

## **Status of Small Business Property Tax Subclass Implementation**

**Date:** May 24, 2022

**To:** Executive Committee

**From:** Chief Financial Officer and Treasurer

**Wards:** All

### **SUMMARY**

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At its November 9, 10 & 12, 2021 meeting, during its consideration of [Item EX27.7: Implementing a Small Business Property Tax Subclass](#), Council adopted the small business property tax subclass for the commercial property tax class, as well as the eligibility criteria, the process to approve the inclusion of properties in the subclass and the process to address requests for reconsideration, appeals and other provisions related to the implementation and administration of the subclass.

In its consideration of this item, Council also directed the Chief Financial Officer and Treasurer, in consultation with the City Solicitor, to report back in 2022 on:

- the feasibility of developing a mechanism for ensuring that subclass property owners with tenants in gross leases pass down the benefits of the reduced property taxes to those tenants; and
- if such a mechanism is not feasible by the City, whether changes to provincial laws could be made to achieve this objective.

In addition, Council directed the Chief Financial Officer and Treasurer to collaborate with Strategic Communications to develop a public awareness campaign directed at both property owners and business operators/tenants about the Subclass, including how it works and who should benefit from it.

In response to these directions, staff have examined possible mechanisms to require property owners to pass through tax reductions to tenants. Given that current legislation does not provide a mechanism by which the City can interfere in the contractual relationship between a commercial landlord and their tenant, it appears that the City has limited means available to enforce a pass-through of property tax decreases to tenants. A public awareness campaign for the Subclass is under development to ensure that business owners and tenants are informed of the tax reductions available, and the dispute/appeal mechanisms that are available. This information is outlined within this report.

## RECOMMENDATIONS

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The Chief Financial Officer and Treasurer recommends that:

1. The Executive Committee receive this report for information.

## FINANCIAL IMPACT

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There are no new financial implications arising from this report. Financial implications are consistent with information that was reported during Item EX27.7: [Implementing a Small Business Property Tax Subclass \(toronto.ca\)](#)

## DECISION HISTORY

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At its November 9, 10 & 12, 2021 meeting, in its consideration of [Item EX27.7: Implementing a Small Business Property Tax Subclass](#), Council directed staff to report back on the feasibility of developing a mechanism for ensuring Subclass property owners with tenants in gross leases pass down the benefits of the reduced property taxes to those tenants, and further, if this is not feasible by the City, whether changes to provincial law could be made to achieve this objective. In addition, staff were directed to develop a public awareness campaign directed at both property owners and business operators/tenants about the Subclass, including how it works and who should benefit from it.

## COMMENTS

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The staff report to Council on the implementation of the small business tax subclass ([Item EX27.7](#)) identifies the issue that tenants in gross lease agreements may or may not receive the benefit of reduced tax rates for small business properties. The report provides:

"The provincial regulation that sets out the requirements for the small business subclass does not provide any mechanisms that require a property owner or landlord to pass on all or any portion of the tax reduction attributable to the property being included in the Subclass.

A property owner may voluntarily pass on tax savings to a tenant, in the form of reduced rents, in the situation where the tenant does not pay the property tax directly (e.g., a gross lease arrangement), but this cannot be enforced by the City.

As owner/tenant or landlord/tenant arrangements and tenancy agreements vary considerably across the City, and given that the City is not party to these

agreements, this report has not included any recommendations nor provisions to enforce a pass-through of any tax decreases to tenants at this time."

It should be noted, however, that any commercial tenants that hold net lease agreements with landlords/property owners, that is, where the tenant is responsible for paying property taxes directly, would experience the benefit of the tax rate reduction for small business. During consultations, commercial stakeholders advised that up to 85% of commercial tenants are in net lease arrangements and pay property taxes directly, and would therefore see the benefit of lower taxes as a result of the small business tax rate reduction.

In response to Council's direction to determine the feasibility of methods to ensure that property owners pass through any reduction in taxes to tenants holding gross leases, staff have confirmed with Legal Services that there are no specific provisions in the *City of Toronto Act, 2006 (CoTA)* that authorizes the City to require property owners/landlords pass through tax decreases to tenants.

In general, the provisions in the *City of Toronto Act* relating to property taxes apply to the taxes levied on the property itself, or to the "owner" of the property, and do not recognize a tenant's contractual interest, regardless of whether a tenant holds a gross or net lease. Additionally, the City of Toronto is not a party to private agreements or leases/rental contracts between property owner/landlords and tenants. This means the City has no means to influence, change or enforce the terms of a rental contract, nor to legally compel either the owner or tenant to do anything. The City also has no access to lease arrangements between landlords and tenants, and cannot compel owners or tenants to provide what are essentially confidential contracts between private parties.

In summary, the City cannot enforce a requirement that would require a property owner to pass through a tax reduction to a tenant holding a gross lease. A property owner may voluntarily pass on tax savings to a tenant, in the form of reduced rents, in situations where the tenant is in a gross lease arrangement, but this cannot be enforced by the City.

Revenue Services staff met with Economic Development & Culture's Business Growth Services and the Toronto Association of Business Improvement Areas (TABIA) to discuss any available mechanisms that would see tenants in gross leases able to share in the benefit of a reduced tax rate for small business properties. While the *City of Toronto Act* provides no direct mechanism to allow this, the provincial regulations that establish the City's authority to adopt a Small Business Subclass provide considerable flexibility for municipalities to enact by-laws to define the eligibility criteria for inclusion in the subclass.

It is therefore technically possible to amend the current by-law to include, as a condition of continuing eligibility that the owner must demonstrate that any property tax reductions have been flowed through to tenants in gross leases, in the form of reduced rents or other monetary considerations. Where it can be established that property owners/landlords did not provide this reduction in rent, the property could be deemed ineligible to be included in the small business subclass in the next or subsequent taxation year(s). This type of provision exists in the current City of Toronto by-law that

establishes the eligibility criteria for Live Music Venues under the City's Creative Co-location Facilities tax subclass.

However, such a provision would be impractical and extremely challenging to enforce for small businesses, given that there are over 29,000 properties in the small business subclass, and the City has no information that could identify which properties are tenanted, or which tenants received a reduction in taxes or reduced rents. Additionally, the City has no authority or means to compel property owners or tenants to disclose the details of their lease or financial details, including monthly rental amounts, which would make it impossible to verify or substantiate claims from tenants whether they did or did not receive a reduction in rent, or whether the reduction in rent was equivalent to the tax reduction for the property.

Given that current legislation does not provide a mechanism by which the City can interfere in the private contractual relationship between a commercial landlord and their tenant, and that the City lacks the ability to substantiate whether owners/landlords have fully passed through the small business subclass tax reductions to tenants, the City has not included any provisions within the City of Toronto Municipal Code to enforce a pass-through of any tax decreases to tenants.

As to whether changes to provincial laws could be made to achieve this objective, it is anticipated that the Province may similarly claim that there are no current provisions that would compel owners/landlords to share tax reductions with tenants, again on the basis that lease arrangements are essentially private contractual relationships between a commercial landlord and their tenant, to which neither the Province nor the City are party.

Staff will, however, consult with provincial representatives to determine whether legislative amendments could provide a mechanism to require that the benefit of the tax reduction resulting from the introduction of the Small Business Property Tax Subclass is passed on to commercial tenants. It is likely that the current provincial election period will delay any discussion of or changes to legislation in the immediate short term. Staff will report back to Council in 2023 on this and other possible changes to eligibility criteria for the small business subclass.

## **Communications Efforts**

Revenue Services staff have worked closely with Strategic Communications to develop a public awareness campaign to ensure both property owners and business operators/tenants are aware of the small business subclass, including how it works and who should benefit from it. To date, the following actions have been completed:

- There were five news releases which were all accompanied by social media posts advising of the new subclass and providing eligibility details.
- A webpage titled '[Small Business Tax Subclass](#)' has been created that includes information about the subclass, the eligibility criteria, the list of eligible properties and the appeal process.
- Customized messaging is included on the inner flap of the 2022 Final Tax Bill for properties included in the subclass.

- The 2022 Final Tax Briefing Note will be circulated to the Mayor and Members of Council once the final tax bills have been mailed to assist with public communications.
- Revenue Services and 311 customer service staff have been advised of updates to the subclass.
- 311 has added a [Small Business Tax Subclass](#) knowledge base article.
- Staff have provided a complete list of all eligible properties on Open Data where both property owners and business operators/tenants can look up their property to determine eligibility.

Final 2022 property tax bills are expected to be mailed at the end of May and beginning of June. Staff will be providing further communications to remind both property owners and business owners of the Small Business Property Tax Subclass and the reduction they may receive as a result, and the process that business property owners can follow if they believe their property should be included in the subclass.

## **CONTACT**

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## **SIGNATURE**

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