EX30.4

REPORT FOR ACTION

Implementation of Municipal Accommodation Tax (Hotel and Short-Term Rental Tax)

Date: January 10, 2018
To: Executive Committee
From: Acting Chief Financial Officer
Wards: All

SUMMARY

This report responds to Council's direction to implement a municipal transient accommodation sales tax, at the rate of four percent of hotel accommodation sales, and up to ten percent of short-term residential accommodation sales.

The report recommends that the Municipal Accommodation Tax ("MAT") consist of two components: a sales tax on hotel accommodation ("MAT-Hotel"), and a sales tax on short-term rentals[1] ("MAT-STR").

Staff recommend the implementation of a 4% MAT-Hotel and seek all necessary authorities to implement it on all hotel accommodation transactions effective April 1, 2018, including approval of the administrative design features for the tax, enforcement provisions for the tax, and authority to enter into an administration and collection agreement with the Greater Toronto Hotel Association.

The report also recommends that Council adopt the MAT-STR at the same rate of 4%, to be effective on all short term rentals transacted from the date at which the short-term rental bylaw (to be enacted in accordance with Council's decision on LS23.1 titled 'Licensing and Registration Regulations for Short-Term Rentals' on December 5-7, 2017) comes into effect (expected to be on or after June 1, 2018). In order to facilitate efficient collection of this tax, this report recommends that City staff be authorized to enter into agreements with all licensed short-term rental companies pursuant to which they would assume the role of collecting agent of the tax on behalf of the City in respect of all registered operators associated with the company.

[1] The definitions of the terms used in this report, including "short-term rental", "operator", "short-term rental company", and "principal residence" are the same as those in the Short-Term Rental by-law to be enacted in accordance with Council's decision on LS23.1, titled 'Licensing and Registration Regulations for Short-Term Rentals' on December 5-7, 2017.

A provision of $16.1 million in net MAT revenue has been set up in Non-Program Revenue of the 2018 Operating Budget. This is the estimated gross tax revenues to the City less costs related to administration and collection and the estimated value of a transfer to Tourism Toronto.

RECOMMENDATIONS

The Acting Chief Financial Officer recommends that:

1a. City Council approve the implementation of a 4% tax on the sale of transient accommodations other than short-term rentals (the Municipal Accommodation Tax - Hotel, or "MAT-Hotel"), effective for all such transactions commencing April 1, 2018 and adopt the tax features for the MAT-Hotel as set out in Attachment 1 and 1A to this report.

1b. City Council authorize the appointment of the Greater Toronto Hotel Association as the City's collection agent for the MAT-Hotel, and direct the Acting Chief Financial Officer, in consultation with the City Solicitor, to enter into all related agreements on terms substantially as set out in Attachment 2 and upon such other terms as may be acceptable to the Acting Chief Financial Officer.

2a. City Council approve the implementation of a 4% tax on the sale of transient accommodations in short-term rentals (the Municipal Accommodation Tax - Short-Term Rental, or "MAT-STR"), effective for all such transactions commencing on the date on which the pending short-term rental by-law comes into force (expected to be on or after June 1, 2018), and adopt the tax features as set out in Attachment 1 and 1B to this report.

2b. City Council authorize the appointment of licensed short-term rental companies as the City's collection agents for collection of the MAT-STR in respect of short-term rental operators associated with that company, and direct the Acting Chief Financial Officer, in consultation with the City Solicitor, to enter into all necessary agreements with such companies on terms substantially as set out in Attachment 3 and upon such other terms as may be acceptable to the Acting Chief Financial Officer.

3. City Council amend the Non Program Revenue and the Office of the Treasurer's 2018 Preliminary Operating Budget to reflect the recommendations in this report resulting from the adoption of the Municipal Accommodation Tax (MAT) such that:

a. The 2018 Preliminary Non-Program Revenue Budget gross revenue be adjusted to $34.667 million and net revenue of $16.100 million;
b. The transfer in 2018 of $18.000 million to Tourism Toronto;
c. The transfer of $0.225 million to the Greater Toronto Hotel Association for the administration of the Municipal Accommodation Tax as the collection agent for the City of Toronto for the hotel industry; and

d. The recovery of $0.342 million from Non Program to the Office of the Treasurer and increase in the Preliminary 2018 Operating Budget for the Office of the Treasurer by $0.342 million gross and $0 net, and 3.5 new positions for the administration of the Municipal Accommodation Tax.

4. City Council seek the appropriate Federal legislative or regulatory amendments to exempt the Municipal Accommodation Tax from the Harmonized Sales Tax (HST).

5. City Council delegate the hearing of any Municipal Accommodation Tax appeals to the Government Management Committee.

6. The Acting Chief Financial Officer, in consultation with the City Solicitor and upon such terms as may be acceptable to him, be directed to enter into an agreement with Tourism Toronto respecting the financial accountability required to ensure that all MAT amounts paid to Tourism Toronto by the City are used for the exclusive purpose of promoting tourism as required by Ontario Regulation 436/17.

7. Council direct that the Short-Term Rental by-law to be enacted in accordance with LS23.1, titled 'Licensing and Registration Regulations for Short-Term Rentals', include a provision establishing that all information collected in accordance with that by-law, is collected for the purposes of the administration and enforcement of both that by-law and the MAT-STR by-law, and also a provision requiring that the transaction records that operators are required to maintain and provide to Municipal Licensing and Standards shall include information on the nightly price charged for the applicable short term rental.

8. The General Manager of Economic Development & Culture be directed to report back by the second quarter of 2019 on a review of the geographical boundary for Regional Tourism Organization 5 (RTO5) respecting municipal contributions to Tourism Toronto.

9. The City Solicitor be authorized to introduce the necessary bills to give effect to the Municipal Transient Accommodation Tax including: to add the Municipal Accommodation Tax By-law to the City of Toronto Municipal Code as a new Chapter of the Code; to amend the Chapter 27, Council Procedures, of the City's Municipal Code to delegate the hearing of Municipal Accommodation Tax appeals to the Government Management Committee; and to amend the by-law with the Short-Term Rental Operator Registry referred to in recommendation no. 7 as required, and the appropriate City officials be authorized and directed to take necessary actions to give effect thereto.

FINANCIAL IMPACT

By introducing Bill 127 in its 2017/18 budget and subsequently proclaiming the legislation, the Province provided Toronto with the necessary legislative authority, through an amendment to the *City of Toronto, 2006* ("COTA") to levy a transient accommodation tax. Ontario Regulation 436/17 requires the City to provide a minimum guaranteed contribution ("floor") to Tourism Toronto from the accommodation tax revenue to replace revenues previously generated through the Destination Marketing

Program ("DMP"), subject to sufficient tax being collected. The floor will be determined by the amount of DMP fees collected by the Greater Toronto Hotel Association and received by Tourism Toronto for the 2017 fiscal year. The figure will not be known with certainty until the end of Q1 2018 at the earliest. Payment to Tourism Toronto is due no later than 60 days after the 2018 year-end, subject to the receipt of DMP data to the City's satisfaction.

A preliminary operating budget for 2018 for MAT was estimated prior to the release of the Provincial regulation respecting revenue sharing with Tourism Toronto, at $37.0 million gross, and $16.1 million net (with $20.0 million payment to Tourism Toronto, and $0.9 million in associated costs). This budget is based on initial assumptions regarding the design parameters, collection agreement terms, costs estimates and revenue sharing requirements, and assuming implementation dates of April 1, 2018 for MAT-Hotel and June 1, 2018 for MAT-STR.

This report recommends that the City retain the Greater Toronto Hotel Association to help administer the MAT-Hotel for an initial period of up to two years at an expected cost of $225,000 in 2018 and $265,050 in 2019, and that these amounts be funded from the tax revenues.

Additionally, the administrative programs required for the tax (e.g. call centre customer services, tax revenue accounting/reporting and corporate IT support) are expected to cost the Revenue Services Division an estimated $222,000 in 2018 and $296,000 annually thereafter for the MAT-Hotel, and $120,000 in 2018 and $200,000 annually thereafter for the MAT-STR. The estimated costs incorporate recruiting and hiring of 3.5 FTE (full time equivalent) support staff and are a refinement of previous estimates. This report recommends that Council include related provisions in the consideration of the 2018 Operating Budget.

Subsequent to the release of the Provincial regulation, financial estimates were updated to reflect the required revenue sharing with Tourism Toronto and other costs. Table 1 below summarizes the revised recommended budget in Non-Program Revenues of the 2018 Operating Budget:

Table 1 - Revised Recommended 2018 Operating Budget		
Gross MAT revenue	**$**	**34,667,000**
Payment to Tourism Toronto		18,000,000
Administration Costs:		
Greater Toronto Hotel Association		225,000
Office of the Treasurer (Revenue Services): 3.5 full-time positions		342,000
Net MAT Revenue	**$**	**16,100,000**

As the proposed taxes and licensing programs are new, and data for the current DMP revenues have not been made available, actual net revenues may vary and will be closely monitored and reported to Council as part of in-year variance processes. Any material change to the recommended tax design or to the terms of the administration agreement or arrangements that would jeopardize the MAT-Hotel April 1, 2018 implementation date would reduce net revenues in 2018.

Table 2 below provides a potential range of the net estimated revenue ranging from $14.6 million to $23.0 million for 2018. This is based on the terms of the regulation, assumed revenues of approximately $32.8 million to $38.4 million from MAT-Hotel, $1.2 million to $1.7 million from MAT-STR, and an assumed $16.5 million to $18.8 million payment to Tourism Toronto. The recommended revised gross revenues and payments to Tourism Toronto are within the range of the estimates.

Table 2 - Forecast of Municipal Accommodation Tax Revenue
($millions)

	2018*	Annualized
Gross Revenues		
MAT-Hotel	32.8 to 38.4	41.0 to 48.0
MAT-STR	1.2 to 1.7	2.0 to 3.0
	34.0 to 40.1	**43.0 to 51.0**
Payment To Tourism Toronto	-16.5 to -18.8	-22.0 to -25.0
MAT after payment to Tourism Toronto	**15.2 to 23.6**	**18.0 to 29.0**
Administration Costs		
MAT-Hotel	-0.5	-0.6
MAT-STR	-0.1	-0.2
Net Revenues	**14.6 to 23.0**	**17.2 to 28.2**

* Implementation dates assumed to be April 1, 2018 for MAT-Hotel and June 1, 2018 for MAT-STR

This report also discusses the revenue allocation of the proceeds from the new tax. Consistent with the approach used with the other existing taxes authorized under COTA, such as the Municipal Land Transfer Tax and the Third Party Sign Tax, staff have proposed that the preliminary 2018 Operating Budget be based on the tax proceeds being directed to general corporate revenues, i.e. non-program revenues.

DECISION HISTORY

On January 28, 2016, Executive Committee referred item [EX11.19 Regulating Temporary Accommodation Rentals] to the Executive Director, Municipal Licensing & Standards (ML&S), and the Chief Planner and Executive Director, City Planning, to provide an interim report in the third quarter of 2016 and a final report in 2017 on regulating temporary accommodation rentals.

On October 28, 2016, Executive Committee adopted [EX18.12 Developing an Approach to Regulating Short-Term Rentals] and directed the Executive Director, ML&S, and the Chief Planner and Executive Director, City Planning, to report no later than the end of the second quarter of 2017 with proposed regulations for short-term rentals.

On December 13, 2016, City Council adopted EX20.2 The City of Toronto's Immediate and Longer-term Revenue Strategy Direction requesting that the Province make legislative and/or regulatory reforms to grant the City authority to collect a hotel and short-term rental tax. Upon legislative changes from the Province, City Council endorsed the implementation of the hotel and short-term rental tax and requested that the City Manager report back on a recommended tax rate for short-term rentals that is no higher than 10%. City Council also requested the City Manager to report to the Budget Committee as part of the 2017 budget process to consider increasing the City's investment in Arts and Culture funding from a portion of the revenue generated from a Hotel Tax.

On February 15, 2017, City Council adopted EX22.2 2017 Operating and Capital Budget, which endorsed the creation of a hotel and short-term rental tax in the City of Toronto, at rates of four percent of hotel accommodation revenues, and up to 10 percent of short-term rental revenues, subject to receiving the necessary legislative authority, and directed staff to report back on the proposed design features and implementation authorities, including a revenue allocation policy, and status of the required legislative authority, for implementation as soon as practical in 2017.

On June 19, 2017, Executive Committee adopted EX26.3 Proposed Regulations for Short-term Rentals for Consultation, with amendments, and directed the Chief Planner and Executive Director, City Planning, to prepare amendments to all applicable general zoning bylaws to permit short-term rentals; hold community meetings as required by the Official Plan and a public meeting as required under the Planning Act; and, to report with final zoning amendments to a statutory meeting of Planning and Growth Management Committee. In addition, Executive Committee directed the Executive Director, ML&S, to conduct public consultation on the proposed licensing and registration framework; and directed the Executive Director, ML&S, to report with the licensing and registration requirements to the Licensing and Standards Committee in the fourth quarter of 2017.

On November 15, 2017, Planning and Growth Management Committee considered PG24.8 Zoning By-law and Zoning By-law Amendments to Permit Short-term Rentals which recommended zoning changes to permit short-term rental activities in principal residences across the city.

On November 16, 2017, Licensing and Standards Committee considered LS23.1 Licensing and Registration Regulations for Short-Term Rentals which recommended a registration and licensing program for short-term rental activities in Toronto.

On November 17, 2017, Economic Development Committee considered EC25.5 Ensuring a Robust Hotel Supply to Strengthen Tourism which recommended a review of the potential for the implementation of a hotel accommodation replacement policy and or strategy.

On Dec 5-7, 2017 City Council adopted both PG24.8 and LS23.1 with amendments, which recommended zoning changes to permit short-term rental activities in principal residences across the City, and a registration and licensing program for short-term rental activities in Toronto.

COMMENTS

1. Revenue Strategy

The Long-Term Financial Direction report considered by Council in June 2016 (EX15.1) outlined a series of principles and directions to guide the development of new strategies for the management of expenses and the expansion of revenues.

In accordance with these principles, staff provided Council, in December, 2016, with a framework for the application of existing and new revenues, principles for the selection of potential revenues, a discussion on social and economic impacts, along with implementation considerations.

While the framework focused on options for the application of major existing and potential revenue sources such as property tax, land transfer tax, and expressway tolls, the framework also considered a variety of "specialty taxes" that would be applied to a much narrower base of taxable activity and from which the potential revenues would be considerably smaller, including a potential "hotel tax".

As with the other potential revenue sources, the specialty taxes were evaluated on the following criteria, which were detailed in the December 2016 report:

1. Incidence/Fairness
2. Efficiency
3. Policy Fit
4. Minimization of Economic Impacts
5. Revenue Quality
6. Legislative Authority

The assessment of a potential hotel tax was determined to have a "medium" ranking under the first four of the above criteria, a "low" ranking for revenue quality (less than $50 million) and low for legislative authority, which has now been rectified.

In order to avoid long-term impacts on hotel supply in Toronto, the report proposed that hotels be taxed at a rate not more than two percentage points higher than the effective rate currently being collected by the Greater Toronto Hotel Association for the voluntary Destination Marketing Program (or "DMP") (i.e. 2.66%).

It was also proposed that if the City is going to impose a tax on hotels, it ought to also implement a comparable tax on short-term rentals in order to avoid distorting the existing competitive tension between the two forms of lodging. Industry stakeholders believe that short-term rentals already benefit from a number of competitive advantages that are difficult to overcome, such as paying lower residential property tax rates relative to commercial properties, kitchen access, and no HST requirement when annual sales do not exceed a prescribed threshold.

In a Revenue Options Study submitted to the Executive Committee in June 2016 as part of the staff report titled "Updated Assessment of Revenue Options under the City of

Toronto Act, 2006" (EX16.3), KPMG estimated that a 4% City hotel tax could raise approximately $40 million annually, of which approximately half would be used to replace the up to $20 million of the existing voluntary Destination Marketing Program funding to Tourism Toronto, and leave $20 million in net new annual revenue to the City, assuming the Province continues its $10 million annual grant to the Regional Tourism Organization 5 (Tourism Toronto).

Similarly, a 4% tax on lodging applied to short-term rentals was estimated to generate approximately $1 million to $3 million annually, based on recent statistics on industry activity.

Subsequently, the staff report EX20.2 titled 'The City of Toronto's Immediate and Longer-Term Revenue Strategy Direction' adopted with amendment by Council on December 13, 2016 indicated that it would be impractical to collect a short-term rental tax directly on the individual residential units scattered throughout the City at approximately 10,000 locations and growing (versus a total of approximately 200 hotel locations). These units may only be rented intermittently, so each location or owner may be associated with relatively low dollar values. Collection and compliance costs would be high. Therefore, the report suggested that the City should seek arrangements to collect the tax through short-term rental companies such as Airbnb, rather than from individual units, as has been done in some jurisdictions, such as Quebec.

2. Provincial Legislation to Enable Municipal Accommodation Tax

The authority to implement a Municipal Accommodation Tax is enabled by provincial legislative amendments to COTA and the Municipal Act. COTA was amended to add transient lodging to the list of activities excluded from the prohibition on sales taxes, joining taxes on tobacco, alcohol products and amusement/entertainment entrance fees as permitted sales taxes. The Municipal Act was amended to allow single and lower tier municipalities the option of this tax as well.

The amendments were introduced as part of the 2017/18 Provincial Budget and received Royal Assent on May 17, 2017. Proclamation of the relevant sections was delayed until the fall pending establishment of provincial regulations pertaining to the obligation to share municipal tax proceeds with Regional Tourism Organizations (RTO) and eligible tourism entities.

On November 23, 2017 the Province issued Ontario Regulation 436/17 Transient Accommodation Tax, which came to force on December 1, 2017, the same the day the amendment to COTA which authorized this tax (section 5 of Schedule 4 to the *Stronger Healthier Ontario Act (Budget Measures), 2017*) came into force.

The final regulation is the result of the province's consultation with municipalities and the tourism industry on the draft regulation which related to the Sharing of Revenues from Transient Accommodation Tax with eligible tourism organizations.

There are two versions of the regulation – Ont. Reg 436/17 that is made under the *City of Toronto Act, 2006* (COTA), and 435/17 made under the *Municipal Act* for all other single-tier and lower-tier Ontario municipalities.

2.1 Tax Sharing Formula for Toronto

The regulation prescribes a formula for sharing the tax revenue with the regional tourist organization (Tourism Toronto or RTO5 in the case of the City of Toronto) which incorporates the following elements:

2.1.1 Floor Transfer Amount

The formula establishes a minimum annual transfer amount to Tourism Toronto based on the amount collected under the DMP (by the Greater Toronto Hotel Association) in the last fiscal year (2017) that ended before the tax comes into effect (2018) and that was received by Tourism Toronto under the DMP in the same year (the "floor").

2.1.2 First Year Transfer Amount

In the first year of implementation (2018), the transfer amount will be based on the floor amount but there may be adjustments for the following:

- Where the tax is implemented for a partial year, the transfer amount shall be prorated by the number of days that the tax is in effect in the fiscal year.

- If DMP continues to be collected by the Greater Toronto Hotel Association for some period of time after the implementation of the tax, the transfer amount shall be reduced by the amount of DMP revenues collected during this overlapping period

2.1.3 Transfers in Year 2 and Beyond

Starting in year two, the amount paid to Tourism Toronto will be the greater of:

- the floor amount
  or
- the previous year's transfer amount adjusted using an index based on a ten-year average of the annual change in Ontario's total tourism receipts

2.2 Other Key Features of the Regulation

Other key features of the Regulation are:

- Purchase of short-term accommodation at a university, college or post-secondary institution will be exempt from the tax.
- Tourism Toronto shall provide the DMP receipt information at the City's written request for the purpose of the revenue sharing formula.

- The City shall pay tax revenues to Tourism Toronto within 60 days of the end of the fiscal year, provided the latter has complied with the above request.

- The City shall enter into an agreement with Tourism Toronto respecting reasonable financial accountability to ensure the amounts paid to Tourism Toronto is for the exclusive purpose of promoting tourism, which includes the development of tourism products.

- A provider of transient accommodation in the City that is required to collect the tax shall include on every invoice or receipt the amount of tax on transient accommodation, and the amount shall be identified as "Municipal Accommodation Tax" or "Toronto Accommodation Tax".

2.3 Tax Sharing Requirements for Other Municipalities

For other Ontario municipalities where no formal DMP exists, the Regulation requires that at least 50% from the tax less the municipalities' reasonable costs of collecting and administering the tax must be shared with an eligible tourism organization.

3. Required Tax Revenue Transfers

3.1 Transfers to Tourism Toronto

3.1.1 Amount to be transferred

As discussed above, one of the key elements of the proposed regulation is a guaranteed, municipal contribution to Tourism Toronto, subject only to a sufficient amount of MAT being collected. This amount will be based on the amount transferred to Tourism Toronto in 2017.

The Greater Toronto Hotel Association (GTHA) has been funding its contributions to Tourism Toronto using funds that have been collected through its DMP. The DMP collections were based on 2.66% (plus HST) of the room revenues generated in participating hotels. Table 3 below provides a summary of the amounts recently transferred to Tourism Toronto by the Greater Toronto Hotel Association.

Table 3 — Summary of GTHA funding for Tourism Toronto 2014-2017 ($Million)

	2014	2015	2016	2017 budget	2017 proj. year-end
Greater Toronto Hotel Association's DMP funding provided to Tourism Toronto	17.6	19.0	22.0	22.0	from 22.0 to 25.0

Source: All years except 2017 projected year-end -- Tourism Toronto's 2017 Business Plan and Budget; Tourism Toronto's 2016 audited financial statement
2017 projected year-end -- City staff estimate

The 2017 actual figure will not be known until Tourism Toronto data has been received. Based on an assumed implementation date of April 1, 2018, it is estimated that the City's 2018 contribution amount will range from $16.5 million to $18.8 million**,** prorated for nine months of the year, as indicated in Table 2.

3.1.2 Requirement to Enter into Agreement

Ontario Regulation 436/17 requires that the City of Toronto and Tourism Toronto enter into an agreement regarding, but not limited to, reasonable financial accountability matters in order to ensure that amounts paid to Tourism Toronto are used for the exclusive purpose of promoting tourism.

This report recommends that the Acting Chief Financial Officer, in consultation with the City Solicitor, be directed to enter into an agreement with Tourism Toronto respecting the financial accountability required to ensure that all MAT amounts paid to Tourism Toronto by the City are used for the exclusive purpose of promoting tourism as required by Ontario Regulation 436/17.

3.1.3 Fairness in Municipal Contributions to Tourism Toronto

Although Tourism Toronto acts as a destination marketing organization for Mississauga and Brampton as well as for Toronto, only a limited number of hotels in Mississauga and Brampton currently provide DMP contributions to Tourism Toronto. As a result, if Mississauga and/or Brampton were to implement a MAT, they may be able to retain a larger share of the MAT revenue generated, while still benefiting from the services of Tourism Toronto.

This report recommends that the General Manager of Economic Development & Culture be directed to report back by the second quarter of 2019 on a review of the geographical boundary serviced by Tourism Toronto (Regional Tourism Organization 5 - RTO5) respecting municipal contributions to Tourism Toronto.

3.2 Harmonized Sales Tax

The current system of DMP collections from hotels is subject to HST. The DMP is calculated at 2.66% of the room charges, or 3% including HST. Any new municipal accommodation tax would also be subject to HST unless the Federal government agrees to pass a regulation listing the tax as exempt, as was done in regard to the City's Municipal Land Transfer Tax. Such a designation by the Federal government would eliminate a tax on tax, which despite its nominal cost, can be a major public irritant. Accordingly, it is recommended that the City seek the appropriate changes from the Federal Government to exempt municipal accommodation taxes from HST.

4. New Regulations for Short-Term Rentals

On December 7, 2017, Council adopted, with amendments, zoning changes (PG24.8) and a licensing and registration program for short-term rentals in Toronto (LS23.1).

The elements of these regulations that will have the most important impacts on the potential implementation of a tax on short-term rentals are:

- Short-term rentals across the city will only be permitted in the principal residence of any owner or tenant.

- A Secondary Suite can be used as a short-term rental, if it is exclusively and separately occupied as a principal residence.

- Anyone who operates a short-term rental in their home will be required to register with the City and companies that facilitate short-term rental activity, like Airbnb, will have to be licensed.

As a result, the forecast tax revenue will be lower than that estimated before the new regulation and licensing regime was adopted.

5. Public and Stakeholder Consultations

Public consultations were carried out across the City in December 2016 on the City's Long Term Financial Direction. These consultations included discussion of various revenue options such as a hotel tax. Both the general public and industry stakeholders were invited to these meetings. The majority of the public respondents (65%) supported a hotel tax as a revenue tool, while 22% of the respondents were undecided, and 13% found it unacceptable.

During the consultations on the short-term rental regulations led by Municipal Licensing and Standards and City Planning in the summer of 2017, the public and industry stakeholders (e.g. operators and companies like Airbnb) were also consulted on a potential short-term rental tax, including an 'appropriate' tax rate that may range from zero to 10%. Some of the responses were:

- short-term rentals should contribute to City revenue;
- the tax rate on short-term rentals should be the same as the rate on hotels to level the playing field; and
- there was no justification for a 10% short-term rental tax for properties that might be designated as principal residences.

6. Tax Implementation Steps

COTA requires that Council enact a tax by-law for any new tax implemented under COTA's Part X taxation provisions, which by law is required to contain a description of the subject of the tax, the applicable rates, and the manner of collection of the tax, including the identification of any agent responsible for collection.

COTA also permits the City to require persons or entities to collect the tax as agents of the City, and to enter into voluntary agreements with third parties to collect the tax on the City's behalf.
The MAT will apply to the rental fees paid by transient accommodation guests. The seller of the service, typically the hotel proprietor or its agent, or the short-term rental operator or short-term rental company, will be required to collect the tax from the guests and remit it within specified timeframes to the City.

In respect of the MAT-Hotel, it is recommended that the City retain the Greater Toronto Hotel Association as its collection agent for a two year period. This report recommends that the City enter into a service agreement with the Greater Toronto Hotel Association for such collection services in accordance with the terms in Attachment 2.

A transition period of 60 days is required for the effective implementation of the tax in order to allow hotels to exit the DMP program (i.e. terminate the DMP agreements with Greater Toronto Hotel Association) and program billing systems, and for the City to implement the collection agreement with Greater Toronto Hotel Association. Accordingly, it is recommended that the MAT-Hotel be implemented effective April 1, 2018.

It is also recommended that the Acting Chief Financial Officer be authorized to enter into agreements for the collection and remittance of MAT-STR with City-licensed short term rental companies that collect fees on behalf of short-term rentals operators on their platform.

7. Tax Design Considerations

The Municipal Accommodation Tax will be the City's first sales tax. Sales taxes are paid by the buyer of the service, in this case, the guest at a hotel or short-term rental. The by-law will require that the seller - the hotel operator or operator of the short-term rental - collect and periodically remit the tax to the City.

Different design considerations will need to be taken into account in applying the tax to hotels and to short-term rentals. These specific considerations are discussed further below.

7.1 Application of Tax to Hotels

7.1.1 Types of Accommodation to be Taxed

As with any tax design, it is desirable to treat similar activities in the same manner. For the purposes of this component of the tax, staff propose to include most non-residential properties which are rented out for transient accommodation purposes. This will include clubs, hostels, condo hotels and service clubs. The full list of accommodation to be included is set out in Attachment 1.

The tax will only apply to rooms defined under the current Greater Toronto Hotel Association Destination Marketing Program as "sleeping rooms" and not to rooms rented for meeting or conference hospitality purposes.

Some forms of transient accommodation would not be subject to the tax. Summer camps, for example, where overnight stays are part of the programming, would not be taxed. As well, short-term shelter accommodation provided by City or its agencies at contracted hotels or motels are not taxed. These kinds of activities are often consistent with City program objectives (youth services, shelter housing) and in any case do not operate in the same market as hotels. Other exempted types of transient accommodation include: treatment centres receiving Provincial aid under the Ministry of

Community and Social Services Act, halfway houses, tent or trailer sites at campgrounds, and employee accommodation supplied and operated by the employer.

Bed and Breakfasts are required by the zoning bylaw to operate from an operator's principal residence and would therefore be treated as a short-term rental rather than as a hotel. Accordingly, bed and breakfast operators will be required to collect the MAT-STR rather than the MAT-Hotel.

Exemptions will be provided to all transactions involving entities listed in section 268 of COTA, which provides that the Crown and various provincially affiliated entities cannot be taxed by the City. Entities may also be exempted by regulation. For example, university residences operating as transient accommodation outside of the school year are excluded from the applicability of the tax.

7.1.2 Types of Charges to be Taxed

The City's by-law will specify the charges that are included in the taxable costs as per Attachment 1, but for clarity, charges for ancillary services related to a hotel stay are excluded from the tax, such as room service, mini bar use, internet, food, and phone charges, provided they are itemized separately on the bill. Where such charges are not itemized separately on the bill, the tax will apply to the full amount of the bill.

7.1.3 Duration of Accommodation to be Taxed

The proposed tax would apply for continuous stays of 30 days or fewer. This term would result in consistency with the HST rules, which applies to stays of 30 days or fewer. Longer stays are effectively considered long term rental under the HST rules, and are not taxed. The hotel industry is in favour of the City's tax being on the same basis as the HST, to simplify implementation and ongoing administration. Note that the City's new zoning bylaw amendments and licensing and registration system related to short-term rentals apply to rentals of less than 28 days, which is different from above.

Rentals may also occur for periods shorter than the typical daily rate. The by-law would impose accommodation tax for any contracted stay of four hours or longer, again consistent with the application of HST.

Hotels already track and report these revenue types for DMP purposes, and others not part of the DMP would track them for various management accounting purposes.

7.2 Application of Tax to Short-Term Rentals

7.2.1 Tax Rate

As discussed in the City's Immediate and Longer-Term Revenue Strategy Direction report, industry stakeholders believe that short-term rentals currently benefit from a number of competitive advantages such as paying lower residential property tax rates relative to commercial properties, kitchen access, and no HST requirement on the operator when his/her annual income from short-term rentals does not exceed a prescribed threshold.

However, by restricting short-term rentals to principal residences, the regulations adopted by Council in December 2017 will eliminate investor-operated short-term rental accommodations that would compete directly with the hotel industry.

Consequently, once the regulations come into effect short-term rentals will only serve to generate supplementary income for homeowners from under-utilized portions of their own residences.

Council directed staff to report back on a recommended tax rate for short-term rentals that is no higher than 10%. Staff propose that a tax rate of 4%, equal to the tax rate on hotels, would bring a reasonable degree of parity between hotel and short-term rental accommodation. A tax rate closer to 10% may be perceived as punitive on these homeowners, act as a disincentive to comply with regulations, and potentially drive them into the underground market.

Other Canadian jurisdictions that have recently implemented or are considering implementing a short-term rental tax have considered tax rates ranging from 3% to 4%. Effective October 1, 2017, the Province of Quebec have signed an agreement with Airbnb to collect a 3.5% short-term rental tax on behalf of operators in the province. The City of Vancouver is considering the option of applying a transaction fee no higher than 3% of booking prices which would be remitted to the City of Vancouver. (Vancouver does not currently have the legislative authority to impose a municipal sales tax). Other Ontario cities which are in the process of introducing a municipal accommodation tax in 2018 – Ottawa and Mississauga – both adopted a tax rate of 4%.

7.2.2 Types of Accommodation to be Taxed

This report recommends that the tax apply to all accommodations defined in the short-term rentals in the proposed short-term rental by-law. A short-term rental is defined as all or part of a dwelling unit in the City of Toronto used to provide sleeping accommodation for any rental period that is less than 28 consecutive days in exchange for payment. This includes existing bed and breakfasts and excludes hotels and motels and accommodations where there is no payment.

7.2.3 Types of Charges to be Taxed

The charges to be taxed would be the same as for hotels.

7.2.4 Duration of Accommodation to be Taxed

Staff recommend an eligible transaction definition of less than 28 days for the short term rental regulatory framework, to align with the short-term rental bylaw, and this definition would apply to short-term rental activities if the City elects to impose a MAT-STR.

8. Collection

Sales taxes are calculated, imposed, collected and remitted by the seller, in accordance with the law. Accordingly after adopting a by-law imposing a sales tax on transient accommodations, the City is required to sufficiently communicate the terms of the tax, and provide channels for periodic reporting and remittance. Revenue Services Division staff have indicated that a substantial amount of time will be required to organize resources in order to take these steps and implement a new sales tax.

Different approaches towards collection will be applied towards the hotel and short-rental components of the proposed tax. These approaches are described below.

8.1 Collection from Hotels

Section 271 of COTA provides that the City may enter into agreements with another person or entity, to provide for the collection of taxes imposed under section 267 of COTA and for the administration and enforcement of the by-law imposing the taxes. Therefore, a number of options have been considered for Hotel Tax collection, including using a third party collection agent such as the Greater Toronto Hotel Association or the Canada Revenue Agency ("CRA").

The CRA was contacted to determine whether they would be able to provide collection administration and audit services for the MAT-Hotel, as an extension of their current HST activities. A potential benefit of using the CRA for this service was that HST records could be used in the validation of the revenue amounts reported by hotels.

However, the CRA has indicated that a realistic timeframe for their implementation of the MAT-Hotel collection on behalf of the City would be approximately two years. Also, staff have concluded that the revenues reported for HST payment are not sufficiently matched to the revenues that would be used for determining the MAT-Hotel amounts (because the revenues reported for HST would potentially include non-accommodation revenues such as charges for ancillary services). Therefore, staff would not be able to verify the MAT-Hotel collected by matching it to the HST collected by the same hotel establishment.

Staff have instead determined that the best third-party option would be to enter into an agreement with the Greater Toronto Hotel Association (GTHA). The GTHA is currently managing the collection of the DMP, which has a similar structure to the proposed MAT-Hotel (i.e. it is based on reported hotel room revenue). The GTHA already has audit and registry data base systems that would enable the City to have a more orderly and speedy implementation of the tax. The City of Ottawa has entered into a similar arrangement with their local hotel association.

The hotels will need to make relatively modest adjustments in order to ensure that the tax is applied in accordance with the by-law. The tax has been designed to mirror existing HST and DMP processes to the extent possible. Nevertheless the affected parties require sufficient time to program collection procedures and implement tracking reporting and remittance procedures. The hotel tax also requires the orderly unwinding of the DMP, with its attendant collection contracts with the Greater Toronto Hotel Association. In preliminary discussions with the head of the Greater Toronto Hotel Association, it is believed that if Council adopts the tax as recommended at its meeting on January 31- Feb 2, 2018, the tax could be implemented effective April 1, 2018.

Table 4 below compares the two collection options, namely the use of the Greater Toronto Hotel Association as a collection agency, versus using the City's own resources:

Table 4 — Collection Options: Greater Toronto Hotel Association vs City

	Greater Toronto Hotel Association	**City**
Annual Cost	Under $1 million	Under $1 million
Earliest Effective Date	April 1, 2018	June 1, 2018
Communications with Remitters	Greater Toronto Hotel Association	City
Audit Systems	Existing subcontract, subject to modification	RFP to purchase service
Hotel Operator Database	Existing, subject to augmentation	To be developed

Consequently, staff are recommending that authority be granted to enter into an agreement with the Greater Toronto Hotel Association for an initial term of two years, with an option to renew annually for a further two one-year periods, in accordance with the terms in Attachment 2. The City will assess and evaluate its collection options before the expiry of the first term of the collection agreement.

8.2 Collection from Short-Term Rentals

8.2.1 Collection from Short-Term Rental Companies

This report recommends that the bulk of the MAT-STR revenue also be collected through third-parties, where possible.

As discussed in greater depth in LS23.1 Licensing and Registration Regulations for Short-term Rentals, it is likely that the majority of short-term rentals are arranged through short-term rental companies such as Airbnb. These companies collect room rental payments from buyers on behalf of the operators.

Currently, the primary approach used by other jurisdictions to collect occupancy taxes on short-term rentals has been to enter into collection agreements with these companies or imposing legal obligations on the companies to collect the tax. Given the on-line nature of the business there may be jurisdictional issues in enforcing any obligations to collect imposed on short-term rental companies by law. The voluntary collection agreements are recommended as they are used in the vast majority of other jurisdictions that impose similar accommodation taxes and allow for efficient collection by short-term rental companies. Many U.S. jurisdictions, such as Chicago, San

Francisco, Philadelphia, and New Orleans have signed a voluntary collection agreement with Airbnb to retain it for the collection and remittance of the tax on short-term rentals.

This report recommends that the City enter into a tax collection agreement with all willing STR companies that collect rental fees on behalf of short-tern rental operators using their platform, for the purpose of engaging the STR companies to collect the MAT-STR on behalf of the City in respect of those operators. This approach will result in the efficient collection of the tax from the large number of operators currently providing short-term rental accommodation through an internet platform. Attachment 3 sets out the proposed terms of an agreement between the City and a short-term rental company for the purpose of collecting and remitting the MAT-STR to the City on behalf of the operators associated with the company.

Under the terms of this agreement, the companies would have the following principal responsibilities:

- Collecting the MAT-STR directly from guests at the time that accommodation fees are collected through their platform
- Notification of operators and guests of the City's tax requirements and how such taxes will collected at the same time as the fees
- The reporting to the City of aggregate tax revenues collected each month
- The monthly remittance to the City of tax revenues that have been collected

The companies would be subject to penalties for late or incomplete reporting and to compliance audits to verify remittance of all taxes that have been collected.

This report recommends that the Short-Term Rental By-law include a provision establishing that all information collected in accordance with that by-law is collected for the purposes of the administration and enforcement of both that by-law and the MAT-STR by-law. This will include a provision that the operators are required to maintain transaction records that include information on the nightly price charged, in addition to the number of nights rented, for the applicable short term rental, and to provide this information to Municipal Licensing and Standards upon request. This will allow staff to conduct a reasonableness check on the amounts of tax remitted.

8.2.2 Collection Directly from Short-Term Rental Operators

Collection from operators that do not make use of short-term rental companies, and from operators who use STR companies who have not entered into a collection agreement with the City, will be carried out by Revenue Services Division. Staff may make use of the short-term rental operator registry, which is managed by Municipal Licensing and Standards, as required.

Individual operators would be subject to penalties for late or incomplete reporting as described in Attachment 1 of this report. However, it is anticipated that challenges will still exist with the enforcement of accurate revenue reporting by these unaffiliated operators. The extent to which expenditures on detailed auditing will be necessary to maintain compliance is uncertain.

9. Updated Financial Estimates:

9.1 Revenue Forecast

The revenue estimates for both MAT-Hotel and MAT-STR are shown below, based on the most recent data and a number of assumptions.

9.1.1 MAT-Hotel Revenue Forecast:

One of the key assumptions in estimating hotel tax revenue is that the number of rooms continues to remain stable, as it has over the past ten years, based on a report by the General Manager of Economic Development and Culture on Ensuring a Robust Supply to Strengthen Tourism.

Table 5 below shows the gross tax revenue potential based on average occupancy and average daily rates of Toronto hotels with an estimated 25,281 rooms. The gross revenue is reduced by price elasticity and avoidance factors based on the methodology as outlined in KPMG's June 2016 Revenue Options Study. The resulting gross revenues if a 4% tax was imposed on hotels in 2015 and 2016 are estimated at $41.4 million and $48.0 million respectively.

Table 5 — MAT-Hotel Gross Revenue Estimate

	2016	**2015**
Number of hotel rooms in city of Toronto *	25,281	25,281
Average occupancy *	75%	72%
Number of room nights sold per year	6,929,901	6,616,164
Average Daily Rate (ADR) *	$183.5	$166.1
Total hotel revenue ($M)	$1,271.78	$1,099.21
Tax Revenue potential:	$Million	
MAT-Hotel @4%	$50.9	$44.0
Price Elasticity Reduction	-$2.0	-$1.8
Avoidance Deduction	-$0.9	-$0.8
Annual Revenue Potential (Gross)	$48.0	$41.4

* Data Source: Economic Development and Culture Division / CBRE

9.1.2 MAT-STR Revenue Forecast:

There is limited data for short-term rental activities in Toronto. Data from Airbnb and VRBO indicated that there were approximately one million room nights booked in 2016, and assuming 50% of those are booked in principal residences, rented at an average daily rate of $100, a 4% sales tax would generate an annual tax revenue of $2 million. Airbnb estimated that for the 12-month period from October 1, 2016 to September 30, 2017, a 4% tax on all short-term rentals booked through the platform would generate $5.1 million. Hence staff estimated that a 4% tax would generate a range of $2 million to $3 million annually. If the tax is implemented part-year, effective June 1, 2018, the gross revenue potential is estimated to be $1.2 million to $1.7 million in 2018.

9.1.3 Revenue-Sharing with Tourism Toronto

As discussed in section 3.1.1, the provincial regulation requires the City to share its MAT revenue with Tourism Toronto, at a minimum amount of the actual DMP fees received from the Greater Toronto Hotel Association in 2017 (the "floor"), which is estimated at a range of $22 million to $25 million. For illustration purposes, if the MAT-Hotel is effective April 1, 2018, the floor would be prorated to $16.5 million to $18.8 million in 2018. However, the actual figure will depend on the actual amount of DMP collections and received by Tourism Toronto in 2017, which may not be known until well after the year end.

9.2 Administration and Collection Costs

The City's Revenue Services Division will be responsible for the administration and reporting of the MAT-Hotel and MAT-STR, if implemented. The City's total costs of implementation and ongoing administration and collections, including audit, will vary depending on whether the City collects the MAT using its own resources and systems, or whether the City employs the Greater Toronto Hotel Association as the City's collection agent, to take advantage of the GTHA's experience, existing collection pathways, forms and agreements and database of hotels currently participating in the DMP.

This report recommends that the City enter into an agreement with the Greater Toronto Hotel Association to act as its collection agent for MAT-Hotel at a cost not to exceed $225,000 in 2018 if implemented effective April 1, 2018, and 265,050 in 2019. Under this scenario, Revenue Services staff have estimated that the City's costs will require 1.5 full-time staff positions, and up to $222,000 in 2018 (over and above the Greater Toronto Hotel Association's fees), and annual costs will be approximately $296,000. Costs for auditing hotels will be in addition to these estimates and subject to discussions with the Greater Toronto Hotel Association.

For the administration and collections related to MAT-STR, it is believed that utilizing an external collection agent (through a voluntary agreement with a short-term rental company, e.g. Airbnb) at no cost to the City will result in efficiencies in administration. Depending on how a MAT-STR is applied, the City's costs to administer and report on taxes collected can be expected to comprise primarily salaries and benefits for 2 full-time staff positions, with costs estimated at up to $200,000 per year. If the MAT-STR is implemented effective June 1, 2018, the City's 2018 cost would be approximately $120,000.

In summary, the total collection/administrative costs are estimated to be $567,000 in 2018 and $761,050 on an annual basis, as in Table 6 below:

Table 6 - Summary of Collection /Administrative Costs			**Full-time positions**	**2018**	**2019 / annual**
MAT-Hotel					
	Greater Toronto Hotel Association				
		One-time set up costs		25,900	na
		On-going costs		199,100	265,050
	Total Greater Toronto Hotel Association		n/a	225,000	265,050
	Office of the Treasurer (Revenue Services)		1.5	222,000	296,000
	Total MAT-Hotel			**447,000**	**561,050**
MAT-STR					
	Office of the Treasurer (Revenue Services)		2.0	**120,000**	**200,000**
Total MAT			**3.5**	**$567,000**	**$761,050**

* Implementation dates assumed to be April 1, 2018 for MAT-Hotel and June 1, 2018 for MAT-STR

All costs for collection and administration of the tax will be funded from the tax proceeds. The net revenue estimate for MAT, after sharing with Tourism Toronto in accordance with the provincial regulation, is estimated to be ranging from $17.2 million to $28.2 million annually, and $14.6 million to $23.0 million in 2018 if the MAT-Hotel is implemented on April 1, 2018, and the MAT-STR is implemented on June 1, 2018.

Table 7 below summarizes the gross and net revenue estimates.

Table 7 - Forecast of Municipal Accommodation Tax Revenue ($millions)		
	2018*	**Annualized**
Gross Revenues		
MAT-Hotel	32.8 to 38.4	41.0 to 48.0
MAT-STR	1.2 to 1.7	2.0 to 3.0
	34.0 to 40.1	43.0 to 51.0
Payment To Tourism Toronto	**-16.5 to -18.8**	**-22.0 to -25.0**
MAT after payment to Tourism Toronto	**15.2 to 23.6**	**18.0 to 29.0**
Administration Costs		
MAT-Hotel	-0.5	-0.6
MAT-STR	-0.1	-0.2
Net Revenues	**14.6 to 23.0**	**17.2 to 28.2**

* Implementation dates assumed to be April 1, 2018 for MAT-Hotel and June 1, 2018 for MAT-STR

A preliminary operating budget for 2018 for MAT was estimated prior to the release of the Provincial regulation respecting revenue sharing with Tourism Toronto, at $37.0 million gross, and $16.1 million net (with $20.0 million payment to Tourism Toronto, and $0.9 million in associated costs)

It is recommended that the 2018 operating budget be amended to reflect the most recent gross revenue and cost estimates**.** These updated numbers are within the range of the estimates as contained in Table 7 above.

Revised Recommended 2018 Operating Budget		
Gross MAT revenue	**$**	**34,667,000**
Payment to Tourism Toronto		18,000,000
Admin Costs:		
Greater Toronto Hotel Association		225,000
Office of the Treasurer (Revenue Services): 3.5 full-time positions		342,000
Net MAT Revenue	**$**	**16,100,000**

10. Revenue Allocation

When City Council endorsed the creation of a hotel and short-term rental tax in its deliberation of the 2017 Operating and Capital Budget, it also directed staff to report back on a revenue allocation policy.

Staff propose that the MAT proceeds be directed to general non-program revenues. This is in accordance with the approach taken with the Municipal Land Transfer Tax, Personal Vehicle Tax (though subsequently repealed), and Third-Party Sign Tax. The net proceeds of these taxes have been directed to general corporate revenues, i.e. non-program revenues, and applied towards areas where expenditure requirements are the highest. This approach is considered more flexible than earmarking revenues as it provides the maximum benefit to programs where funding is needed most.

11. Other Ontario Cities Implementing a Transient Accommodation Tax

City of Ottawa

The Ottawa Gatineau Hotel Association (OGHA) administered a voluntary 3% Destination Marketing Fee in conjunction with Ottawa Tourism and hoteliers in Ottawa until the end of 2017, which is similar to the arrangement in Toronto where Greater Toronto Hotel Association administers a voluntary DMP on behalf of local hotels. Approximately 50% of the hotels in Ottawa, representing about 90% of the hotel room stock, had an agreement with OGHA which expired on December 31, 2017.

On December 12, 2017 Ottawa City Council approved a mandatory 4% Municipal Accommodation Tax effective January 1, 2018, with a two-month transitional period. The City will provide revenue proceeds to Ottawa Tourism as prescribed by Ontario regulation 435/17, for services and activities supporting the promotion and development of tourism to Ottawa, in an amount that is the same as what was received in 2017 through the DMP before the tax came into effect.

The City of Ottawa has entered into an agreement with OGHA to use it as the collection agent for MAT, in a way similar to what this report recommends using the Greater Toronto Hotel Association as Toronto's collection agent for MAT-Hotel.

City of Mississauga

On November 8, 2017, the City of Mississauga approved the introduction of a transient accommodation tax at the rate of 4% (consistent with Toronto's rate due to the proximity of the two cities), to be effective July 1, 2018. A consistent rate between the two cities would ensure local hotels will continue to be competitive.

With 7,500 hotel rooms, an average occupancy rate of 64% and average daily rate of $140, a 4% tax would generate $9.8 million annually. In accordance with provincial requirements, a portion of the revenue would be provided to Tourism Toronto, which covers the cities of Toronto, Mississauga and Brampton (as RTO5). The staff report proposed that the city's portion of the revenue could be used to support tourism-related capital expenditures, and programs and services including recreation, culture, parks and forestry and economic development.

The report also suggested that the city would be able to undertake the administration of the tax within existing resources using a simplified remittance model, similar to that used by businesses to remit GST/HST to the Canada Revenue Agency.

A final report is expected to go to General Committee on January 17, 2018 and Council on January 24, 2018.

12. Conclusion

Following the presentation to Council of the Long-Term Revenue Strategy Direction report in 2016, the overall outlook for the MAT has been impacted by:

- Recommended changes to the City's zoning and licensing by-laws related to short-term rentals
- Revenue-sharing terms in the Provincial Regulation
- A voluntary offer by Airbnb to collect tax revenues on behalf of the City

This report provides an assessment of the impact of these changes as well as recommended specific tax design features and revenue allocation, and seeks required implementation authorities.

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ATTACHMENTS

Attachment 1 - Administrative Design Features for the Municipal Accommodation Tax (MAT)

- Attachment 1A - Additional Administrative Design Features for Municipal Accommodation tax - Hotel (MAT-Hotel)

- Attachment 1B - Additional Administrative Design Features for Municipal Accommodation Tax - Short-Term Rentals (MAT-STR)

Attachment 2 - Key Terms of Collection Agreement between the City of Toronto and Greater Toronto Hotel Association

Attachment 3 - Key Terms of Collection Agreement between the City of Toronto and Short-Term Rental Company