TORONTO

REPORT FOR ACTION

Future of the City's Vacant Commercial and Industrial Tax Rebate Program

Date: May 5, 2017
To: Executive Committee
From: Treasurer and General Manager, Economic Development & Culture
Wards: All

SUMMARY

In 2016, the Ontario Ministry of Finance, as part of the Special Purpose Business Property Assessment Review (SPBPAR), conducted consultations on possible amendments to the *Municipal Act/City of Toronto Act* provisions surrounding vacancy rebates, both with a municipal reference group and a business reference group (commercial/industrial property owners and advocacy groups).

On November 14, 2016, the Province released its Fall Economic Statement that provided additional tax policy flexibility to municipalities. Municipalities may now tailor their business property tax programs such as the Vacant Commercial and Industrial Unit Rebate (VUR) and Vacant/Excess land subclass tax reductions to meet local municipal objectives.

On February 15, 2017, Toronto City Council adopted Motion 313. The motion proclaims Council's intention to request the Minister of Finance to allow the City to reduce the allowable rebate percentage for the vacant unit rebate program for commercial and industrial properties by 50%, effective July 2017 and to eliminate the program entirely in 2018. Motion 313 also directed staff to report back on possible re-investment opportunities. The Province requires municipalities to engage in consultations and to obtain a Council resolution before changes to the vacant unit rebate program are approved.

This report responds to the direction of City Council to eliminate the Vacant Unit Rebate (VUR) program and includes the findings of the stakeholder consultations undertaken by the City in accordance with Provincial requirements.

RECOMMENDATIONS

The Treasurer and General Manager, Economic Development & Culture recommends that:

1. City Council request that the Province of Ontario adopt regulations and make any other legislative amendments required to adjust the vacancy rebate program as follows:

    a. For the period January 1 to June 30, 2017, the applicable rebate percentage for qualifying vacancies be set at 30 per cent for properties in any of the commercial tax classes, and 35 per cent for properties in any of the industrial tax classes;

    b. For the period July 1, 2017 to June 30, 2018, the applicable rebate percentage for qualifying vacancies be set at 15 per cent for properties in any of the commercial tax classes, and 35 per cent for properties in any of the industrial tax classes; and

    c. Effective July 1, 2018, the vacancy rebate program for commercial and industrial properties be discontinued.

    d. That the Minister of Finance prescribe a deadline date of February 28, 2018 for receipt of applications for vacancies occurring in 2017, and a deadline date of September 28, 2018 for receipt of applications for vacancies occurring in 2018.

2. City Council approve that, for the 2018 taxation year, the final municipal tax rates for the industrial classes be reduced by an amount equivalent to half of the estimated municipal portion of industrial taxes to be rebated under the vacant unit program for 2017, with the other half to be reduced in 2019.

3. City Council request that the Province of Ontario, in setting Toronto's education rates for 2018, reduce the commercial and industrial education tax rates by the estimated amount of the education portion of rebates that would have otherwise been rebated within each of the commercial and industrial property tax classes respectively, or alternatively, that these amounts be directed to the City of Toronto for reinvestment in accordance with Recommendations 5 and 6 of this report.

4. City Council authorize the Treasurer to forward this report and the recommendations adopted by Council to the Ontario Minister of Finance and to provide any additional information required to clarify the intent of the adoption of recommendations 1 and 3.

5. City Council request that the General Manager, Economic Development & Culture, report back within the context of the 2018 budget process on proposals that would see a portion of the reduction in rebate expenditures reinvested in programs or initiatives designed to stimulate economic growth and job creation by enhancing local retail areas that are challenged by high vacancy rates.

6. Council request the Deputy City Manager & Chief Financial Officer report within the context of the 2018 budget process on a plan to reinvest the remainder of the reduction in rebate expenditures, in programs or initiatives that support Toronto's poverty reduction strategy and to balance the tax-supported budget.

7. City Council request the Treasurer and the General Manager, Economic Development & Culture to report to the Budget Committee on the financial and other implications of changes to the tax rates for the Commercial and Industrial Vacant Land and Excess Land Subclasses as part of the 2018 budget process.

8. City Council authorize the introduction of any necessary by-laws to give effect to the foregoing.

FINANCIAL IMPACT

Reducing the allowable rebate for commercial properties by half for 2017 with an effective date of July 1, 2017 would result in reductions in Non-Program expenditures of approximately $5 million.

Eliminating the program in its entirety for future years would result in additional reduced rebate expenditures to the City of approximately $18.0 million per year. The net impact of $15.7 million from the elimination of the vacancy rebate program in 2018 (after reduction for the industrial impact of $1 million, which will be offset by a reduction of industrial taxes) will be reinvested in poverty reduction programs, economic development for depressed retail areas, and tax relief in 2018 and future years. Actual allocations will be addressed during the 2018 budget process. Full year impacts of $21 million net will be reflected in various budgets in 2019 as determined.

An additional reduction in annual operating expenditures of approximately $1 million annually is forecast for 2020 (one year after elimination of the vacant unit rebate) within the budget of the Office of the Treasurer (Revenue Services), attributable to reductions in staff, administration and contract costs associated with eliminating the vacancy rebate program. These expenditure savings will be reported in the Office of the Treasurer (Revenue Services) 2020 Operating Budget.

The Deputy City Manager & Chief Financial Officer has reviewed this report and agrees with the financial impact information.

DECISION HISTORY

At various times since 2011, City Council has requested staff to investigate the feasibility of redesigning the Vacant Unit Rebate Program (VUR) to stimulate economic development activities and to meet with provincial officials to discuss possible changes to the vacant rebate provisions in the City of Toronto Act (COTA) including:

http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2011.MM10.10
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2013.ED19.4

http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2014.ED30.6
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2015.EX7.2
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2015.EX8.1
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2015.ED8.5

At its meeting of April 16, 2014, the Economic Development Committee adopted, with amendments, a staff report from the General Manager, Economic Development & Culture dated March 28, 2014, as Item ED30.6: Re-designing the Vacant Commercial and Industrial Tax Relief Program to Stimulate Economic Growth (Collaborating for Competitiveness, Implementation Action 8). The Committee's decision is available at:

http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2014.ED30.6

During its consideration of this item, the Committee requested, among other things, that the General Manager, Economic Development & Culture submit a report to the May 6, 2014 meeting of City Council on a breakdown of vacancy rebate amounts paid by commercial vs. industrial and by geographic area.

At its June 22, 2016 meeting, the Economic Development Committee directed a letter from Councillor Davis to the General Manager Economic Development & Culture Division requesting that:

> The Deputy City Manager and Chief Financial Officer and the General Manager, Economic Development & Culture report to the September 19, 2016 meeting of the Economic Development Committee with an update on the Provincial Review of the Vacant Unit Rebate policy and the status of the working group.

http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2016.ED13.10

On September 30, 2016, Mayor Tory sent a letter to the Minister of Finance expressing the City's interest in redesigning the Vacant Unit Rebate Program. This letter requested that the City be permitted to "…vary the rate and conditions of the Vacant Unit Rebate Program, up to and including the ability to opt out of the provincial program entirely."

On November 14, 2016, the Province released its Fall Economic Statement . Additional flexibility is now available to municipalities in managing business property tax issues (p.178). The full report can be read online:

Building Ontario Up for Everyone: 2016 Ontario Economic Outlook and Fiscal Review

In the Province's Fall Economic Statement (Chapter V: A Fair and Sustainable Tax System), the provincial government stated:

"The Province is providing additional flexibility to enable municipalities to better tailor property tax programs to reflect their local needs and circumstances, while ensuring the property tax system continues to remain fair and competitive…"

At its meeting of February 15, 2017, City Council adopted Item EX22.2: 2017 Capital and Operating Budgets, which contained the following Motion:

313. With respect to the Vacancy Rebate Program, City Council:

a) request the Minister of Finance by regulation, to allow the City to reduce the allowable rebate percentage for vacant commercial and industrial properties under the program by half for 2017 effective July 1, 2017, and to eliminate the program in its entirety for future years; and

b) subject to receiving the necessary regulation, request the Deputy City Manager and Chief Financial Officer to report back on the proposed design, re-investment priorities based on Council's previously approved motions, timing, implementation requirements and any by-laws as may be required, as soon as practical.

Link to Item EX22.2: 2017 Capital and Operating Budgets:
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2017.EX22.2

ISSUE BACKGROUND

Introduced in 2001, the Property Tax Rebate Program for Vacant Commercial and Industrial Buildings provides property tax relief to owners of vacant commercial and industrial buildings. This program is currently mandatory, and is governed by Ontario Regulation 121/07 and Section 331 of the *City of Toronto Act, 2006*.

The vacancy rebate program provides a rebate of property taxes levied for eligible vacant space within commercial and industrial buildings. The rebate percentage is 30% of the property taxes levied for eligible vacant space within commercial buildings, and 35% for industrial buildings, as set out in the *City of Toronto Act, 2006*. Eligibility criteria and other program requirements for the vacancy rebate program are available at:

http://www1.toronto.ca/wps/portal/contentonly?vgnextoid=df25ff0e43db1410VgnVCM10000071d60f89RCRD&vgnextchannel=63b0ff0e43db1410VgnVCM10000071d60f89RCRD&vgnextfmt=default

Revenue Services staff administer the Property Tax Rebate Program for Vacant Commercial and Industrial Buildings. Property owners have the choice to apply annually or bi-annually to receive this rebate. The application form identifies those portions of the commercial or industrial building that meet the eligibility criteria, including a requirement that the space must have been continuously vacant because it is unused, undergoing repairs and renovation, or unfit for occupation for a minimum period of 90 days or longer during the year.

Attachment 1 to this report provides a summary of vacant commercial and industrial unit information from program inception in 2001 to 2015. Attachment 1, Table 1 identifies that the total rebates (municipal and education portions) paid each year since 2001 range between $28 and $38 million, with the exception of taxation years 2014 and 2015, as rebates continue to be actively processed for these years. Rebates payable in 2014 and 2015 are expected to exceed $40 million once all rebates have been processed for those years.

With 15 years of actual rebate data, i.e., from 2001 to 2015, it is possible to provide a high level overview of the amount of City rebates paid annually, the breakdown of property types receiving the rebates and a geographic overview of the VUR.

- The City pays approximately $45 million annually in Vacant Unit Rebates (VUR) to commercial and industrial properties, with the exception of taxation years 2014 and 2015, as rebates continue to be actively processed for these years as outlined in Attachment 1, Table 1. Approximately $22 million of the total rebates paid represent the provincial education portion of rebates, which are funded by the Province of Ontario, therefore the City impact is $23 million.
- On average, VUR paid to commercial properties represent approximately 91.8% of all rebates paid, while industrial rebates represents approximately 8.2% overall as summarized in Attachment 1, Table 2.
- The largest percentage of rebates are paid for properties located in Wards 27 and 28, Toronto Centre-Rosedale, representing 11.6% and 23.2% respectively of all rebates paid over the period of 2001 to 2015. These wards represent the central downtown area, which houses the largest concentration of commercial buildings as outlined in Attachment 1, Table 3.
- Small and large office buildings account for the largest percentage of vacancy rebates paid, at 20.8% and 32.9% of all rebates paid as summarized in Attachment 1, Table 4.
- Approximately 9% of all rebates are paid to owners of large commercial shopping centres i.e. Yorkdale, Eaton Centre and Sherway Gardens, etc. as displayed in Attachment 1, Table 4.
- Small neighbourhood retail properties (typically storefront with residential units above) account for less than 2% of all rebates paid, yet this type of property represents the highest number, at 1,967 properties, that applied for and received rebates for the period 2001 to 2015 as outlined in Attachment 1, Table 4.
- Less than 20% of all small neighbourhood retail properties in the City received a VUR as summarized in Attachment 1, Table 4.
- Only 193 small neighbourhood retail properties received a VUR for more than 5 years from 2001 to 2015 as outlined in Attachment 1, Table 5.
- The majority of properties applied for and received rebates for 1 to 4 years over the period spanning 2001 to 2015. Only 837 properties city-wide (8% of all rebates paid) applied for and received rebates for 10 or more years during this same period. Properties that received rebates in multiple years are typically large office, large commercial and industrial or large shopping centres, that may have multiple periods of vacancies as tenants come and go, as summarized in Attachment 1,Table 5.

COMMENTS

The City of Toronto, as directed by City Council, has been reviewing and analysing the implications of redesigning the Vacant Unit Rebate program for the past several years.

Input has been obtained from stakeholders and the business community, in the form of consultations and surveys.

The Province has now provided municipalities with a legislative framework to facilitate increased flexibility with the Vacant Unit Property Tax Rebate program as well as the Vacant and Excess Land Subclass Tax Reduction program. The vacant land and excess land subclass tax reduction applies to commercial or industrial lands that are either vacant or are not being used for business purposes.

Proposed Plan for the Vacant Unit Rebate Program

The City's current proposal relates only to the Vacant Unit Property Tax Rebate program. The recommendations in this report would see a reduction in the allowable rebate percentage for vacant commercial properties from 30% to 15% for the period July 1, 2017 to June 30, 2018.

The rebate percentage for industrial properties would remain at 35% for all of 2017 and up to June 30, 2018, recognizing the additional impacts that a reduction in rebate amounts would have on industrial properties, which typically remain vacant for longer periods of time given the often purpose-built nature of industrial properties. Additionally, it is recognized that vacant industrial properties may come under increased pressure to convert to other uses, which would diminish Toronto's already shrinking industrial tax base. For 2018, using the rebate expenditure reductions to reduce tax rates overall within the industrial tax class recognizes the importance of reduced taxation levels to support the viability and financial health of Toronto's critical employment sector.

It is recommended that the vacant unit rebate program be discontinued for industrial and commercial properties beginning July 1, 2018, and that an amount equivalent to the half the estimated municipal portion of industrial taxes to be rebated for 2017 be used to reduce the overall municipal tax rates for the industrial property class in 2018, with the other half to be reduced in 2019. By reducing the industrial rates in 2018 and 2019, ongoing relief will be embedded in the industrial rates for future years.

Additionally, this report recommends that the Province of Ontario be requested to reduce industrial education tax rates for 2018 in amounts equivalent to the estimated vacancy rebates that would otherwise be payable to properties in these classes, and consider using the additional education tax room from elimination of the commercial vacant unit rebate program in a similar manner as the City, i.e. reinvested in poverty reduction programs, economic development for depressed retail areas, and education tax relief.

Expenditure savings from the elimination of the vacancy rebate program will be reinvested in poverty reduction programs, economic development for depressed retail areas, and tax relief in 2018 and future years. Allocations will be addressed as part of the 2018 budget.

Should Council choose to adopt the recommendations in this report, the City will be in a position to engage the Province by submitting Council's resolution, along with details of the proposed changes, which the Province should then implement through regulatory changes.

Stakeholder Consultations

Further to the direction of City Council, staff undertook a stakeholder consultation process to request feedback from stakeholders how the elimination of the Vacant Commercial and Industrial Unit Rebate program. In order to maximize efficiency, staff also requested stakeholders to provide feedback on the potential impact on the elimination of the Vacant/Excess Land Subclass Tax Reduction program.

The consultation process comprised three (3) phases, consisting of meetings with representatives from large commercial and industrial property owners, along with representatives from the City's Business Improvement Areas, public consultation sessions open to all interested parties, and an on-line survey available through the City's web site. Stakeholders were able to complete the survey between April 11 and April 28. Feedback was received from a wide range of stakeholders ranging from commercial/industrial property owners, the business community at large, non-profit organizations, the arts and culture community, and city residents.

Summary of Results from Online Survey

A total of 415 individuals responded to the survey, of which, 164 surveys were completed fully. This translates to a 40% completion rate.

The following section highlights key findings of the survey. Full details of survey responses are included as Attachment 4 to this report.

In terms of survey respondents, of the 174 respondents who completed the question on the group they belong to: 6 per cent identified themselves as an owner/tenant of an industrial property, 14% as owner/tenant of commercial properties, 11% as owner/tenant of commercial retail properties, and 8% as owner/tenant of a non-profit property. A total of 26 respondents (15%) identified themselves as a member of a business or professional association representing business owners or tenants, while almost half of all respondents (81, or 47%) fell into the "other" category, which included residential property owners, members of the arts or community organizations, or other interested parties.

In response to the question "What impact will the elimination of the Vacant Unit Property Tax Rebate Program have on your business model?", of the 127 total respondents: 40 respondents (31%) indicated the changes would have no or minimal impact, while 26 (20%) indicated changes would have a significant impact. Importantly, almost half or 61 respondents to this question (48%) entered a response of "not applicable", meaning that these respondents would likely not be affected by the elimination of the program, in that they were not commercial/industrial property owners, or they were residents or members of arts or other groups.

In response to the question "How long will it take your organization/business/group to adjust to changes to the Vacant Unit Property Tax Rebate Program?", of the 121 total respondents: 79 or 65% of respondents indicated it would take less than 6 months to adjust, 7% indicated 6 months to one year, 10% responded one year to two years, and 21 or 17% of respondents indicated more than two years.

Stakeholder Feedback on the Elimination of the Vacant Unit Rebate (VUR)

Through the various means of providing feedback, stakeholders representing large commercial property owners and industrial property owners have made it clear that they are against the elimination of the VUR program. In essence, large commercial property owners view any reduction in relief available through the VUR program as a form of a tax increase. This is not surprising considering that about half of all of the dollar value paid out as rebates under this program have been to these property owners. The change to the program will require new business models to be developed, which will take time and will increase owners' operating costs, which will ultimately be passed through to business tenants in the form of increased rents.

A coalition of business interest groups representing large commercial property owners advanced a proposal (see Attachment 2) to allow the current vacant unit rebate program to continue, using a self-funding mechanism (i.e., to fund the program costs from within the commercial and industrial tax classes through a special levy, similar to the way that charitable tax rebates are currently funded). This approach would require a legislative change to implement. This business coalition also advanced suggestions to extend the time for phasing out the program, in order to allow businesses to adjust, and to consider time limits on eligibility, i.e., to disallow or reduce the rebate after a period of time for long vacant properties. As a result of the consultations and the case made by commercial entities for a longer phase-in, the Deputy City Manager & CFO has recommended in this report that the full elimination of the vacant unit rebate be postponed from January 1, 2018 to July 1, 2018.

Industrial property owners noted that the VUR has value because it encourages companies experiencing slow business cycles to keep buildings intact for future use during growth periods, rather than demolish them if underutilized. Further, the program encourages companies that plan to grow to buy a large site and hold on to part of it for later use. This tax relief provided by the VUR offers a form of protection to industrial landowners to resist financial pressures to convert industrial lands to other uses.

Stakeholders representing BIAs in some cases contend that the VUR contributes to owners being able to keep their storefront vacant for extended periods of time, e.g., during a land consolidation for redevelopment, and were generally in favour of the elimination of the program. The desire is to animate streetscapes with many retail options and the VUR is seen as a deterrent to achieving this goal in some neighbourhoods.

Toronto residents and representatives from the arts and non-profit communities indicated strong support for eliminating the VUR program and re-investing the funds in programs that would revitalize neighbourhoods in distressed retail areas. Strong support was also received to provide incentive programs that would provide low cost space for the arts, non-profit and business start-up/incubator uses.

While there were strong voices on both sides of the argument to keep or eliminate the VUR program, the strongest voices heard during the consultations were from small business, not-for-profits and residents that the savings that would be realized from the program would be better funnelled into programs that directly support neighbourhoods and main street retail.

Please see the report attachments for more details on the consultation and survey findings, as well as written submissions received from various stakeholders.

Proposed Usage of Funds Available from Elimination of Vacant Unit Rebate

Funds available from the elimination of the VUR will be invested in the following three priorities: poverty reduction programs, economic development for depressed retail, and tax relief.

This report recommends that the General Manager, Economic Development & Culture, report back on proposals that would see a portion of the reduction in rebate expenditures reinvested in programs or initiatives designed to stimulate economic growth and job creation by enhancing distressed (high vacancy) retail areas or that encourage community and local economic activity in depressed retail areas.

Further, the Deputy City Manager & Chief Financial Officer, in consultation with the Deputy City Manager Cluster A and the Executive Director of Social Development, Finance and Administration, will report on plans to reinvest a portion of the reduction in rebate expenditures in programs or initiatives that support Toronto's poverty reduction strategy, and in tax rate reductions. Further details of the proposed uses will be included in the 2018 budget.

Eliminating the vacancy rebate program will also result in direct operational savings in the form of reduced expenditures to administer the program, including staff costs and contract expenses, estimated at approximately $1 million per year.

Tax Reductions for Vacant and Excess Commercial and Industrial Lands

Toronto's consultations with business stakeholders also solicited input on the implications and financial impacts to businesses on changes to the current tax reductions that apply to vacant and excess commercial and industrial lands. The vacant land and excess land subclass tax reduction applies to commercial or industrial lands that are either vacant or are not being used for business purposes.

Currently, lands classified within the commercial vacant/excess land subclass are taxed at a rate that is set at 70 per cent of the full commercial tax rate (i.e., a 30% reduction in the rate), while industrial vacant/excess lands are taxed at 65 per cent of the full industrial tax rate (a 35% reduction).

Currently, the tax reductions for the vacant and excess land subclass tax reductions total approximately $19.7 million. Of this total tax reduction, the City portion is $10.7 million, and the provincial education portion is $9 million. Roughly 70 per cent of the tax reduction (or $13.7 million) is attributable to industrial properties, while 30% (or $6.0 million) is attributable to commercial properties.

The Province's 2016 Fall Economic Statement has provided municipalities with additional flexibility in setting the percentage tax reductions that could apply to vacant/excess commercial and industrial lands, up to and including eliminating the subclass tax reductions altogether, beginning in 2017. Eliminating the current subclass tax reductions could result in additional taxation revenues of approximately $10.7 million annually. Similar to changes to the vacant unit rebate program, any proposed changes to the subclass tax reductions have to be prescribed by provincial regulation, and only after consultations with businesses and Council has adopted a resolution approving such changes.

During consultations on this issue, stakeholders expressed concern that eliminating the tax reduction program for excess land may put added pressure to rezone industrial land for non-manufacturing purposes. This could reduce land stock that can accommodate employment uses. It was pointed out that property owners invest in vacant industrial land as a method of protecting themselves from speculators and to keep industrial land for future expanded manufacturing uses. Similarly, concerns were raised that MPAC values vacant land at its 'highest and best use', making vacant land values extremely high, potentially making industrial lands scarcer to find for rent or ownership.

Staff received written submissions from the Railway Association of Canada (see Attachment 2). The association pointed out that rail operations are land intensive operations and require large tracts of vacant land. Eliminating the vacant/excess land tax reduction program will not alter the land requirements of the railway industry. Eliminating the tax reduction program will have a negative impact on railway industry and may result in higher costs being passed on to customers.

This report does not make recommendations regarding the vacant/excess commercial and industrial land subclasses. Further recommendations concerning changes to vacant/excess land subclass tax reductions will be considered within the context of the 2018 operating budget and reported to Council through the budget process, having due regard to stakeholder feedback received to date and through the budget consultation process.

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SIGNATURE

Mike St Amant
Treasurer

Mike Williams, General Manager
Economic Development & Culture

ATTACHMENTS

Attachment 1: Summary of Vacant Commercial and Industrial Property Information from 2001 to 2015

Attachment 2: Copies of written submissions received:

a) Railway Association of Canada, dated March 22, 2017
b) Toronto Industry Network, dated April 4, 2017
c) Toronto Real Estate Industry Coalition, dated May 2, 2017

Attachment 3: Summary of Stakeholder Consultations

Attachment 4: Summary of Survey Results