TORONTO

STAFF REPORT
ACTION REQUIRED

Supplementary Report - Municipal Land Transfer Tax Reduction Options

Date:	December 30, 2013
To:	Budget Committee
From:	Deputy City Manager and Chief Financial Officer
Wards:	All
Reference Number:	P:\2014\Internal Services\Cf\Bc14001Cf (AFS #18749)

SUMMARY

This supplementary report builds on the report from the City Manager and the Deputy City Manager and Chief Financial Officer to the July 3, 2013 Executive Committee EX33.28 titled "Municipal Land Transfer Tax Reduction Options" which was referred to the Budget Committee to be dealt with as part of the 2014 budget process. That report contained potential options for capping, reducing (by 10%), or eliminating the City's Municipal Land transfer Tax (MLTT) over four years. This report focuses on the more moderate option for reducing the tax by 10% or less.

The preliminary 2014 budget for net Municipal Land Transfer Tax (MLTT) revenue is $335 million, based on 2014 net revenue of $350 million matching the projected 2013 net actual revenue, and incorporating an offsetting $15 million buffer provision for the risk of housing market slowdown. The budget figure does not take any potential rate changes into account. A 10% reduction on its own would reduce revenue by an estimated $35 million, equivalent to a 1.5% residential property tax increase.

The MLTT has been an important City revenue since its 2008 implementation, and has grown to generate almost 10% funding for the net tax-supported operating budget. To replace it entirely with property tax would require a 15% increase in the residential property tax. City Council has recently approved, as one of the strategic actions for 2013-2018 under the Fiscal Sustainability theme, the expansion of the City's revenue base including revenues that grow with the economy as part of the long-term fiscal plan. Reducing the MLTT revenue would be inconsistent with that strategic action, and is therefore not recommended.

RECOMMENDATIONS

The Deputy City Manager and Chief Financial Officer recommend that:

1. This report be received for information.

Financial Impact

There is no financial impact resulting from the adoption of this report. The net revenue losses associated with various rate changes and other adjustments to the MLTT are illustrated within this report.

DECISION HISTORY

On July 3, 2013 The Executive Committee considered the June 18, 2013 report from the City Manager and the Deputy City Manager and the Chief Financial Officer EX33.28 titled "Municipal Land Transfer Tax Reduction Options", and referred the report to the Budget Committee to be dealt with as part of the 2014 budget process.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2013.EX33.28

On October 8, 2013 City Council adopted the City Manager's report EX34.5 titled "Advancing Council's Strategic Plan – Strategic Actions for 2013-2018", including adding a new Strategic Action to the Fiscal Sustainability theme – Expansion of the City's revenue base including revenues that grow with the economy as part of the long-term fiscal plan.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2013.EX34.5

ISSUE BACKGROUND

Municipal Land Transfer Tax was introduced in 2008 in Toronto following the enactment of the *City of Toronto Act, 2006*. The tax expanded and diversified the City's revenue base. The tax revenue has grown at an average annual rate of almost 20% as the number of grandfathered transactions has diminished, and market volumes and prices associated with residential and commercial real estate transactions in Toronto have increased.

First-time homebuyers (FTHB) typically make up about one-third of all transactions. The City's FTHB rebate has grown to be worth between $50 million and $60 million annually, and applies to virtually all residential purchases of less than $400,000, and many above this value.

Some advocacy and interest groups have been calling for the reduction or elimination of the MLTT claiming it is unfair and makes our city less affordable. While no taxes are perfect, the reduction or elimination of MLTT should be considered in terms of the alternatives: an expenditure cut of up to 10% of the net operating budget, or residential property tax increase of up to 15% (along with a non-residential property tax increase of 5%). Either of these options would also impact fairness and affordability.

The potential advantages of MLTT over a comparable increase in property tax include:

1. The MLTT is triggered by a voluntary transaction at an agreed upon price that is by its nature somewhat means-tested, unlike the property tax which is mandatory and based on assessment;
2. MLTT may be more progressive due to the tiered tax rate, the first-time homebuyer rebate, and its only indirect impact on renters (almost half the city's households);
3. MLTT tends to grow with the economy like a sales tax, consistent with Council's Strategic Action revenue diversification objectives, unlike property tax which grows less than 1% per year without Council approved rate increases.

These attributes may have influenced Council's decision at its October 8, 2013 meeting to adopt a new Strategic Action to expand the City's revenue base including revenues that grow with the economy.

As identified in Table 1 of the June 18 staff report to the July 3 Executive Committee, the City's tiered MLTT tax rate structure is similar to the provincial LTT structure, although some City rates are lower. The City's tax rates are:

- 0.5% for the first $55,000 of consideration (purchase price);
- 1% for consideration from $55,000 to $250,000;
- 1% from $250,000 to $400,000 (provincial rate is 1.5%);
- 2% (residential[1]) / 1.5% (non-residential[2]) above $400,000;
- (non-residential only) 1% for the portion of the purchase price over $40 million (provincial rate is 1.5%)

The City's tax also provides a rebate for first-time homebuyers – rebating all the tax on the first $400,000 of consideration up to $3,725. The provincial LTT first-time home buyer rebate is lower and limited to the first $227,500 of consideration, a maximum of $2,000.

2013 MLTT Revenues:
For the first nine months of 2013, total net MLTT collected was $264.0 million, a positive variance of $25.4 million (or 10.7%). For October 2013, sales transactions in the city were up by 19% compared with October 2012, with strong growth in almost all sectors except semi-detached houses. Average residential resale price in the city has increased to $594,000 in October 2013, up by 10% compared with October 2012. A strengthening residential resale market compared to the same period in 2012 suggests that the 2013 variance will continue to grow through to year end. As a result, the current year-end net MLTT revenue forecast is $350.0 million, up from the previous figure of $340.0 million.

[1] A residential property is a property containing at least one, and not more than two, single family residences

[2] All other properties not falling under the above definition of the residential class

Table 1 summarizes the MLTT revenues since its inception in February 2008:

TABLE 1
Net MLTT revenue since implementation
Net Revenue ($ Million)

		2008	2009	2010	2011	2012	2013 Q3 YTD	2013
Budget		155.0	160.0	170.0	220.0	288.0	238.6	315.0
Actual		154.9	178.5	274.5	319.2	344.5	264.0	350.0*
Variance	**Amount**	-0.1	18.5	104.5	99.2	56.5	25.4	35.0*
	%	-0%	11%	61%	45%	20%	11%	11%

* projected year-end

Preliminary 2014 Budget:
The preliminary 2014 budget is currently $335.0 million, which represents a repeat of projected 2013 results, less a $15.0 million buffer or market risk provision. The real estate market can be subject to significant swings in volumes and prices, and under-achieving the budget would directly affect the City's annual surplus, and potentially the following year's budget. Previous MLTT budgets had been set at 10% below the prior-year actual. A smaller discount vs. prior year actuals ($15 million is approximately 4%) is now considered appropriate as the Federal mortgage rule tightening in mid 2012 has been absorbed by the market, and interest rates are expected to be relatively stable over the next 12 to18 months. A net budget of $335.0 million represents 6% growth over the 2013 budget, which is consistent with a moderate long-term growth estimate for the tax revenue.

The 2014 budget launch occurred November 25th. The preliminary budget is based on the current MLTT rates and policies continuing through 2014.

COMMENTS

In July 2013, Executive Committee referred EX33.28 (a report identifying certain tax reduction scenarios) to the Budget Committee for consideration as part of the 2014 budget process. The report identified options to reduce the MLTT in a number of ways, including implementing a cap, increasing the first-time homebuyers rebate, phasing the tax out over four years, and reducing the tax by 10%. Appendix A contains updated tax change scenario Tables 7 and 8 as reported in EX33.28.

The July report emphasized that reducing MLTT rates would impact the 2014 operating budget. It also suggested that the tax impact could be mitigated, or the tax reduction deeper, if applied only to the 'residential' transactions (as defined within the collection system as two units or less), and combined with changes to the first-time homebuyer rebate to bring it more in line with the provincial rebate. The report illustrated how reductions could best be implemented, by reducing or eliminating the rates starting at the bottom price tiers. The July report also discussed the City's agreement with the Province to share administrative information of the Province's compliance audits on the land registry system. Staff are currently processing the information and may report back if there are implications for the effectiveness and appropriateness of the City's current rebate levels.

This supplementary report focuses on the more moderate of these options, i.e. reducing the net tax revenues by 10%, 5% or 0%, combined with adjustments to the first-time home buyer (FTHB) rebate. Staff have updated the scenarios in accordance with the 2014 projected revenues of $350.0 million (i.e. before the $15 million provision for market risk), and where the FTHB rebate is harmonized with the provincial rebate.

1. $35 million (10% revenue cut) Budget Impact Option:

If Council elects to implement a 10% ($35 million) tax revenue reduction, the suggested approach would be to apply the rate cuts only to one- and two-unit residential purchases, work from the lowest tax tier up, and combine the rate changes with harmonization of the FTHB rebate with the provincial rebate (i.e. a maximum of $2,000). This option reduces the residential tax so that it does not reach $2,000 until the transaction price reaches $415,250. Consequently, the maximum fully rebated first-time home buyer transaction actually increases, from $400,000 to $415,250. All other residential purchases benefit from a lower tax rate, as shown in Table 2 below.

TABLE 2
Impact of a 10% ($35 million) revenue reduction on a $400,000 residential purchase

	Net MLTT payable/transaction		
	Current $0 - $55,000 = 0.5% $55,000 - $250,000 = 1%	**Reduced rates [3] & FTHB rebate harmonization** $0 - $55,000 = 0% $55,000 - $250,000 = 0.1%	**Change**
First-time homebuyers	Nil	Nil	**Nil**
Non first-time homebuyers	$3,725	$1,695	**-$2,030**

2. $17 million (5% revenue cut) Budget Impact Option:

If Council elects to implement a 5% ($17 million) tax revenue reduction, the suggested approach would be the same as for a 10% reduction. This option reduces the residential tax so that it does not reach $2,000 until the transaction price reaches $358,350. Consequently, the maximum fully rebated first-time home buyer transaction decreases, from $400,000 to $358,350, and many first-time homebuyers would be exposed to a slightly higher tax (up to $417 more). All other residential purchases benefit from a lower tax rate, as shown in Table 3 below.

[3] Only reduced rates (on one-to two-unit residential properties) are shown. Other rates remain unchanged.

TABLE 3
Impact of a 5% ($17 million) revenue reduction on a $400,000 residential purchase

	Net MLTT payable/transaction		
	Current	**Reduced rates [3] & FTHB rebate harmonization**	**Change**
	$0 - $55,000 = 0.5% $55,000 - $250,000 = 1%	$0 - $55,000 = 0% $55,000 - $250,000 = 0.47%	
First-time homebuyers	Nil	$417	**$417**
Non first-time homebuyers	$3,725	$2,417	**-$1,309**

3. Zero Budget Impact Rate Reduction Option:

Rates can be lowered with no budget impact if the first-time homebuyer rebate is harmonized with the Provincial rebate. Based on the 2014 forecast, residential rates can be reduced by almost 6% with no budget impact. The revenue loss from rate reduction (about $13 million) would be offset by an equal amount of revenue gain from lowering the maximum FTHB rebate from $3,725 to $2,000. The maximum MLTT free purchase price available to a first-time home buyer would be reduced to $303,750 (from $400,000), and first-time homebuyers could pay up to $963 more in MLTT. All other purchasers benefit from the lower tax rates, as shown in Table 4.

TABLE 4
Impact of zero budget impact rate reduction on a $400,000 residential purchase

	Net MLTT payable/transaction		
	Current	**Reduced rates [4] & FTHB rebate harmonization**	**Change**
	$0 - $55,000 = 0.5% $55,000 - $250,000 = 1%	$0 - $55,000 = 0% $55,000 - $250,000 = 0.75%	
First-time homebuyers	Nil	$963	**+$963**
Non first-time homebuyers	$3,725	$2,963	**-$762**

CONCLUSION

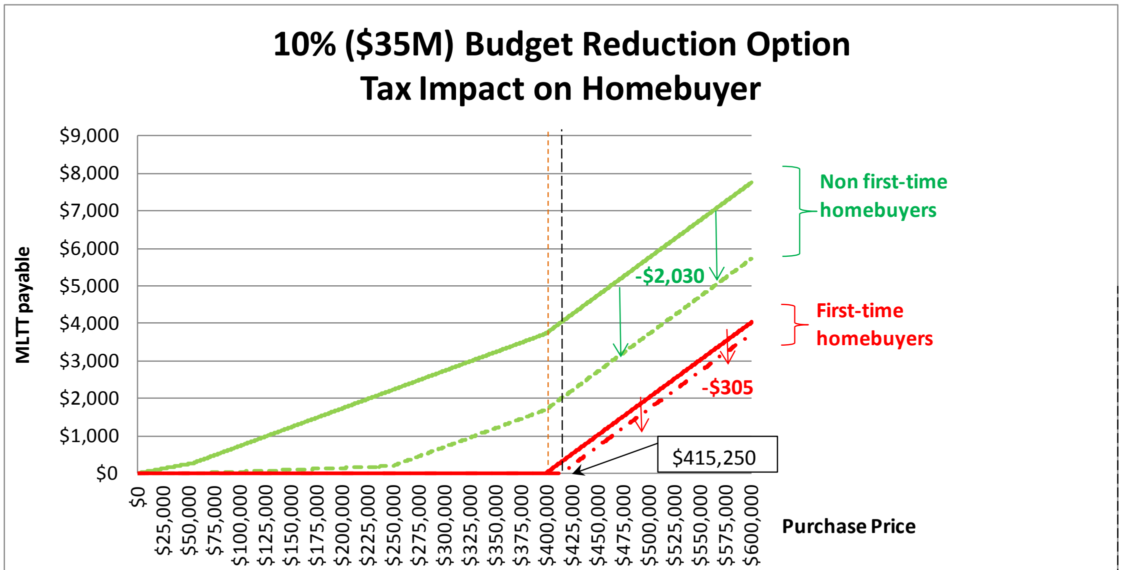
If Council elects to reduce the MLTT, reducing the tax rates only for residential transactions while harmonizing the FTHB rebate with the Provincial rebate would be the suggested approach as it permits deeper broad based rate cuts that partially offset the impact on first-time homebuyers. This report illustrates changes costing from $0 (a 6% residential cut combined with a reduction in the first time home buyer rebate to $2,000) to $35 million (a 10% over-all revenue cut, with concurrent changes to the first-time home buyer rebate). Table 5 summarizes the various options:

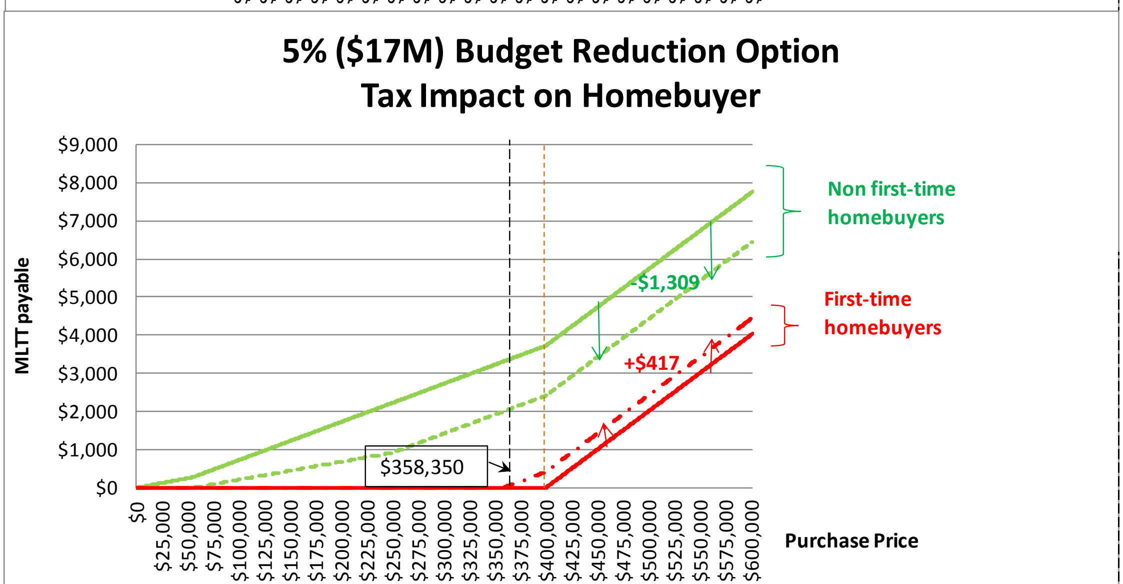
[4] Only reduced rates (on one-to two-unit residential properties) are shown. Other rates remain unchanged.

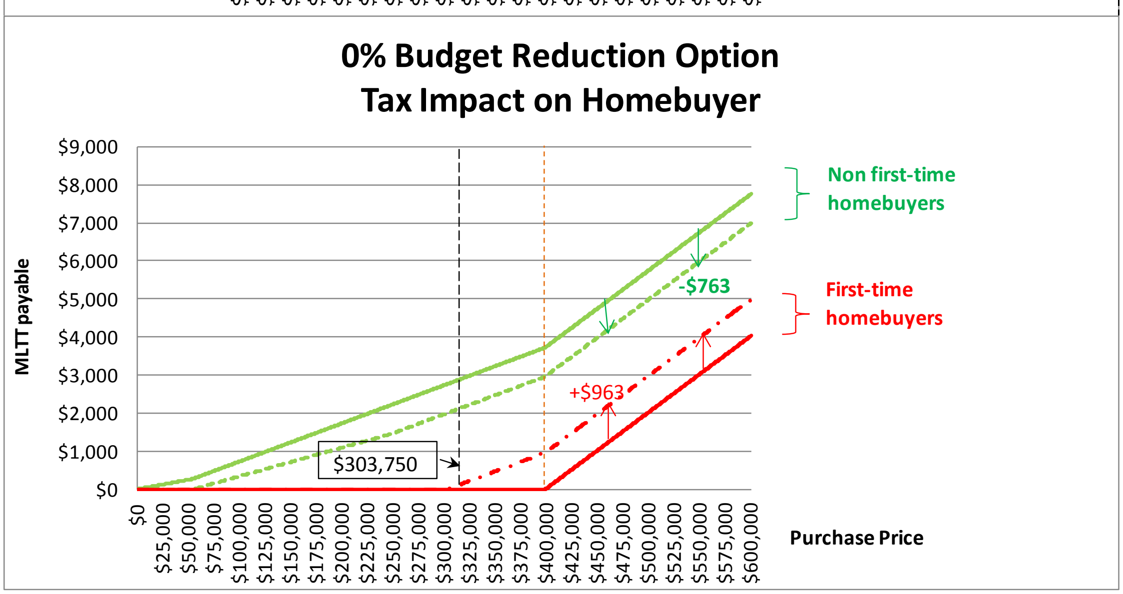
TABLE 5
Summary of Rate Reduction Options (for residential only)

Options	City Budget impact	Rates on purchase price[4]		Maximum no tax price	Impact on a $400,000 home purchase	
		$0 - $55,000	$55,000 - $250,000		First-time homebuyer	Non first-time homebuyer
Current	*n/a*	*0.5%*	*1.0%*	*$400,000*	*n/a*	*n/a*
1 – "10%"	($35M)	0.0%	0.1%	$415,250	nil	($2,030)
2 – "5%"	($17M)	0.0%	0.47%	$358,350	+$417	($1,309)
3 – "0%"	zero	0.0%	0.75%	$303,750	+$963	($763)

The following chart depicts the MLTT payable by homebuyers as a function of the purchase price under the three options discussed above.


10% ($35M) Budget Reduction Option
Tax Impact on Homebuyer
MLTT payable
$9,000
$8,000
$7,000
$6,000
$5,000
$4,000
$3,000
$2,000
$1,000
$0
Non first-time homebuyers
First-time homebuyers
-$2,030
-$305
$415,250
Purchase Price


5% ($17M) Budget Reduction Option
Tax Impact on Homebuyer
MLTT payable
Non first-time homebuyers
First-time homebuyers
-$1,309
+$417
$358,350
Purchase Price


0% Budget Reduction Option
Tax Impact on Homebuyer
MLTT payable
Non first-time homebuyers
First-time homebuyers
-$763
+$963
$303,750
Purchase Price

City Council has recently adopted the Strategic Actions for 2013-2018 associated with Council's Strategic Plan, including a new one on the "expansion of the City's revenue base including revenues that grow with the economy as part of the long-term fiscal plan". Reducing the MLTT revenue would be inconsistent with that strategic action, and represent a direct 2014 operating budget pressure. Therefore change that impacts revenue is not recommended. A revenue neutral change as illustrated above could achieve better alignment of the City's rebate program with the provincial system, and could be considered within the Strategic Plan objectives.

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SIGNATURE

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Deputy City Manager and Chief Financial Officer

ATTACHMENT

Appendix A – Updated MLTT Rate Reduction Scenarios

Appendix A

Updated MLTT Rate Reduction Scenarios

The following tables are the updated Tables 7 and 8 of the report (June 18, 2013) from the City Manager and Deputy City Manager and the Chief Financial Officer EX33.28 considered by the Executive Committee on July 3, 2013, in accordance with the preliminary 2014 revenue forecast based on the most recent actual data.

Updated Table 7

Residential		**Tax Rate Reduction Scenarios**				
Tax Rate Reduction Scenarios	***Current***	**1**	**2**	**3**	**4**	**5**
≤$55K	*0.5%*	0.0%	0.0%	0.0%	0.0%	0.0%
$55K- $250K	*1.0%*	1.0%	0.5%	0.0%	0.0%	0.0%
$250K - $400K	*1.0%*	1.0%	1.0%	1.0%	0.5%	0.0%
>$400K	*2.0%*	2.0%	2.0%	2.0%	2.0%	2.0%

Incremental Revenue Impacts (+/-)	**Scenarios**				
A Continue FTHB rebate	**1A**	**2A**	**3A**	**4A**	**5A**
Net revenue impact (+/-$M)	**(6)**	**(25)**	**(43)**	**(69)**	**(94)**
Net impact as % of projected 2014 revenue	*-2%*	*-7%*	*-12%*	*-20%*	*-27%*

	Scenarios				
B Harmonize FTHB rebate with Provincial rebate *	**1B**	**2B**	**3B**	**4B**	**5B**
Net revenue impact (+/-$M)	**10**	**(16)**	**(37)**	**(53)**	**(67)**
Net impact as % of projected 2014 revenue	*3%*	*-5%*	*-11%*	*-15%*	*-19%*

* Scenarios B in the June report show eliminating the FTHB rebate

Updated Table 8

Non-Residential		**Tax Rate Reduction Scenarios**				
Tax Rate Reduction Scenarios	***Current***	**1**	**2**	**3**	**4**	**5**
≤$55K	*0.5%*	0.0%	0.0%	0.0%	0.0%	0.0%
$55K- $250K	*1.0%*	1.0%	0.5%	0.0%	0.0%	0.0%
$250K - $400K	*1.0%*	1.0%	1.0%	1.0%	0.5%	0.0%
$400K - $40M	*1.5%*	1.5%	1.5%	1.5%	1.5%	1.5%
>$40M	*2.0%*	1.0%	1.0%	1.0%	1.0%	1.0%
Incremental Revenue Impacts (+/-$M)		**(4)**	**(18)**	**(31)**	**(36)**	**(40)**
Net impact as % of projected 2014 revenue		*-1%*	*-5%*	*-9%*	*-10%*	*-12%*