



Supplementary Report: Property Tax Capping Policies for 2020

Date: February 5, 2020
To: Executive Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

This is a supplementary report to Item BU14.1: 2020 Property Tax Rates and Related Matters and recommends the 2020 policies for property tax capping protection for business properties.

Specifically, this report recommends to continue the tax capping policy of limiting tax increase to 10% of a property's prior year's taxes to any property in the commercial, industrial and multi-residential tax classes in 2020.

In addition, in order to ensure that progress continues to be made in moving properties to their full Current Value Assessment (CVA) level of taxation, it is recommended that Council adopt a policy that properties that are within \$500 (plus or minus) of their full CVA level of taxation in the current year are excluded from capping/claw-back provisions for that year, and be taxed at full CVA.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. City Council adopt the following property tax capping policies for the 2020 taxation year:

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, by opting to have subsection 292(1), paragraph 1, of the City of Toronto Act, 2006, apply for the 2020 taxation year;

b. continue to provide that the 10% cap on tax increases apply to any property within the commercial, industrial and multi-residential classes, regardless of

whether the property had reached full Current Value Assessment taxation levels in a prior year, subject to the threshold adopted in Part c. below.

c. for the purposes of subsection 292(1), paragraphs 3 and 4 of the City of Toronto Act, 2006, adopt a threshold limit of \$500 to determine the taxes for municipal and school purposes, such that properties that are within \$500 (plus or minus) of their full Current Value Assessment level of taxation in the current year are taxed at full Current Value Assessment taxation levels for the year, and are therefore excluded from capping/claw-back provisions for that year.

FINANCIAL IMPACT

There is no financial implication to the City of Toronto's budget arising from the capping policy changes recommended in this report. Under the capping and claw-back system, the foregone revenue resulting from the capping limit on Current Value Assessment (CVA)-related tax increases for properties in the commercial, industrial and multi-residential property tax classes is funded by withholding (clawing-back) a portion of the tax decreases that would otherwise be applied to other properties within each class.

DECISION HISTORY

City Council adopted tax rates, education rates and claw-back rates and other tax policy decisions for the 2019 taxation year by adopting items [EX2.1: 2019 Property Tax Rates and Related Matters](#) and [EX4.6: 2019 Education Property Tax Levy and Clawback Rate By-law](#).

COMMENTS

Toronto's current tax policies are shaped by legislative and regulatory requirements set out in the City of Toronto Act, 2006 (COTA) and the Assessment Act, and by Council's previously adopted tax policy measures. Mandatory limitations on annual allowable tax increases (tax capping) and the withholding of tax decreases (claw-backs) for properties in the commercial, industrial and multi-residential tax classes have been in place since 1998.

Tax Capping

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 system, tax capping has been in place in Toronto since 1998. Under COTA, capping is mandatory for properties in the commercial, industrial and multi-residential tax classes, although municipalities have some flexibility in setting the tax capping parameters.

In order to recover the tax revenue foregone by the capping limits on properties experiencing tax increases, provincial legislation and regulations permit municipalities to withhold a portion of the tax decrease that would otherwise apply to properties that have experienced an assessment-related tax decrease, i.e., the "clawing-back" of decreases. Each year, Council establishes a claw-back rate for each class that prescribes the percentage of the tax decrease that must be withheld (clawed-back) to fund the costs of capping protection.

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 by business property owners and the legal community and real estate and tax professionals that represent them.

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.

Toronto's Current Tax Capping Policies

Toronto Council's long-term property tax policies have included, from 2009 to 2017, 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.

In terms of municipal flexibility, COTA allows annual tax capping limits to be based on a maximum allowable increase equal to 5 per cent or 10 per cent of the prior year's annualized taxes, or 5 or 10% of the prior year's CVA-level taxes. A municipality may also decide whether to exclude a property from the capping/claw-back provisions once the property has reached its full CVA level of taxation, or to continue to have capping/claw-back apply in any subsequent year.

"Annualized taxes" refers to the actual amount of taxes levied in the year, or in the case of properties where, during the taxation year, a change in taxes occurred that applied to a portion of the taxation year (e.g., due to assessment or other appeals, a change in tax status, or a change in the assessed value of the property arising from new construction, improvements, renovations, demolitions, change in zoning, etc.), annualized taxes refers to the taxes that would have been payable had the change applied to the full year.

From 2006 - 2016, Council adopted a capping limit of 5% of the prior year's CVA-level taxes and prior to 2006 the City's caps were based on 5% of annualized taxes. In 2017, in order to accelerate progress towards full CVA taxation, Council approved an increase in the capping limit to 10% of the prior year's full CVA. In 2018 and 2019, Council approved the capping limit of 10% of annualized taxes for the reasons discussed below.

Changes to Tax Policies in 2018 and 2019

The 2017 province-wide reassessment saw many business properties faced with assessment increases of 10 per cent or more, with incremental increases phased-in over each year from 2017 to 2020. In 2017, where properties had reached their full CVA-level of taxation in a prior year, tax increases were no longer eligible for capping protection, resulting in many business properties facing tax increases of greater than 10 per cent, and in some cases substantially more.

In 2018 and 2019, Council adopted measures to ensure a level of protection against such unmitigated increases, by adopting a cap to ensure that tax increases would not exceed 10 per cent of the prior year's annualized taxes, regardless of the magnitude of assessment change, even if a property had reached its full CVA level of taxes in a prior year. This change, however, had the effect of reversing years of progress in moving properties to and keeping them at their full CVA level of taxation, as shown in Figure 1 below. Figure 1 illustrates steady progress between 2009 and 2017 in the number of commercial properties taxed at full CVA taxation levels, and a corresponding reduction in the number of properties subject to capping and claw-back over this same period.

Figure 1: Percentage of properties taxed at full CVA, and percentage of properties subject to capping or claw-back, Commercial Class, 2009 to 2019

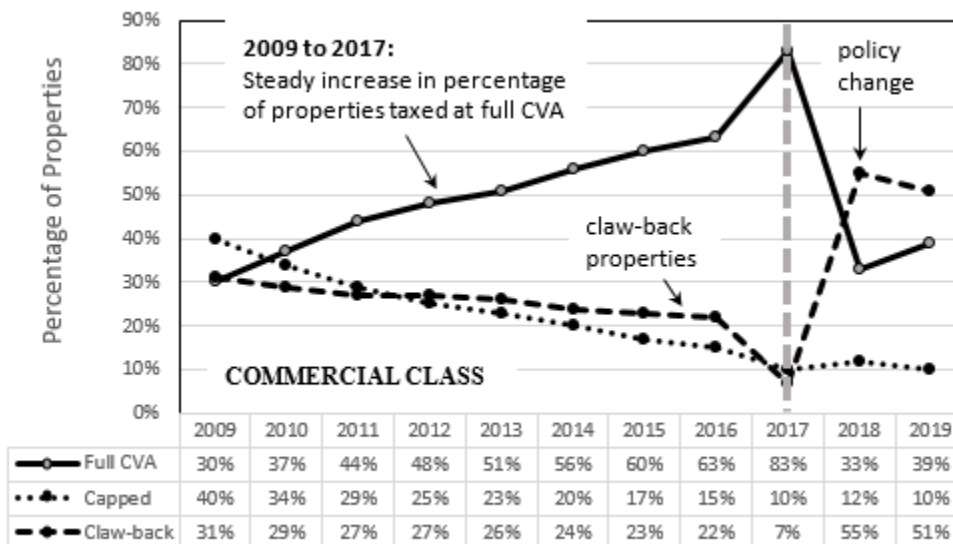


Figure 1 also shows that the policy change adopted in 2018 and 2019, that saw properties eligible for tax capping protection regardless of whether they had reached full CVA taxation levels in a prior year, had the effect of reverting properties that had previously been taxed at full CVA tax back into capping/claw-back regime, and causing the number of properties subject to claw-back to substantially increase. Even where a property was very close to full CVA taxation levels, i.e., either above or below, the property again became subject to capping/claw-back adjustments, and was therefore no longer taxed at full CVA taxation. This outcome is not consistent with the objective of accelerating progress towards full CVA taxation.

Fortunately, the drop in the number of properties taxed at full CVA levels in 2018 and 2019 can be considered a reversible trend, through the adoption of threshold limits. The City of Toronto Act allows for the adoption of a threshold when determining maximum allowable tax increases and capping/claw-back adjustments. Adopting a threshold limit of \$500, for example, would see any property whose taxes are within plus or minus \$500 of the property's full CVA taxes for the year taxed at the full CVA tax level, and therefore excluding from capping/claw-back provisions. This change in tax policy is recommended for the 2020 taxation year.

Figure 2 below shows the projected change in the number of properties taxed at full CVA levels, and the percentage of those subject to capping or claw-back, if a \$500 threshold was adopted for 2020.

Figure 2: Projected percentage of properties taxed at full CVA, and projected percentage of properties subject to capping or claw-back, Commercial Class, 2020 if \$500 threshold applies

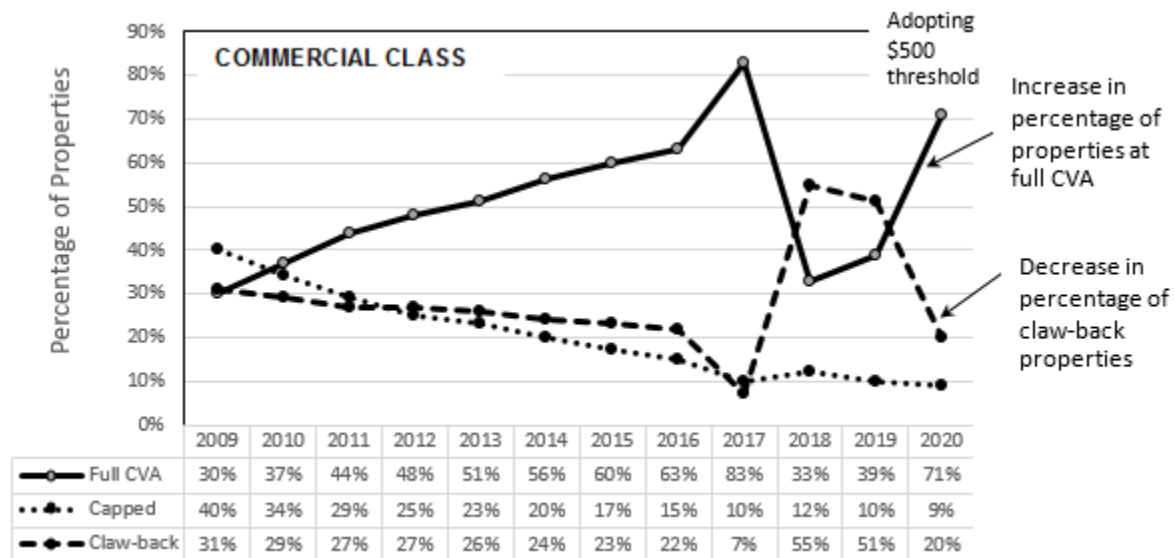


Table 1 below summarizes the estimated impacts of adopting a \$500 threshold on each of the commercial, industrial and multi-residential property classes, showing the number of properties within each class that would be taxed at full CVA taxation levels, or subject to capping or claw-back respectively, if no threshold was adopted, and if a \$500 threshold was adopted. Table 1 also provides an estimate of the change in the claw-back rate required (the percentage of the tax decrease that is withheld in order to fund the caps on tax increases) that would result from adopting a \$500 threshold.

Table 1: Comparison of number of properties at full CVA or capped and clawed-back, with and without \$500 threshold and change in claw-back percentage

Tax Class	If No Threshold Applies				With \$500 Threshold			
	Properties at Full CVA	Capped Properties	Claw-back Properties	Claw-back Percentage	Properties at Full CVA	Capped Properties	Claw-back Properties	Claw-back Percentage
Commercial	15,441	3,813	20,086	65.1%	27,740	3,715	7,885	66.4%
Industrial	1,332	127	2,132	50.1%	2,313	115	1,163	51.6%
Multi-Residential	1,683	116	2,121	39.9%	2,191	113	1,616	40.7%
Total:	18,456	4,056	24,339		32,244	3,943	10,664	

Table 1 provides that, by adopting a \$500 threshold, 32,244 properties across the business classes would be paying taxes at full CVA taxation levels, compared to 18,456 if no threshold was adopted. Similarly, the number of properties subject to claw-back decreases sharply under a threshold, from 24,339 to only 10,664 properties. More importantly, the change in claw-back percentages with the adoption of a threshold is only a slight increase in the claw-back percentage (an increase of 1 to 1.5 per cent), resulting in minimal actual tax impact to properties subject to claw-back.

Recommended Changes to Tax Policies for 2020

This report recommends that Council continue to limit allowable tax increases for the commercial, industrial, and multi-residential property classes in 2020 to 10% of the preceding year's annualized taxes, consistent with the capping rules applied in 2018 and 2019.

It is further recommended that:

- a) Council adopt a threshold of \$500 for the determination of taxes for municipal and school purposes under S. 292(1) of the City of Toronto Act, such that properties that are within \$500 (plus or minus) of their full CVA level of taxation in the current year be taxed at full CVA taxation levels for the year, and therefore excluded from capping/claw-back provisions for that year; and

These measures will ensure a level of protection against unmanageable increases, while providing certainty and predictability for property owners and business tenants, such that no taxpayers within the business tax classes will face an assessment-related tax increase that is greater than 10% of last year's annualized property taxes, provided the tax increase is greater than \$500, and excluding budgetary rate increases.

Staff will be reporting to a future meeting of Executive Committee, or directly to Council or a special meeting of Council if necessary, on the 2020 tax rates for school purposes, and the 2020 percentage of the tax decreases required to recover the revenues foregone as a result of the cap limit on properties in the commercial, industrial and multi-residential property classes (the 2020 'claw-back' rates). A full analysis of the

individual impacts by property of the tax policies recommended in this report cannot be completed until the education rates and claw-back rates have been finalized.

Although the tax policies recommended for 2020 will provide protection against large tax increases, further analysis of additional options that align with Council's strategic objectives, and approaches to provide targeted tax protection to identified or vulnerable groups, will continue to be studied by staff in consideration of 2021 and future years.

CONTACT

Casey Brendon, Director, Revenue Services
Phone: (416) 392-8065, E-mail: Casey.Brendon@toronto.ca

Boriana Varleva, A/Director, Financial Policy and Strategies
Phone: (416) 392-4949, E-mail: Boriana.Varleva@toronto.ca

SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer
