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CURRENT VALUE ASSESSMENT ("CVA") AND PROPERTY TAX ISSUES

The Finance and Administration Committee recommends;

1. **The receipt from the Commissioner of Finance of further information providing comparable Property Tax Ratios for Peel, Durham, Halton and Toronto; comparison of taxes payable on a $300,000 residential, commercial and industrial property in Markham, Toronto, Mississauga, and Oakville; plus other factors impacting taxes paid (a copy of which is on file with the Office of the Regional Clerk);**

2. **The adoption of the recommendations contained in the following report, undated, from the Commissioner of Finance with the notation that the following matters (as provided by the Commissioner of Finance pursuant to direction of the Committee) would be considered by the new Committee:**

    1. **Capping of assessment related tax increases for properties in the Commercial, Industrial and Multi-Residential classes including methodology issues and an exit strategy;**
    2. **Assessment averaging requirement for the 2005 taxation year;**
    3. **Appropriate tax ratios and the prescribed "range of fairness";**
    4. **Timing of property (re)assessment and delivery of returned roll; and**
    5. **New voluntary tax mitigation tools that could be used by municipalities.**

1. RECOMMENDATIONS

It is recommended that:

1. The Minister of Finance be requested to establish a jointly chaired committee representing the Province and municipalities with a mandate to examine property tax fairness issues and recommend appropriate changes to assessment and property tax legislation.

2. PURPOSE

The purpose of this report is to discuss current value assessment and property tax fairness issues.

3. BACKGROUND

At its meeting of February 19, 2004, Council directed staff to prepare a report which discussed current value assessment and property tax fairness issues, particularly as they relate to residential taxpayers.

The issue of tax fairness has also been raised by other municipalities, municipal associations and rate payers groups. In addition, Marcel Beaubien was appointed by the previous provincial government to review and report back on specific assessment and property taxation matters.

Council has received a resolution from the City of Sarnia, dated December 11, 2003, which asked the provincial government, "to immediately review the current assessment system to correct a number of injustices that are occurring and to immediately review the so-called "tax fairness legislation" that is mandating communities to shift the tax burden from multi-residential industrial commercial to residential."

In a separate correspondence, the Mayor of Sarnia also expressed a concern about the Municipal Property Assessment Corporation ("MPAC"). The services delivered by MPAC are integral to the provision of a fair assessment and property tax system in Ontario. Staff has prepared a separate report outlining in greater detail the service and quality assurance issues experienced with MPAC by York Region and other municipalities.

3.1 Assessment Experience in Ontario

Property taxation was introduced to Upper Canada in 1793. A revision to the *Assessment Act* in 1845 stipulated that a property must be valued at its actual or market value. In 1849, the jurisdiction for assessment was transferred to municipalities, allowing each to develop its own system and method for valuing property. "This resulted in inconsistencies in property assessment and the distribution of property taxes. Within a municipality, properties with a similar appearance and value could have very different assessments. There were also very different assessments from municipality to municipality" (*MPAC*, *Guide to Property Assessment in Ontario, 2003*). In 1970 the Province reassumed responsibility for property assessment until 1998 when it transferred it to the Ontario Property Assessment Corporation, now called MPAC.

From 1970 until 1997, municipalities had the option to tax properties using an assessment based on its market value, its market value discounted to a given base year or a local assessment based on property values determined as far back as 1940. At the time of implementation of CVA, there existed considerable variation in the use of base years. Toronto used a 1954 reassessment based on 1940 property values. (Report of the GTA Taskforce, January 1996). The base years used for assessment valuation in York Region municipalities varied from 1967 to 1984. This inconsistency in valuation dates and methodologies resulted in inequities within classes of property, between classes within a municipality and between municipalities.

The latest form of property tax reform was implemented by the Province in 1998. From 2003 forward, properties must now be reassessed annually using Current Value. The *Assessment Act* definition of Current Value is "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*"*. This is similar to the former "Market Value" definition used in the

Assessment Act prior to 1997. However, CVA is mandated to be updated by a regular province-wide reassessment to its current value.

3.2 Alternative Methods of Property Assessment

Property assessment can be based on one of two broad streams ─ area-based assessment or value-based assessment.

Area based assessment includes unit assessment and unit value assessment. Unit Assessment applies a tax to the land or the land plus buildings on a unit basis such as per square metre. Unit Value Assessment adds modifiers to distinguish classes of property such as multiple-unit residential, commercial, industrial and farm land and possibly to account for factors such location, age and quality of structure or other factors.

Value based assessment options include: site value; market value; rental value, and self-assessment. Site value is a special application of market value where only the land portion is assessed. Rental value (used in France, Morocco and India) and self-assessment (used in Peru and Turkey) are rather specialized and will not be covered further in this report. For a value based property tax, the assessed value of the property is multiplied by a tax rate specific to the class of property.

A comparison between Unit Value assessment and Market Value assessment was prepared by Professor Enid Slack from the University of Toronto in her publication, *Alternative Approaches to Taxing Land and Real Property, 2001:*

<u>Unit Value Assessment</u>

- Avoids fluctuation in value due to market forces; easy to understand; easy to administer for single unit residential property, more difficult for multi-unit residential, commercial and industrial property;
- Fails to capture the effects of neighbourhood and other local services; fails to allow for the condition of the property and other unique attributes that would be factored into market value. The preceding conditions could result in a greater burden for low income families because a lower income neighbourhood would attract the same tax rate as a higher income neighbourhood.
- When adjustments or modifiers are added to allow for property differences, the system tends to become as complex or more complex than market value over time.
- Unit value is often used in economies with poorly developed real estate resale markets (Eastern Europe); tried and abandoned in the Netherlands and Israel.

<u>Market Value Assessment</u>

- Reflects the effect of neighbourhoods and services, land and structure improvements and quality; no more complex to administer than other methodologies;
- Subject to fluctuations at each assessment as market forces dictate the value that could be received for the property; subject to assessment errors relative to other properties;

- Market value tends to reflect the wealth value associated with a property; ability to pay tends to be reflected in the ownership of the property.

Professor Harry Kitchen of Trent University noted in his publication *Alternative Methods of Taxation and Assessment, 1989* that "Over the past two decades, virtually every report, committee or commission examining local government finance in Ontario has recommended that Ontario move to province wide market value assessment immediately." However, in 1993 the Ontario Fair Tax Commission recommended site value assessment as the preferred methodology for Ontario.

In 1997, the Province chose to use Current Value as the required means for assessing a property's value for taxation purposes in Ontario.

3.3 Property Taxation Tools

The tax reform legislation introduced by the Province in 1998 made provision for a number of tax policy tools that a municipality may employ to maintain taxpayer fairness in response to significantly changing property value assessments. There are essentially three classes of tools: broad tax policy tools such as flexible tax ratios, tax discounts for vacant land and tax discounts for farmland awaiting development. A second set that relate to the treatment of properties within classes are tools such as optional property classes, graduated tax bands and the phase-in of tax increases. A third set is more targeted through tax relief for charities, seniors and the disabled and other special circumstances.

Tax ratios allow a municipality to adjust the tax burden of a particular property class relative to the residential class. There are seven major classes of property, additional optional classes and subclasses (e.g. vacant lands, excess lands and farmland awaiting development). For example, from Table 2 below, the tax ratio for the Industrial property class in York is 1.3 times the Residential rate, therefore, the Industrial tax rate will be 1.3 times that of the Residential class. Municipalities can use these ratios to balance the tax burden between the classes of property however the use of tax ratios is limited by a Range of Fairness prescribed by the Province.

Table 2: Prescribed Range of Fairness

Class	Prescribed Range of Fairness
Residential	1.0000
Multi-Residential	1.0 to 1.1
Commercial	0.6 to 1.1
Industrial	0.6 to 1.1
Pipelines	0.6 to 0.7

The Range of Fairness for tax ratios prescribed by the Province requires that tax ratios must be within a very narrowly defined range for the municipality to have full discretion in adjusting the ratio. If a municipality's class ratio or ratios are above the prescribed range, the ratio may only be moved toward the range of fairness, not away from it. The net effect is that municipalities with ratios outside the range of fairness (which applies to many municipalities) have little flexibility to adjust ratios to meet their individual circumstances and tax burden is being shifted to the residential property class.

The Region of York has a policy to encourage the construction of multi-residential units and to foster business within the Region and thus the ratios for these classes are quite favourable, particularly in comparison to the other GTA municipalities. In support of the multi-residential housing policy, the tax ratio for this class has been reduced from 2.0875 to 1.0 over the last three years. Section 4 provides more discussion on tax ratio policy and the Range of Fairness.

The second set of property class tools have had limited application both within York and across most municipalities. Conceptually the tools are of value but the application has proven to be more problematic. For example, graduated tax bands allow a lower rate of tax on an initial level of assessment, say the first $500,000 and then a higher rate on the next higher level or levels but, the overall tax by the class must remain the same. The intent was to shift tax burden from the small business person to large business with the capacity to pay. Ultimately, the Province negated the utility of this tool by "capping" tax increases for the commercial, industrial and multi-residential classes. Each of the optional tax policy tools has been carefully considered in respect to the overall tax policy of the region.

With respect to the third group of tax policy tools, the Region has provided tax relief for charities and similar organizations and since 1998, for seniors and low income disabled.

3.4 Beaubien Report

In December 2000, Marcel Beaubien M.P.P. was commissioned by the Minister of Finance to conduct a review of the property assessment system in Ontario. His mandate was to review "the operational structure of Ontario Property Tax Assessment Corporation; the relationship between OPAC and the provincial government; and the regulation defining property classifications (Ontario Regulation 282/98)". Beaubien's first report was submitted in April 2001 and his final report in November 2002.

Beaubien undertook extensive public consultation in the preparation of his reports. Subsequent to his first report, the governance model of MPAC was changed to add taxpayer representatives to the Board of Directors; municipalities no longer had the right to opt out of MPAC and property tax relief for heritage properties was introduced. The second report focused on property classification and assessment. Beaubien identified "capping" as an issue and recommended that consultations and analysis be undertaken to assess the impact of removing the capping provisions. The previous government took no action on these recommendations prior to the provincial election.

3.5 The Recent Provincial Announcement on Tax Ratios

On March 16, 2004 the Province passed tax policy legislation that will permit two adjustments previously requested by municipalities.

Municipalities with "tax ratios" that are currently greater than the prescribed Range of Fairness will be able to increase their tax ratios to compensate for any tax burden shifted to the residential class as a result of reassessment. For example, York Region would now be permitted to increase their tax ratios for commercial and industrial properties to compensate for household tax increases in 2004 that could result from reassessment but only to the extent of maintaining the same relative tax burdens between classes as the previous year.

Also, the approximately 36 municipalities who would not be able to pass along tax increases to businesses because their tax ratios exceeded a provincial "hard cap" will now be permitted to do so at half the rate charged to the residential class. This will not impact the Region of York whose business tax ratios are among the lowest in the Province.

4. ANALYSIS AND OPTIONS

Taxpayer fairness issues can be broken down into two categories – those that result from the assessment system and how it is implemented, and those that result from property tax policy.

4.1 Property Assessment Issues

Assessment systems that are based on market value are subject to fluctuations resulting from changes in the market. In fact, the low interest rate environment experienced over the last several years has generally made properties more affordable and has significantly pushed up market values. According to CMHC, the average house price in Canada increased by 23% since 1998.

However, an increase in a property's market value does not necessarily result in an increase in property taxes. Municipalities are required to adjust their tax rates to compensate for the changes due to reassessment. As a result, only those properties whose assessed value increased more than the average will experience a tax increase, while those with an increase less than the average would be eligible for a tax decrease before adding in the affect of a municipality's new budgetary requirements.

Some fairness issues also pertain to how CVA has been implemented. As noted earlier, concerns have been raised about the computer model now used by MPAC to determine a property's market value. Also, some taxpayers disagree with recent changes in assessment methodology, while others have raised communication issues. MPAC service issues are the subject of a separate report to Council.

4.2 Property Taxation Issues

Many tax fairness issues are the result of tax policies designed to provide tax stability and fairness to one taxpayer group which have consequences to other taxpayer groups. "The property tax reform process in Ontario, for example, started out with the goal of bringing equity (fairness based on ability to pay), accountability, and simplicity of administration to the property tax system. Subsequent policies, however, have focussed on tax stability.

The result has been sacrifice equity and simplicity and to confuse accountability." (Slack, Enid. *Property Tax Reform in York Region: Issues for 2001, June, 1999)*

4.2.1 Capping in the Commercial, Industrial and Multi-Residential Property Classes

The "capping" of assessment related property tax increases was introduced in 1998 as a means to provide tax stability to individual businesses facing large tax increases as a result of reassessment. Property tax increases were initially limited to 10% with subsequent increases held to only 5%. There is no requirement that a protected property reach the full amount of its tax payable within a specified period.

Capping creates inequities.

Within the commercial, industrial and multi-residential classes, capped business owners have an indefinite financial advantage over their competitors who are unable to receive their full property tax decrease because of "clawbacks" needed to fund the capping requirements. Originally, this advantage was limited to existing properties within a protected class. However, this was extended to new properties in 2001 as part of Bill 140.

4.2.2 Tax Ratios

As noted earlier, tax ratios represent the relative tax burden between a property in a class compared to a similarly assessed one in the residential class.

Because an upper or single tier Council can adjust the tax ratio (and therefore the relative tax burden) of a property class either toward or within the prescribed Range of Fairness, it must make tax fairness decisions. As a result, it may create greater tax fairness between classes within a municipality, but the shift in tax burden to the residential class, can create a new perceived inequity. For example, the City of Toronto's relatively high tax burden on commercial and industrial property classes has resulted in the tax rate for their residential taxpayers to be much lower than neighbouring municipalities such as York Region who have a much lower tax burden rate on businesses.

Table 3: Property Tax Ratios 2003

Class	Tax Ratios					Prescribed Range of Fairness
	Durham	Halton	Peel	Toronto	York	
Residential	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000
Multi-Residential	2.2629	2.2619	1.7050	3.8705	1.0000	1.0 to 1.1
Commercial	1.4819	1.4565	1.2971	3.5206	1.1000	0.6 to 1.1
Industrial	2.2598	2.3599	1.4700	4.1220	1.3000	0.6 to 1.1
Pipelines	1.2294	1.0617	0.9239	1.7080	0.9190	0.6 to 0.7

4.3 Need for a Coordinated Approach

Since tax reform was implemented in 1998, many municipalities and municipal associations such as AMO, Association of Municipal Managers, Clerks and Treasurers of Ontario (AMCTO), Municipal Financial Officers Association (MFOA) and the Association of Municipal Tax Collectors of Ontario (AMCTO) have made presentations to the Province expressing concerns about assessment, property tax policy and MPAC service issues. While many of the issues they raised have remained unaddressed, the March 15, 2004 announcement by the new Provincial Government has demonstrated a willingness to listen.

Therefore, it is recommended that the Minister of Finance be requested to establish a jointly chaired committee representing the Province and municipalities with a mandate to examine property tax fairness issues and recommend appropriate changes to assessment and property tax legislation. This recommendation builds on other recommendations put forward from associations such as the MFOA that call for dialogue and an end to some of the legislation such as capping and tax ratio constraints.

5. FINANCIAL IMPLICATIONS

The cost to individual taxpayers resulting from CVA and property tax fairness issues cannot be fully calculated. However, as a result of the Province's requirement to limit assessment related tax increases for commercial, industrial and multi-residential properties to 5%, approximately $32 million of potential tax decreases (York FIR 2003) for almost 6700 business taxpayers were "clawed back" in 2003. In addition, since the available decreases were insufficient to fund all the lost revenue resulting from the "caps", the Region was also required to absorb a shortfall of approximately $35,000.

6. LOCAL MUNICIPAL IMPACT

The local municipalities collect tax revenue on behalf of themselves, the Region and the School Boards and have direct contact with taxpayers on many of these issues. The municipalities have also been required to fund their share of the capping shortfall which was approximately $12,000 in 2003.

7. CONCLUSION

Fairness to taxpayers in York Region is influenced by both the use of CVA and assessment implementation issues and tax policy legislation that has been imposed by the Province. Municipalities and their associations have advocated strongly for changes to improve taxpayer fairness. Many of the recommendations have yet to be implemented.

The Senior Management Group has reviewed this report.