authority to implement business tax capping. This authority rests with the Region and further, the commercial class is already subject to a business tax capping program, it simply doesn't capture any of the subject properties at this time. That said, we have prepared the following to explore this avenue of enquiry in greater detail.

#### *Historic Sketch*

Legislation creating the mandatory "10-5-5" tax capping program was originally presented as a transitional measure to provide temporary tax protection for the 1998 through 2000 tax cycles. In 2001, however, the Province introduced additional property tax reforms that served to reinforce the prescriptive nature of the property tax policy environment in Ontario. At this time, tax capping became a permanent feature of the property tax landscape as the original, temporary 10-5-5 program was replaced with a modified model known as the "5% limit on increases".

Beginning in 2005 a number of capping options were made available to single and upper-tier municipalities. This initial range of optional tools included the ability to increase the annual cap from 5% of the previous year's final capped taxes up to 10%, a second limit for annual increases of up to 5% of the previous year's annualized CVA taxes and dollar thresholds that moved properties with nominal capping adjustments directly to their CVA tax liability in any given year.

The 2009 taxation year represented another in a long series of reform and reassessment cycles. In addition to a number of fundamental changes to the assessment system, which included the introduction of a four-year reassessment cycle coupled with a program to phase-in assessment increases, the Province gave municipalities the option to begin permanently excluding individual properties from capping by utilizing "stay at CVA tax" and "cross-over CVA tax" tools.

For 2016 the Minister of Finance passed legislation that granted municipalities more local autonomy in respect of the business tax capping; including the ability for municipalities to opt-out of capping altogether if no properties remained eligible for protection. Where properties remained eligible for protection, new and expanded calculation parameter options and a phase-out program helped accelerate progress towards full CVA tax. These options were further enhanced and expanded as of the 2017 taxation year.

### *Trend to Eliminate Capping Programs*

The optional capping tools have been embraced by municipalities on an almost universal basis and the overwhelming majority of upper and single-tier municipalities, including Niagara Region, have applied a mix of tools that will bring the swiftest possible end to the capping program.

In addition to the administrative costs and encumbrances the program presents, it also creates natural inequities in the property tax system, which policy makers generally see as undesirable.

Under this system, two properties in the same municipality, assessed at the same value, can be subject to very different tax liabilities. While one may enjoy a large capping credit, the other could be forced to fund the cap with a tax liability in excess of what its CVA and prevailing tax rates would otherwise suggest. In another instance, one property may be eligible for capping protection, while another facing an identical assessment and CVA tax increase, might be excluded.

There are endless combinations and examples that could be provided, but the critical point is that the capping program creates inequities by distorting the tax liability of each property subject to an adjustment, which results in similar properties paying disparate taxes. Ultimately, this undermines the intention of the property tax system to treat similar properties in a similar manner by breaking the link between one's assessment, the tax rates and the final taxes owing.

### *Options to Re-Introduce Capping in St. Catharines*

The business tax capping program is structured by Part 9 of the *Municipal Act, 2001* and supporting regulations made under that *Act*. Municipal specific options and parameters are set by single and upper-tier jurisdictions only. As a local municipality within a Regional structure, the City of St. Catharines has no authority over its local capping program, what parameters are used and/or whether the capping will even apply once the Region is eligible to discontinue it for all classes. And, it seems inevitable that the Region will exit capping for the commercial and industrial classes at its earliest opportunity as it already has for the multi-residential property class.

The only option available to capture properties that are currently not subject to increase limits would be for the Region to remove the following tools from its current capping regime:

- Cross CVA Tax Exclusion;
- Stay at CVA Tax Exclusion;
- Flow-Through Current Cycle Increases; and
- Capping Phase-Out (currently in year 2 of 4)

The removal of these options from the commercial capping program would result in reassessment related tax increases in excess of 10% being capped. The eligible increase would only be that portion of a property's tax change that was directly related to the year-over-year phase-in change; municipal levy increases are not subject to capping and flow-through equally for all properties.

It is our understanding that the required by-laws have already been passed and that there is no opportunity to change the capping program for 2018, however, we have considered the hypothetical implications of re-introducing a 10% cap at both the Regional and local levels.

### *Regional Implications*

Preliminary indications suggest that for 2018 there will be two commercial properties subject to capping protection across the Region of Niagara and that the total cost of this protection will be approximately $5,500. If claw-back is used to fund this, which involves retaining a portion of

reassessment related tax decreases from other property owners, approximately 19 properties will share in this cost.

If the program was altered to provide capping protection to all properties with reassessment related tax increases in excess of 10%, the number of capping adjustments would increase to approximately 150 across the Region at a cost of over $525,000. This cost would be carried by about 1,900 other commercial taxpayers who would see a portion of anticipated tax decreases withheld.

Costs in terms of staff time and administrative resources would also increase significantly for all local municipalities in order to administer this volume of capping when taxes are levied and each time one of these 2,000 + accounts is subject to a change.

***Local Implications***

In the City of St. Catharines the re-institution of a 10% cap would provide protection to approximately 43 properties while moving almost 500 into a claw-back position. That is, the number of property owners who would pay more tax as a result of capping would be almost 10 times the number who would realize relief. This would be true whether the cap was introduced Region-wide as provided for under the *Act,* or just within the City, which is not currently allowed. In fact, if this program was isolated to the City the cost being carried locally by claw-back properties would increase as they would not benefit from the Regional claw-back pool.

It is also critical for the reader to note that the re-introduction of a 10% cap would only provide protection to 7 of the 238[2] commercial properties within the City's Downtown BIA that would be eligible for the capping program. The total capping protection for those 7 properties would be between $14,000 and $15,000 and it would not be distributed equally. Two of the properties would share in over $8,500, or 60% of the group's capping protection, three others would see relief ranging from $1,300 to $1,900 and the final two would be subject to adjustments of approximately $500 - $600.

In addition to this modest level of capping protection, Downtown BIA properties would also become eligible for claw-back. It is estimated that the re-introduction of a 10% cap would place about 23 Downtown BIA properties into a claw-back position, thereby increasing their net taxes over what they would be under the current capping policy.

## TAX PHASE-IN PROGRAM

In addition to the business tax capping program set out under Part 9, the *Municipal Act, 2001* does provide municipalities with the option to establish a stand-alone tax phase-in program in order to mitigate the impact of reassessment. This program, however, cannot be implemented by a local municipality in a two-tier jurisdiction; subsection 318(1) of the *Act* expressly prohibits lower-tier municipalities from passing a tax phase-in by-law. Further, the Minister of Finance has no regulatory authority to convey special permission to a lower-tier municipality under this program. If the City was interested in implementing such a program locally, a special legislative amendment would have to be passed by the Province. It is not inconceivable that such permission might be granted, however, it would take a great deal of time and effort and it could be years before the *Act* was amended.

[2] Three commercial properties within the BIA are PILs that are not subject to Part 9 of *The Act.*

This program was introduced as part of the broad based reforms for the 1998 taxation year and was used by a very limited number of municipalities but was almost completely abandoned by 2001. Unlike capping, which is based on on-going year-over-year change limits, the amount of any increase or decrease to be phased in is calculated as of final billing in the first year of the program and the adjustments are mapped out for each year of the program at that time. This allows the municipality to estimate the total cost of the phase-in program up front, which in turn allow for the calculation of the tax decrease phase-ins (claw-back) that will be required to fund the credits being granted.

The formula for calculating eligible amounts is set out under the *Act* and the phase-in can run for up to seven (7) years. This would be an extraordinarily long period of time and the example below provides an illustration as to how this program would work if a three year phase-in were to be established to address the 2018 reassessment change for four hypothetical properties, two increasing and two decreasing. As can be seen below, the two increasing properties are going up by a total of $2,400 and the other two properties are seeing a combined tax decrease of $3,000. As the eligible increases only represent 80% of the anticipated decreases, we only phase-in 80% of the decreases. If this was not done, the phase-in would produce a surplus.

| Phase-In Calculation Element | Increasing Properties | | | Decreasing Properties | | |
|---|---|---|---|---|---|---|
| | A | B | Total | C | D | Total |
| Base Year Taxes | $5,000 | $10,000 | $15,000 | $10,000 | $7,000 | $17,000 |
| Subject Year Taxes | $5,900 | $11,500 | $17,400 | $8,000 | $6,000 | $14,700 |
| Tax Change | $900 | $1,500 | $2,400 | -$2,100 | -$1,200 | -$3,000 |
| Eligible Phase-In Amount | $900 | $1,500 | $2,400 | -$1,600 | -$800 | -$2,400 |
| | | | | | | |
| Y-1 Phase-In Adjustment | -$600 | -$1,000 | -$1,600 | $1,056 | $528 | $1,584 |
| Y-2 Phase-In Adjustment | -$300 | -$500 | -$800 | $528 | $264 | $792 |
| Y-3 Phase-In Adjustment | $0 | $0 | $0 | $0 | $0 | $0 |

All property specific phase-in credits and adjustments need to be calculated at the onset of the program and are based on that year's reassessment change. This listing must, however, be maintained throughout the term of the phase-in program and updated as property assessments and/or circumstances change. This is a very time and labour intensive exercise and often proves very confusing for the taxpayer; particularly those who are seeing additional charges added to their annual bill to fund the protection.

The level of complication and confusion will increase dramatically if a municipality were to add a phase-in for a subsequent taxation year. This program was designed for the initial 1998 transition to CVA assessment and mitigation of annual reassessment increases was not contemplated. If a municipality wanted to phase-in tax change for 2018, 2019 and 2020, they would essentially start a new phase-in program each year. The following is an illustration of how this would work if the taxes for our hypothetical Property A continued to increase by $900 each year.

| Taxation Year | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|
| Base Year Taxes | $5,000 | $5,900 | $6,800 | $7,700 |
| Subject Year Taxes | $5,900 | $6,800 | $7,700 | $7,700 |
| Eligible Phase-In Amount | $900 | $900 | $900 | $0 |
| | | | | |
| 2018 Phase-In Adjustment | -$600 | -$300 | $0 | $0 |
| 2019 Phase-In Adjustment | $0 | -$600 | -$300 | $0 |
| 2020 Phase-In Adjustment | $0 | $0 | -$600 | -$300 |
| **Final Taxes** | **$5,300** | **$5,900** | **$6,800** | **$8,300** |

As can be seen, this would be a very cumbersome program if utilized on an ongoing basis. Further, there are no existing resources or infrastructure to manage a program of this nature. For a city the size of St. Catharines it would be necessary to either build a purpose designed system to calculate, manage, adjust and track all phase-in data or outsource it. MTE has managed phase-in programs in the past and could be available to do this, but we suggest it would be cost prohibitive. Annual costs to implement a phase-in of this nature for the commercial class could be in excess of $50,000 annually and additional upfront costs are not unlikely.

## EQUITY CONSIDERATIONS WITH TAX MITIGATION PROGRAMS

One of the central tenets of Ontario's property assessment and taxation system is that all properties are revalued as of a uniform valuation date, and that similar properties are to be assessed in a similar manner across the entire Province. While tax rates do fluctuate by jurisdiction and property class, the overall structure of the system is intended to ensure that properties that are similar in nature, value and use carry a similar portion of the overall tax burden.

Our current system was also conceived out of a need to keep these values up-to-date so that the most recent, or current distribution of property wealth was reflected in the distribution of the property tax burden. Simply put, the objective of consistent and current assessments is to facilitate the distribution of taxes based on how property owners' holdings are performing in the market. This is the basis of a progressive property tax system and is not really any different than how a person's income tax increases in response to a raise in salary.

Some may argue that property taxes increase even when salaries do not, but that is irrelevant as property taxes are levied against property, not one's income. In the same way a person's income tax does not increase if their home appreciates in value; there is no connection.

This in mind, policy makers must be cognizant of the fact that any tax mitigation scheme, which serves to limit the assessment to tax connection necessarily detracts from the progressiveness of the property tax system. When we cap taxes, phase-in assessment, or phase-in tax increases someone's proportionate share to the tax burden is reduced and someone else's is increased, or at the very least their anticipated decrease is withheld or lessened.

This is true of all the mitigation programs outlined above, the most dramatic being business tax capping. Under this program there are property tax payers that have been paying taxes in excess of their assessment X rate for two decades. This is paramount to telling someone that even though they lost 10% of their income, they are still going to have to pay the same amount of taxes because we want to increase taxes gradually for their colleague who just received a 10% raise. While this seems to take the discussion into the realm of the absurd, that is ultimately what

we do when we cap or phase-in tax change. We convey a benefit to those whose capital is performing the best in the market we are taxing at the expense of those who are not doing as well in that market.

There are endless combinations and examples and illustration that could be provided, but the critical point is that capping and other tax mitigation programs create inequities by distorting the tax liability of each property subject to an adjustment. Quite simply we end up with similar properties paying disparate taxes.

The authors acknowledge the subjectivity of this portion of the report and it is not intended to ascribe or dictate perspectives or views not shared with the reader. Rather, these comments and thoughts have been included to suggest some of the questions and themes that should be discussed within the context of considering additional mitigation programs.

## GENERAL SUMMARY AND FINAL COMMENTS

As set out in the introduction to this report, the primary goal herein was to present the reader with a broader context for considering the tax changes of concern and the policy options that have been brought up within the related discussions.

While there are clearly some outlier tax changes occurring among commercial properties in the City's Downtown BIA, we would suggest that they may not be a dramatic, or at least as pervasive and they may appear at first glance. This is borne out by the frequency review in the first section of this report, but also in the limited impact that the re-introduction of capping would have on that particular pool of properties. This said, we again acknowledge that defining what is an extreme, significant, modest or acceptable tax shift is necessarily a subjective exercise.

In terms of layering on mitigation programs, there really are no options that the City of St. Catharines can utilize for 2018. Prevailing legislation does not permit City Council to alter the business tax capping program or implement a tax phase-in plan. The reader should also note that direct assistance or subsidizing of the taxes for the subject properties, or compensatory support of any nature would almost certainly be prohibited under the anti-bonusing provisions of section 106 of the *Municipal Act, 2001.*

On a go-forward the City may consider asking Regional Council to re-implement a more robust capping program for the commercial class but this would represent a complete reversal of the policy direction the Region has taken in regards to capping over the past decade or so. Further, it is our understanding that the current approach that will see capping eliminated entirely is strongly supported by the local municipalities across the Region.

It is conceivable that special legislation could be pursued with the Province, however, any such effort would likely take a long time and the City should not expect that rules would be changed in time to address concerns related to the current reassessment cycle.

St. Catharines | Corporate Report
Budget Standing Committee





**Report from** Financial Management Services, Billing

**Date of Report:** March 28, 2018 **Date of Meeting:** April 16, 2018

**Report Number:** FMS-B012-2018 **File:** 10.57.1

**Subject:** Non-Residential Tax Capping Policy

# Recommendation

That the Budget Standing Committee (BSC) receives this report for consideration; and
That in the event BSC determines tax capping policy in the Niagara Region requires further review for 2019 taxation year;
That BSC refer this report to City Council in order for a referral to Niagara Region Council for inclusion and consideration with 2019 tax policy.

# Summary

The City of St. Catharines, as a lower tier municipality in a two-tier system does not have the authority to institute tax capping policy changes. It is the responsibility of the upper-tier, Niagara Region. A tax policy change requires the support of majority of Niagara municipalities and is the decision of Niagara Regional Council.

As the 2018 tax policy has been approved by the Region's Corporate Services Committee at its meeting of April 4, 2018. It is schedule for consideration by Niagara Regional Council on April 12, 2018. Therefore, any changes to tax capping would be part of 2019 tax policy and a decision of Regional Council.

# Background

The BSC has directed staff to prepare a report on the model adopted by Toronto that created a 10% cap on annual property tax increases resulting from assessment increases and feasibility of implementing a similar system for downtown St Catharines for 2019.

Tax capping refers to the practice of prescribing a maximum allowable limit on year-over-year increases in property taxes. Originally intended as a temporary transitional measure to mitigate large property tax increases arising from the introduction of the Current Value Assessment (CVA) system.

In 1998, the Province of Ontario introduced the Tax Capping program to protect commercial, industrial, and multi-residential properties from significant property tax increases. Capping, limits land owners from paying the full amount of taxes based on

the assessed value of the property as they are paying less tax than if they calculate their taxes using the general formula. To address the tax increase, limits were placed on the amounts by which taxes could increase each year. When properties experience a decline in property value, this would ordinarily lead to a decrease in property tax. However, the capping program uses a "claw back" to fund revenue shortfall resulting from the capping limits by withholding some or all of the reduction to property owners. These reductions result in net winners and losers properties and municipalities across the Region as the intent of the capping program is to be revenue neutral. As shown in the chart below.

| Municipality | Total Impact of Capping Program (since 2001) |
|---|---:|
| Fort Erie | ($864,241) |
| Grimsby | $887,505 |
| Lincoln | ($729,771) |
| Niagara Falls | $31,351,664 |
| Niagara-On-The-Lake | $8,621,158 |
| Niagara Region | ($68,648) |
| Pelham | ($1,179,312) |
| Port Colborne | ($2,736,148) |
| St. Catharines | ($20,292,473) |
| Thorold | ($3,547,906) |
| Wainfleet | ($50,368) |
| Welland | ($10,599,360) |
| West Lincoln | ($792,100) |
| Total of All Non-Residential Classes | **$0** |

In the chart above the negative amount represents the municipalities that paid funds to the Region to be distributed to the municipalities with a positive amount. Therefore Grimsby, Niagara-On-The-Lake and Niagara Falls received capping funds through the Region and the other ten municipalities providing the funds to the Region. As shown, Niagara Falls was the largest recipient of funds of $31.4M, with St. Catharines being the largest contributor of funds at $20.3M.

The system was originally intended to last 3 years, with increases on these classes limited to 10% in 1998,15% in 1999 and 20% in 2000 and was referred to as “10:5:5”. Twenty years later, the tax capping program in Niagara continues, although the number of properties impacted has shrunk significantly.

Tax capping has proven to be an effective tool to mitigate large tax increases, and the rules surrounding capping and claw-back are now generally well understood. The negative consequences of tax capping/claw-backs are that inequities in taxation are preserved and prolonged. Owners whose properties have experienced large increases

in assessment continue to pay less than their full share of taxes (i.e., the taxes that would be payable if the taxes were based on full CVA times the tax rate), at the expense of owners whose properties would otherwise be entitled to a tax decrease.

The 2017 province-wide reassessment saw many business properties face significant tax increases. The increase can be expected to continue in each year from 2018 to 2020 as assessments continue to be phased in over a 4-year reassessment cycle. Many properties, having reached their full CVA value of taxation in a prior year were no longer eligible for capping protection against assessment related tax increases.

In 2015, the Province announced new options and changes to the existing capping and clawback program that municipalities would be able to consider in 2016. The more significant changes that have been made to the program since its inception provide municipalities with options to move properties more quickly towards “uncapped” status. The mandatory 5% base increase requirement remains in place but municipalities have the authority to increase the rate to 10%. As well, to increase the dollar threshold increase and decrease limits to up to $500 respectively. Perhaps most important, municipalities are provided with the option of keeping properties out of capping and clawback once they reach the “uncapped” tax point. This option has significantly reduced the number of properties that continue to be subject to capping and clawbacks.

These changes also allow municipalities (if eligible) to increase the prior year current value assessment capping limit from five per cent to 10 per cent. Regional Council having the responsibility for tax policy has approved the utilization of the new options available which includes opting to phase-out the capping program for eligible property classes over four years. Region continues strategies to exit the capping program. For 2018, the commercial class has 3 capped properties and 12 clawed back properties, total dollars $10,100 and the industrial class 1 property capped and 1 clawed back, total $816.

## Report

The Municipal Act provides upper tier municipalities the responsibility to establish tax policy to raise levy requirements however these are reviewed and discussed with local area treasurers. The Municipal Act (Act) requires a municipality, other than a lower–tier municipality to pass a by-law for tax policy.

Over the years tax policies have included provisions to accelerate progress towards full CVA taxation, as a means of restoring equity and simplicity in taxation. This included a requirement that a property, on having reached full CVA taxation levels, would no longer be eligible for capping or claw-back adjustments in subsequent years. This policy saw a gradual but steady increase in the number of properties paying taxes at full CVA levels and a reduction in the number of properties subject to capping/claw-back.

## City of Toronto Model

The City of Toronto for its 2018 tax policy adopted measures to provide a level of protection against unmitigated increases as an interim strategy while continuing to evaluate other tax policy options that will accelerate progress towards full CVA taxation.

The following property tax capping polices were approved for the 2018 taxation year, to:

a) limit tax increases for the commercial, industrial, and multi-residential property classes by capping taxes at 10% of the preceding year's annualized taxes, through the adoption of subsection 292(1), paragraph 1, of the *City of Toronto Act, 2006,* for the 2018 taxation year;

b) discontinue the policy of removing properties from the capping and claw-back system once they have reached their full CVA-level of taxation, by not adopting section 7.1 of Ontario Regulation 121/07 for the 2018 taxation year, such that the above capping limit apply for the 2018 tax year to any property that has experienced a property tax increase of greater than 10% over 2017 annualized taxes, regardless of whether the property had reached its full CVA-level of taxation in a prior year;

2. City Council direct the Acting Chief Financial Officer to review any additional tax options during 2018, including any potential requests for legislative change, for consideration for 2019 and future years.

The approved tax policy limits tax assessment related increases to 10% in the commercial, industrial and multi-residential class across the City of Toronto for the 2018 taxation year and they are not specific to one area of the City or one class. The tax capping program is generally revenue neutral and requires all properties within the municipality or class participation in the program. The recommended limits on tax increases will be funded by tax decreases which would be otherwise be applied to each class.

**Current Assessment Appeal Process Available**

If a property owner disagrees with MPAC's assessment or classification of their property, they can file a Request for Reconsideration (RfR) and they will review their assessment, free of charge. Deadlines to file as RfR with MPAC are printed on their Property Assessment Notice. Business properties are not required to file an RfR before filing an appeal with the Assessment Review Board.

# Financial Implications

There are no financial implications that arise from the capping protection in a property class as it is funded through a claw back of tax reductions within the same class. Under the capping and clawback system the foregone revenue resulting from the legislated limit on individual properties current value assessment (CVA) related tax increases for properties in the commercial, industrial and multi residential tax class are funded by withholding (clawback) a portion of the tax decreases that would have otherwise be applied to other properties with in each class.

# Relationship to Strategic Plan

**GOAL:**

**1.** Be an affordable city for young people, families and retired older adults.

Actions:

1.1. Update financial controls and debt management strategy to better manage escalating costs of City operations and services.

# Conclusion

The City of St Catharines is not permitted under the Municipal Act to set tax policy. In a in a two – tier municipalities, it is the responsibility of the upper tier. Therefore the decision on tax policy rests with the Niagara Region. As these tax policy decisions could have a significant impact to all the Area Municipalities, a fulsome discussion and review of the impacts and costs to all municipalities of this tax policy change is recommended prior to changes being implemented.

# Notification

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