TORONTO

REPORT FOR ACTION

Additional Property Tax and Legislative Change Options to Support Businesses

Date: July 6, 2018
To: Executive Committee
From: Interim Chief Financial Officer
Wards: All

SUMMARY

In January 2018, Council, in adopting Item EX30.5: *Tax Policy Tools to Support Businesses,* adopted a series of tax policy recommendations for 2018. In its consideration of this item, Council also directed the Interim Chief Financial Officer to engage in broad public consultations to review additional property tax options for 2019 and future years, as well as any potential requests for legislative change for such options, and report to the July 17, 2018 meeting of Executive Committee.

In response to this direction, a number of City divisions worked collaboratively to design, prepare and deliver a series of in-person public consultation sessions, as well as an online survey, that were conducted over the course of April to June of 2018. The feedback and information received from the various consultation sessions and online survey form the basis of this report.

This report also identifies eight considerations for the incoming Council to evaluate in establishing tax policies for 2019 and beyond, as supported by the results of the City's consultations. City staff will continue discussions with Provincial staff and staff of the Municipal Property Assessment Corporation (MPAC) over the remainder of 2018 where legislative or regulatory amendments or changes in practice have been identified that may affect tax policy options or decisions.

RECOMMENDATIONS

The Interim Chief Financial Officer recommends that:

1. Executive Committee receive this report for information.

FINANCIAL IMPACT

There are no financial implications arising from the recommendations in this report.

DECISION HISTORY

At its meeting of December 5, 2017, City Council adopted Item MM35.16: *Saving Toronto's Small Businesses and Character Streets with Intelligent Tax Reform*, directing the Interim Chief Financial Officer to undertake a review of various tax policy tools that can be used to provide relief to small business owners facing unsustainable Current Value Assessment-related tax increases, and to report back to a future meeting of the Executive Committee with recommendations on which tool(s) would most effectively achieve this. This item is available at:
Saving Toronto's Small Businesses and Character Streets with Intelligent Tax Reform

At its meeting of January 31, 2018, City Council adopted EX30.5: *Tax Policy Tools to Support Businesses*, with amendments. This report recommended the adoption of tax policy options for 2018, including that tax increases within the commercial, industrial and multi-residential tax classes be limited to 10% of the previous year's annualized taxes; and that these capping limits apply to all properties within these classes, regardless of whether the property had reached its full Current Value Assessment-level of taxation in a prior year.

In its consideration of this item, Council also directed the Interim Chief Financial Officer to engage in broad public consultations to review additional property tax options for 2019 and future years, as well as any potential requests for legislative change for such options, and report to the July 17, 2018 meeting of Executive Committee. Council's decision is available at: EX30.5: Tax Policy Tools to Support Businesses

Subsequently, Council adopted tax rates, education rates and claw-back rates and other tax policy decisions for the 2018 taxation year by its adoption of the following items: EX31.1: 2018 Property Tax Rates and Related Matters and EX33.11: 2018 Education Tax Levy and Clawback Rates.

ISSUE BACKGROUND

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

In 2005, Council adopted the staff report: Final Recommendations - Enhancing Toronto's Business Climate – It's Everybody's Business, which approved, among other things, a long-term strategy to systematically reduce tax rates within the commercial, industrial and multi-residential taxes to 2.5 times the residential rate by 2020 (later changed to 2023 by a 2017 Council decision). In 2007, Council also approved that tax ratio reductions be accelerated for properties in the new Residual Commercial Tax class to reach a target tax ratio of 2.5 times the residential rate by 2015.

Since 2009, Council has also adopted policies to accelerate progress towards full Current Value Assessment (CVA) taxation levels for non-residential properties, by removing properties from the capping and claw-back system once they have reached their full CVA-level of taxation.

In 2017, the province-wide reassessment saw property values re-assessed to reflect a valuation date of January 1, 2016. This resulted in significant reassessment-related property tax increases for many properties and across all property classes in Toronto. These assessment increases will continue to be phased-in by equal increments in each of the taxation years from 2017 to 2020. Media attention in 2017 focused on large reassessment-related property tax increases, citing instances of assessment increases of 100% and more, and included examples such as 401 Richmond Street West, and Yonge Street properties between College and Bloor Street.

Many of the properties experiencing significant tax increases were those properties that had already reached their full CVA-level of taxation, and were therefore ineligible for capping protection in 2017. With no cap on increases, property owners that experienced large reassessment-related increases were faced with large and unmitigated tax increases. In many cases, these tax increases were either passed on to tenants through increased rents, or borne directly by business tenants under net leases. This gave rise to concerns about the impacts on businesses, particularly small independently-owned entities or single tenant proprietorships, and the potential associated impacts on the character and viability of entire neighbourhoods and retail districts.

Council, in adopting tax policies for 2018, took steps to mitigate extraordinary tax increases by limiting tax increases to 10% of the prior year's annualized taxes, and by offering tax capping protection to all non-residential properties, regardless of whether they had reached full CVA taxation levels in a prior year. Viewed as an interim strategy, Council also directed the Interim Chief Financial Officer to engage in broad public consultations to review additional property tax options for 2019 and future years, as well as any potential requests for legislative change to enable such options, and report to the July 17, 2018 meeting of Executive Committee.

This report provides a summary of the results of those public consultations, and highlights some of the key areas of consensus amongst the City's business community, and identifies key considerations that an incoming Council must consider in adopting tax policies for 2019 and beyond.

COMMENTS

Principles for Tax Policy Reform: Scope and Key Assumptions

In preparing for public consultations, it was necessary to first establish the scope and key assumptions that would shape discussions on tax policy reform. These assumptions reflect Council's long-standing directions on property tax policy, and recognize that, while many tax policy decisions fall within Council's authority under the *City of Toronto Act*, other aspects of the taxation system are provincially legislated and apply to all municipalities across Ontario, especially in regards to the assessment of property by the Municipal Property Assessment Corporation (MPAC). As such, the following scope and key assumptions were advanced as the basis for public engagement.

- The scope of tax policy consultations is focused on tax policy approaches for business properties (i.e., properties within the commercial, industrial and multi residential tax classes);

- Toronto suppports the Current Value Assessment (CVA) approach to taxation, recognizing that Ontario's CVA *ad valorem* approach to property assessment, where properties are assessed at market value as a means of distributing the property tax burden, is an internationally accepted best practice in property taxation theory;

- Toronto Council is committed to a long term strategy to reduce business tax rates (vis-à-vis residential rates), consistent with Council's 2005 approval of *Enhancing Toronto's Business Climate - It's Everybody's Business*; and

- Some form of property tax protection for business may continue to be required, given the rapidly accelerating real estate market in Toronto.

Stakeholder Consultations

In response to Council's direction, staff undertook public and stakeholder consultations to gather important feedback on tax policy considerations, and additional property tax tools and options that may be considered for 2019 and future years. The consultation process comprised three phases:

- Meetings with representatives and owners of large commercial and industrial properties, business associations, representatives from the City's Business Improvement Areas, taxation professionals and academia.

- Two in-person public consultation sessions open to all interested parties, held May 22 and 23, 2018. The sessions were advertised on the City's website, in community papers and through a series of social media announcements; and

- An online survey. The online survey was available from May 17, 2018 to June 1, 2018, and garnered 429 individual responses. The survey was advertised on the City's website, in community papers and through a series of social media announcements.

Details of the meeting dates and participants are included in Attachment 3.

A presentation, included as Attachment 1 to this report, was provided at the stakeholder and public consultation sessions, with certain graphs and charts reproduced as part of the online survey. The presentation included a number of open-ended questions designed to gauge participant reaction, identify areas of concurrence, and to generate discussion. Direct Poll, an interactive tool used to conduct a live poll during a presentation, was utilized during each of the two public consultation sessions to record participants' views. Details of the questions and answers received using Direct Poll can be found in Attachment 2 to this report. Further detail on stakeholder feedback from the consultations can be found in Attachment 3 of this report.

Online Survey Results

The online survey was available from May 17, 2018 to June 1, 2018, and included 46 questions. A total of 429 individuals responded to the online survey, of which 210 were completed fully (all questions answered). This represents a 49% completion rate. The online survey was divided into sections, each representing a specific tax policy tool or option. A detailed copy of the survey questions and results can be found in Attachment 4 to this report.

In terms of the survey respondents, of the 429 who completed question 1: 40% identified themselves as an owner; 38% as a tenant; 5% as representative of an owner, tenant or member of a business association; 0.5% as owner or lessor of a business located outside of Toronto; and 16% residents of Toronto who neither own nor lease property for business purposes. Of those stating that they own or lease in Toronto, 76% were commercial properties, 4% industrial and 5% multi-residential. The remaining 14% was comprised of mixed-use property owners or tenants, representatives, retail, and non-profit organizations.

Stakeholder Feedback from Consultations

The results of the stakeholder and public consultation sessions and online survey results served to identify areas of general agreement amongst participants, areas where opinions were divided (e.g., between small and large business owners, or owners vs. tenants), and where uncertainty exists as to whether certain tax policy options will be appropriate at addressing actual impacts on businesses. The results will serve to inform future development of potential tax policy options that will be put forward for Council approval in 2019 and beyond. The following sections summarize key findings.

Should Toronto continue to reduce the difference between tax rates for business properties vs. residential?

This was the single question for which there was near unanimous agreement amongst participants - results from the consultation session suggest 94% of participants agreed with this statement, while the online survey indicated 85% of respondents agreed or strongly agreed with this statement. Fewer than 6% of respondents indicated they disagreed with this statement.

When asked whether Toronto's progress in reducing business tax rates should be accelerated, slowed down or neither (i.e., maintain current target to reach tax ratios of 2.5 by 2023), 93% of session participants and 78% of online survey respondents indicated that process should be accelerated. Additionally, 14%and 7% of participants and survey respondents respectively felt that current targets should be maintained.

Should tax policies be designed to bring properties to full CVA taxation levels?

In its simplest form, Ontario's system of assessment and taxation works on the premise that property tax is calculated by multiplying the CVA of a property by the tax rate for the class. Limits on tax increases and decreases (tax capping and claw-backs), although intended as temporary measures to ease the transition to full CVA taxation levels, have tended to preserve and prolong inequities, in the form of different effective tax rates between properties and property types.

There was no clear consensus on this question. About 54% of participants indicated yes, while 46% indicated no or unsure. For online survey respondents, 27% responded yes, 29% responded no, and 44% of respondents were neutral or unsure. Moreover, when asked*: is fairness achieved when all properties are taxed at full CVA taxation levels?,* 73% of all respondents indicated no or uncertain - only one quarter of respondents answered yes to this statement.

Should protection (limits on allowable increases) be provided to businesses facing large assessment-related increases?

Of the survey respondents, 65% felt that limits on tax increases (tax caps) should be maintained to protect businesses against excessive tax increases due to rising assessment values. Fewer than 10% answered no to this question, while 27% were unsure.

What types of businesses should be protected?

Responses to this question indicated a wide range of opinions, usually reflecting the individual perspective of the respondent. Online survey responses indicated the largest group (39%) felt that small businesses (small streetfront retail) should be protected (but small businesses also accounted for 71% of online survey respondents). A smaller percentage of respondents (17%) felt that capping protection should be offered to only those properties facing large tax increases (i.e., 25% or more), and to multi-residential properties (16%).

Fewer than 5% of respondents felt that capping protection should be applied to the following property types: large office towers, parking lots, large shopping centres, large sports facilities. Coincidentally, these are the same property types that are excluded from the Residual Commercial Tax class (i.e., those property types to which graduated tax rates do not apply).

When asked if capping protection is still necessary once all properties have reached full CVA taxation levels, a small majority (45%) indicated yes, while the remainder indicated no (18%) or unsure (35%).

Limiting tax increases on certain properties creates a shortfall in taxation revenues - how should this shortfall be funded?

Since 1998, caps on tax increases have been funded by withholding (clawing-back) a portion of tax decreases on properties that have experienced assessment-related tax decreases. Participants in public consultation sessions indicated a marked preference

(78%) that capping protection should be funded by increasing tax rates across *all* tax classes (including residential), i.e., a budgetary increase across all classes. For online survey respondents, 39% suggested that capping protection should be funded by increasing rates across all classes.

Surprisingly, 18% of survey respondents felt that funding for tax caps should continue to be funded by withholding a portion of tax decreases from properties experiencing tax decreases (the status quo), while only 11% of respondents suggested that caps on increases should be funded within the tax class, i.e. a rate increase for commercial properties to fund protection for commercial properties experiencing increases.

This question elicited a wide range of written comments, including commentary that questioned whether capping protection should be considered a revenue shortfall, and many comments that suggested that cutting expenditures and reducing inefficiencies in municipal government could offset the costs of funding protection for tax increases. Other comments identified the unfairness of the current claw-back system: *"Claw-backs are not fair - people are losing money on their real estate investment AND being hit with extra taxes, while those who are getting richer off their investments are also getting a tax break."*

Graduated tax rates

Currently, a lower commercial tax rate applies to the first $1 million of assessment, and a higher tax rate applies to any assessment above this amount. Graduated tax rates were adopted to provide some measure of tax relief to lower valued commercial properties. There are approximately 36,400 properties within the Commercial Residual tax class (which excludes large office towers, large shopping centres, parking lots and large sports facilities) that benefit from graduated rates. The tax rate differential between Band 1 (the first $1 million) and Band 2 (assessment over $1 million) rates is approximately 14%.

Specific questions were asked during the consultation regarding whether graduated tax rates within commercial should be continued; if so, what the threshold for Band 1 should be; if limits on tax increases apply, are graduated rates still needed; and whether the differential between Band 1 and Band 2 rates should be increased to provide more benefit to lower valued properties.

The overall consensus of those that participated in the sessions (predominantly large businesses and business associations) is that graduated rates serve little to no purpose, especially with respect to helping tenants or small property owners, and that the difference between the bands is insignificant. About 67% of participants advised they feel the City should discontinue graduated tax rates, especially if limits on tax increases apply. A large majority, at 71%, feel that if continued, the differential between Band 1 and Band 2 rates should not be increased, and a further 83% feel that the threshold should remain at $1 million.

When asked these same questions through the online survey, however, there was a marked difference in whether the City should continue with graduated tax rates. About 80% of online survey respondents feel that graduated tax rates should continue, and furthermore, the bulk of respondents feel that the threshold for Band 1 tax rates should be increased to $2 million. This is not surprising, considering that 77% of the online survey respondents were commercial property owners or tenants, of which over 70% employ under 10 people. This is the very demographic that Council is seeking to protect through tax policy reform.

Protecting Business Tenants

Responses to the question of whether tax policies should be designed to ensure that business tenants are protected against increases were inconclusive. A majority of online survey respondents (64%) said that tax policies should be designed to protect business tenants where possible, but that City policies should not intervene in landlord-tenant matters.

Options to Protect Small Businesses

Three options were presented during consultation as possible tools that the City could use to mitigate against extraordinary tax increases. These options included a targeted approach to tax capping; a deferral program; and a rebate for property owners demonstrating financial hardship.

Option 1: Targeted Tax Protection for Small Businesses

Currently, there is no tax classification that identifies small business. While the creation of a small business tax class could allow for targeted relief for those requiring protection, there are recognized challenges in defining which properties would be included within this class.

One possible approach would see the creation of a small commercial property tax class defined to include only those properties within the Commercial Residual tax class *and* with a total CVA of $5 million or less. The Commercial Residual class, by definition, excludes large office towers, large shopping centres, parking lots and large sports facilities. This would allow tax protection (i.e. capping limits) to apply to only lower valued commercial properties, with all other properties (i.e., those with CVA > $5 million), taxed at full CVA and not subject to limits on tax increases.

During consultations, 83% of session participants (primarily representatives of large commercial and industrial properties) opposed the idea of targeted protection for small businesses. Slightly different results were received with respect to the online survey, with 54% agreeing or strongly agreeing that a targeted approach to tax protection for small business is required, reflecting the fact that a large majority of online survey respondents are small commercial owners or tenants.

Option 2: Deferral Program for Small Businesses

A deferral program would allow eligible property owners to apply to defer any tax increases above 10% (or some other limit), with interest charged on deferred amounts. Any deferred amounts would become repayable upon the sale of the property or change in use. This option could offer predictability for taxpayers, by limiting tax increases to no more than 10%, with any amounts over and above being deferred.

The results from the consultations were overwhelmingly unfavourable with respect to implementing this type of program. Fully 85% of session participants and 67% of online respondents were either neutral or would not support this option. Some of the reasons noted included that adding more financial burden to small businesses by deferring taxes may end up driving the businesses out sooner. Survey respondents also advised that the City should be striving for simplicity by considering less administratively-burdensome options or tools to target relief for small businesses.

Option 3: Tax Rebate for Small Businesses

The option of providing a rebate to small businesses that demonstrate financial need was also presented. This option was met unfavourably with those who attended the sessions, with 100% of responders indicating that they would not support this option. Similar to the deferral program option, the online survey results were slightly more divided, however, the bulk of respondents (68%) were either not supportive of or neutral on this option.

Comments included the fact that this would be administratively cumbersome for both the City and the applicant, depending on the qualifying criteria and the level of financial proof needed to establish eligibility. While providing targeted relief measures for identified vulnerable groups, such as small businesses, appears to be a fair and equitable response, this may ultimately contribute to and prolong disparity in taxation levels amongst property owners in Toronto.

Other Issues Considered

During the sessions and through the responses to the online survey, various other issues were raised. These are summarized below:

Assessment at Highest and Best Use (HABU)

Ontario's *Assessment Act* requires that properties be assessed according to the Current Value Assessment (CVA) of the property. Current Value means, in relation to land, the amount of money the fee simple, if unencumbered, would realize if sold at arm's length by a willing seller to a willing buyer. Current value is determined with reference to actual market transactions of similar properties. The Municipal Property Assessment Corporation (MPAC) is responsible for establishing assessment values for all properties in Ontario.

In establishing assessed values, MPAC is required to assess a property on its most likely market value, or the amount that it would transact for in an open market sale. In certain cases, a property's market value may be influenced by its potential for redevelopment rather than its current use. In such cases, a property's value in exchange, and it's resulting assessed value may reflect its "highest and best use," i.e., the expected market value or sale price of the property based on its maximum potential redevelopment value, considering the maximum density, height, etc. permitted by the site's zoning and other considerations. The Appraisal Institute of Canada defines highest and best use as "the reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported, financially feasible, and that results in the highest value."

Examples of properties whose assessed values appear to have been impacted by a highest and best use approach became evident in 2017, as a result of the 2016 province-wide re-assessment in Ontario (that applies to taxation years 2017-2020). A number of properties experienced significant increases in assessed value due to the property's redevelopment potential, which was impacting sale prices, even where a change in use had not yet occurred. In many of these cases, the current use of the property did not reflect the full development potential permitted under zoning by-laws.

In 2017, a number of properties in Toronto, having reached their full CVA-level of taxation in a prior year, were no longer eligible for tax capping protection against assessment-related tax increases. With no cap on tax increases, property owners that experienced large assessment increases were faced with large and unmitigated tax increases. In many cases, these tax increases were either passed on to tenants through increased rents, or borne directly by business tenants under net leases.

Proposals to address Assessment at Highest and Best Use

The impact of highest and best use on sales prices and assessed values (particularly in cases where a property's current use did not reflect its highest and best use) and the associated tax increases were raised in a number of consultation sessions. In particular, the Property Tax Coalition for Growth (a group of stakeholders that include the Real Property Association of Canada (RealPAC), the Toronto Region Board of Trade, the Toronto Association of Business Improvement Areas (TABIA), Toronto Industry Network (TIN), BOMA Toronto and others) submitted a presentation titled, "Improperly Assessed as Highest and Best Use".

This group takes the position that extraordinary spikes in property taxes are highly correlated with property assessments that are based on sale prices anticipating a change in use in a localized area, or which had been characterized as "lands in transition". Their analysis suggests that many of the changes in use or a new value are speculative, without regard to likely development timelines and/or potential redevelopment, or the presence of long-term, stable small businesses on a particular site. This group has suggested as a solution that the Province be requested to adopt a regulation under the *Assessment Act* that would compel MPAC to assess commercial properties based on "current use", and only when a building permit is issued would a reassessment at highest and best use be triggered.

An additional suggestion was tabled during the consultation period to explore the feasibility of assessing potential redevelopment lands in a way that would see the current use of the land assessed and taxed according to its value in current use, and separately identifying an assessment value to reflect the redevelopment potential for the site. Both the current use portion and the redevelopment portions would be separately assessed and identified on the assessment roll.

This approach would allow both owners and tenants to understand the taxes attributable to the current use portion of the lands and the redevelopment portion. This approach could also allow differing tax rates to apply to the current use and redevelopment portions of the site, with a lower tax rate being applied to the redevelopment portion, or for a phasing-in of taxes on the redevelopment portion of the site (through incremental tax rate increases as redevelopment proceeds).

Staff have acknowledged the merits of this suggestion, and are prepared to engage MPAC to explore the feasibility and other implications of this proposal. As this approach would also require legislative and regulatory changes to implement, staff will also initiate discussions with the provincial Ministry of Finance over the remainder of 2018 to understand whether such changes might be considered.

Capping Assessment Increases (TABIA proposal)

The Toronto Association of Business Improvement Areas (TABIA) provided a written submission titled *The Benefits of Capping Assessments*. According to TABIA, capping assessment increases (e.g. prescribing a maximum allowable increase in assessment used for taxation purposes), would mitigate large increases in assessment on any given property. TABIA's proposal would see MPAC continue to assess land on the basis of CVA without alteration to its methodology or procedures, while tax bills would simply show the full CVA together with the capped assessment value that would be subject to taxation. TABIA has suggested that once a property sells, the sale would trigger the application of the full assessed value going forward.

TABIA suggests that this would restore predictability for taxpayers, and therefore, the ability to properly plan for tax increases, and that this approach would not impair the City's tax revenues, in that tax rates required to meet budgetary requirements would be determined through the City's tax rate-setting ability.

Other stakeholders feel that this option, similar to tax capping policies, are counterintuitive, in that this type of tax relief is structured to provide the greatest benefit to those whose property values, therefore wealth, have increased the most. It was expressed that this may create increased disparity amongst properties.

City staff, in several meetings with TABIA to discuss their proposal, identified that capping assessments would require tax rate increases across property classes in order to fund the shortfall resulting from capped assessment values, (as assessment caps would limit the total assessment base available to the City for taxation purposes). Preliminary analysis indicated that, if assessment increases greater than 2 times the average annual assessment increase were capped, the shortfall in taxes would be approximately $12 million, resulting in a required tax rate increase on the commercial class of approximately 1% in order to maintain the current levy on this class

Additionally, TABIA's suggestion that assessments remain capped until the sale of the property, at which time the full assessment value would apply, has the potential to introduce significant inequities in the taxation level of similar properties, depending on how recently or how frequently the property had sold. These types of inequities would be magnified over time, and represent a departure from the principle that similar properties be assessed and taxed on a transparent and consistent comparable basis. Finally, this proposal would require significant legislative change to implement, both from an assessment and taxation perspective, and would have province-wide implications.

Eliminating Vacant and Excess Land Sub-class

When asked directly whether they would support eliminating the current tax rate reduction for commercial and industrial vacant and excess land tax classes, two-thirds of participants were not supportive of this measure (67%), while 33% were uncertain. Responses from online survey participants indicated that 55% were not in favour or unsure of eliminating the tax rate reduction for vacant and excess land.

Those not in support of the elimination of the reduced rate advised that vacant and excess lands are vital for planning and economic growth. *"Maintaining this reduction is extremely important to our business since this land provides the opportunity to expand operations in future, as the business grows. Since this land is currently not in use, it should not be taxed at the same rate as property that is in use."*

Considerations for Tax Policy for 2019 and beyond

The following section identifies key principles and approaches that an incoming Council must consider and evaluate in establishing tax policies for 2019 and beyond, as supported by the results of the City's public consultations.

No specific recommendations for tax policy are proposed at this time, given that some of the approaches identified herein may require provincial legislative or regulatory changes to implement, or further discussions with MPAC to understand the feasibility or timing of changes to current assessment practice. Additionally, the financial implications of various tax policy approaches or combinations of approaches will need to be evaluated within the context of budget deliberations and a new Council's stated priorities.

1. Current Value Assessment as the basis for taxation

Tax policies should continue to be based on the Current Value Assessment approach to taxation. Ontario's *ad valorem* approach to property assessment, where properties are assessed at current (market) value as a means of distributing the property tax burden, is an internationally accepted best practice in property taxation theory, and, when applied consistently, provides for a fair, transparent and easily understood taxation system.

To this end, Toronto should continue to adopt policies designed to move properties to full CVA taxation levels, as a means of establishing equity in the distribution of property taxes.

2. Continue to reduce tax rates for business properties

Toronto should continue with a long-term strategy to reduce business tax rates (vis-à-vis residential rates) within the commercial, industrial and multi-residential tax classes, as a means of maintaining Toronto's business competitiveness within GTA municipalities, consistent with Council's 2005 approval of *Enhancing Toronto's Business Climate - It's Everybody's Business*.

3. Protection against property tax increases may continue to be required

Regardless of the tax policy approaches adopted, some form of protection against excessive tax increases for business may continue to be required. Given the volatility of Toronto's real estate market and the potential for increases in assessed value to result in large unmitigated tax increases, tax policies must continue to provide protection against unmanageable increases, while providing a measure of certainty and predictability for property owners and business tenants.

4. Funding for tax protection measures

The costs of providing protection against tax increases must be quantified in advance and an appropriate funding source identified. If current tax cap/claw-back provisions are maintained, caps on tax increases may be funded by withholding a portion of tax decreases on properties experiencing assessment-related tax decreases (the status quo).

Protection measures may also be funded through a general tax rate increase across all classes (including residential), i.e. a budgetary increase, or funded within the tax class to which the tax relief applies, i.e. a rate increase for commercial properties to fund protection for commercial properties experiencing increases. This latter approach would require provincial approval to implement. Staff will initiate discussions with the provincial Ministry of Finance over 2018 to evaluate the feasibility of regulatory change to permit this option.

5. Target tax protection to small businesses

A new tax class that identifies small (i.e., lower-valued) business properties may be effective at providing targeted tax relief to properties within the class. A small commercial property tax class may be defined to include only those properties within the Commercial Residual tax class *and* with a total CVA of $5 million or less. This would allow tax protection (i.e., capping limits) to apply to only lower valued commercial properties, with all other properties (i.e., those with CVA > $5 million), taxed at full CVA and not subject to limits on tax increases. Limiting tax protection to only those properties within a small commercial tax class would reduce the overall costs of providing protection, and minimize tax rate impacts within the commercial class or across all classes. This will not however, provide protection to small business tenants in higher-valued buildings.

This approach would require approval from the provincial Ministry of Finance and regulatory changes to define and implement a small commercial tax class. Staff will be consulting with Ministry of Finance staff to further explore the feasibility of this option.

6. Consider eliminating graduated tax rates

Graduated tax rates were introduced in order to accelerate tax ratio reductions for small business properties (i.e., to reach a target tax ratio of 2.5 times the residential rate by 2015 for properties in the Residual Commercial tax class). This objective was reached in 2015.

Although graduated rates presently provide a modest benefit (reduction in taxes payable) to some 36,400 properties within the Commercial Residual tax class, graduated rates do not offer any form of protection against large assessment-related tax increases, and maintain a perhaps unnecessary level of complexity in property tax calculations.

Maintaining graduated tax rates in their present form, or increasing the Band 1 threshold (to which a lower tax rate applies) or increasing the tax rate differential between Band 1 and Band 2, will still likely require that limits on allowable increases (i.e., capping) be offered to mitigate unmanageable tax impacts on businesses. Future tax policy should evaluate the overall effectiveness of graduated tax rates in reducing tax burdens against the more pressing need to maintain some form of limits on tax increases.

7. Be cautious in creating any new tax classes for special purpose properties

Tax policies should be applied across the existing broad tax classes (i.e., commercial, industrial and multi-residential), to maximize the benefit of tax relief measures and to ensure a level of fairness and consistency for all businesses. Specialized or preferential tax treatment for special purpose properties requires clear definition of any new class or sub-class, as this introduces inequities in tax treatment by providing for additional taxes that must be levied on remaining properties, and undermines efforts to ensure tax policies are fair and broadly applied, transparent, and easily understood by business owners.

8. Consider solutions that address the cause of assessment-related increases

Tax policies can be effective in achieving Council's long-term objectives to reduce business tax rates and to bring properties to full CVA-levels of taxation under stable real estate market conditions. However, where a volatile market results in large assessment-related increases and resulting unmanageable tax increases, the effectiveness of tax policies designed to mitigate increases may be compromised.

Addressing the root causes of large assessment-related increases may require a re-evaluation of MPAC's assessment methodologies and provincial legislation that governs assessment practice. The consultation revealed concerns that the impact of "highest and best use" on market values and resulting assessment values may adversely impact business owners and tenants where a change in use has not yet occurred, or where the current use of a property does not reflect the full development potential permitted for the site.

There is merit in engaging both MPAC and the Province to understand how and when the principle of highest and best use is appropriate, and the feasibility of employing potential solutions to address impacts. As any change to current practices may require legislative and regulatory changes, staff have initiated discussions with the provincial Ministry of Finance and MPAC to further explore this issue.

Conclusions

Given the complexity of assessment and taxation policy, it became evident through the City's consultations with business stakeholders that there is not one singular tool or option that the City could exercise to 'fix' the issues encountered following the 2016 province-wide reassessment. The City's consultations also made clear that extraordinary tax increases experienced by certain properties within Toronto are in some cases assessment-related, and therefore difficult for the City to mitigate through tax policy alone using existing tools.

Stakeholder input reinforced the notion that tax policies should be broad in application, easily explainable, transparent and equitable, and designed to minimize unintended consequences. City staff will continue to engage the Province and MPAC to work together to ensure that Toronto's tax policies continue to preserve economic growth and fairness for all taxpayers.

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ATTACHMENTS

Attachment 1: Tax Policy Public Consultation PowerPoint Presentation
Attachment 2: Summary of Stakeholder Consultations: Direct Poll Results
Attachment 3: Summary of Stakeholder Consultations
Attachment 4: Summary of Online Survey Results