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Mega-changes for Ontario

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Property tax system faces radical change

by Gordon J. Alexander

Since May 10, 1996, the Who Does What panel chaired by David Crombie has submitted six letters of advice along with several other related letters and memoranda concerning assessment and property tax reform to the Minister of Municipal Affairs and Housing for consideration.

The Ontario government has already taken actions on some of the panel's recommendations; in particular the adoption of the Actual Value Assessment (AVA) program and the commencement of a province-wide reassessment of property. Finance Minister Ernie Eves introduced Bill 106, The Fair Municipal Finance Act 1997, in the Legislature on January 16.

Taxation Policy

The proposals in this area represent a radical departure from the status quo. In brief, the government has announced that:

- All properties in the province will be assessed on the basis of current market value: "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"
- There will be six property classes:
  a) residential property
  b) multi-residential property
  c) commercial property
  d) industrial property
  e) pipelines
  f) farms and managed forests
- Tax rates for multi-residential, commercial and industrial properties will be based on a percentage of the residential rate
- Municipalities will set the "variable" rates within a range prescribed by the province
- The business occupancy tax will be cancelled
- Tax rebate programs for farmland, managed forests and conservation lands will be discontinued, and the properties taxed at 25% of the residential rate
- Tax increases and decreases resulting from the province-wide reassessment will be phased in before the year 2004 based on the discretion of local municipal policy

The government has also indicated that municipalities will have the option of:

- Putting new apartment buildings of seven units or less into a new property class with a lower tax rate
- Taxing lower valued commercial properties at a lower rate than office buildings and large commercial developments (one option might be to have one tax rate for assessed value up to a certain amount, and a higher rate for assessed value beyond that amount)

The smoke clears but the uncertainty continues

The details of education property taxes are still up in the air. The Crombie panel initially recommended a uniform tax rate for commercial and industrial property to fund the provincially-controlled Ontario Education Opportunity Fund (OEOF) and a discretionary tax for residential property of up to five per cent of local school board budgets to be used for local education enrichment programs. At this point, the government has said education will not be funded from residential property taxes; taxes on commercial and industrial property will be collected by the province.

Some other Crombie recommendations are still pending:

- Discontinuing the taxation of vacant commercial and industrial property at the residential mill rate
- Reassessing development lands being held as farmland as vacant residential, commercial or industrial land at the point of draft subdivision plan approval, where the change in use was proposed by the property owner, and the municipality has agreed
- Keeping taxation policies affecting recreational property (i.e. cottages) consistent with all other classes of property
- Collecting Gross Receipts Tax charged to telecommunications companies for the use of municipal right of ways (i.e. telephone lines) for use by the province, based on user fees which are to be determined with the aid of the CRTC
- Continuing payments in lieu of property taxes paid by the province and its enterprises to the municipalities, pending a review of the current payments
- Reviewing exempt properties to establish principles from which clear criteria for exemption can be determined, and discouraging private member's bills where property tax exemption is an issue.

Implications for commercial and industrial properties

The most significant changes in taxation policy affecting commercial and industrial property owners are:

- Elimination of business occupancy tax
- Creation of variable tax rates
- How education taxes will be levied on business
- Whether tax relief on vacant space through taxation at the residential mill rate will be discontinued

Elimination of Business Occupancy Tax

This outdated system of taxation was based on the perceived "ability to pay", which was determined circa 1904. The shortfall in revenue resulting from its elimination, an estimated 11 per cent of municipal revenue, will be factored into the variable tax rates recommended for the various property classes.

The effect of this is that landlords will now be liable for property taxes which were previously the liability of their tenants. This, combined with the discontinuation of the mill rate conversion (from commercial to residential) for vacant space, portends difficult times for landlords with gross and semi-gross leases, as they attempt to limit their tax liabilities.

Businesses which are currently paying business occupancy taxes of 30 per cent and 75 per cent could respectively expect tax increases and decreases as a result of the averaging effect of business occupancy taxes being factored into the variable tax rates.

Variable tax rates

The legislation proposes that all property be categorized into property classifications and that each of these classifications be taxed in relationship to the lowest class: single family residential property. The ratio is to fall within a range determined by the province. Although the ratio is not spelled out, the Crombie panel found that current practice falls within the ranges shown in the chart.

These rates may indicate the range within which a municipality would be given the discretion to tax the indicated property classes. For example, a municipality could elect to have industrial property pay taxes as a percentage of actual value which is six and one half times higher than single family residents.

Uniform tax rate for education

Currently it is unclear how education taxes will be levied on businesses. The rate could be calculated as a percentage of actual value or in a manner similar to the now-defunct Commercial Concentration Tax (CCT), based on a static unit of measurement, such as area.

Discontinuation of tax relief for vacant space

With the potential for higher property taxes accruing solely to the property, discontinuation of tax relief for vacancy would present short term problems, as the marketplace adjusted to this new condition. The Who Does What panel suggested that since properties will be revalued on a regular and frequent basis, the vacancy problems will be factored into the value of the property, thereby providing appropriate tax relief. Given the fluctuating nature of tenancies it is difficult to ascertain if this approach would provide the expected tax relief for vacancy.

Valuation and assessment practice

The recommendations affecting this area of property taxation, although comprehensive, have more of the appearance of fine tuning the existing system than a radical departure from the status quo.

The recommendations proposed for assessment valuation include the following:

- All valuations are to be based on current value
- All assessing jurisdictions throughout the province are to be reassessed on a common base of June 30, 1996

Property Class	Tax Rate Range (as a % of residential tax rate)
Multi-Residential	100 - 490
Commercial	140 - 460
Industrial	190 - 650

- All assessments are to be updated annually, based on a three-year rolling average
- The new assessment system is to be fully implemented by the year 2004

Although not specifically mentioned by the Who Does What panel, it is anticipated that the current valuation techniques (sales, cost and income approaches to value) will be employed to conduct the reassessment. However, it is rumoured that single family residential property will be reassessed using a multiple regression analysis technique, based on residential sales.

Changes in the area of assessment appeals represent a departure from the current process. What has been recommended is a process which is similar to that found in the province of Nova Scotia.

The recommendations proposed are briefly as follows:

- Creation of a 60 - 90 day appeal period to provide additional time for alternative dispute resolution (ADR) through discussion and negotiation
- Creation of a single tier appeal system through the Assessment Review Board
- Elimination of the current second tier appeal tribunal at the Ontario Municipal Board as of 1998
- Ensuring that presiding members of the Assessment Review Board are knowledgeable with respect to appraisal theory assessment practices and the municipality in which the property under appeal is located

These changes will streamline the current system, but will also limit an appellant's opportunities to seek a satisfactory settlement. Consequently, the appeal process will have to be conducted more aggressively, with an emphasis on preparation and evidence.

Conclusion

Although the new legislation and regulations will create a more uniform and streamlined assessment and property tax system for the province of Ontario, it is still not known with any certainty who will benefit and who will be burdened by property tax reform. For example, which communities will be the most beneficial to live in, to work in, and to invest in? Where will the tax shifts be and on what classes of property? How will the tax shifts impact on the value of real estate? What can a prudent property owner do to prepare for these impending changes?

As unsettling as the current environment concerning these issues is, there are initiatives that property owners can undertake to be prepared. Property owners should ensure that they know the value of their property as of June 30, 1996. They should make themselves aware of the rental activity and sales of similar property in their neighbourhood. They should be prepared to discuss the new 1996 valuation of their property with the assessor. They should be prepared to contest the assessor's valuation, should it not meet with their expectations.

Pending Issues

While the introduction of Bill 106 clarifies the general direction in which the government is heading, much still remains unclear:

- Actual details to be prescribed in the regulations
- Impact of other Who Does What panel recommendations
- Impact of community tax shifts
- Impact of property tax shifts
- How education taxes will be levied on business
- Assessment valuation methodologies

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Development charges could drop

by Jeannette Gillezeau

In November 1996, the Ontario government introduced Bill 98, a new Development Charges Act (DCA). The government's stated intentions are to:

- **"create new construction jobs and make home ownership more affordable"** by reducing development charge rates and simplifying front-ending provisions
- **"make municipal council decisions more accountable and more cost effective"** through requirements for municipal contributions for projects financed from development charges, stronger reporting requirements and mandatory long-term capital and operating cost forecasting

The Bill is expected to be sent to one of the Standing Committees for hearings late this winter or early in the spring. This article outlines some of its major implications.

Reduced Development Charge Rates

For many municipalities, the provisions of Bill 98 will result in substantial reductions in development charge rates - by more than 50 percent in some cases. Municipalities that are likely to face substantial reductions are those where parkland acquisition, administration buildings and recreation facilities account for a large share of the growth-related costs covered by their current development charges.

On the other hand, municipalities that did not choose to adopt development charges to cover the full range of permitted growth-related costs may find that they can still charge similar rates.

Municipalities that allowed for a 10 per cent "credit" in their development charge calculations will not be affected to the same extent as municipalities that allowed for a smaller "credit" or no credit at all.

Regional municipalities that focused their development charges on the financing of roads, water and sanitary sewer infrastructure will be affected less than those that chose to devote a significant share of their development charges to administration buildings, hospitals, homes for the aged, museums and/or regional parks.

Pressure on Municipal Taxes and User Charges

The requirement that municipalities pay some or all of the cost of growth-related capital projects from non-development charge revenues will put pressure on municipal taxes and user charges. Again, the impact will be greatest for those municipalities which will face substantial changes from their current practices.

This is likely to result in cutbacks in capital spending plans, increases in taxes and user charges and a return to debentures as a regular source of municipal capital financing.

Cost Shifting to Developers

For developers, costs may appear simply to shift, as municipalities try to avoid the requirements for municipal contributions by:

- redefining some capital projects previously covered by development charges as "local services", which developers will be required to provide directly
- requiring that capital projects needed to service new development be covered by front•ending agreements and, perhaps,
- pressuring developers to directly provide development charge projects and then refusing credits for such services.

However, the shift probably won't offset the savings from lower development charges.

Key elements of Bill 98 first proposed in 1980s

by Robert Feldgaier

Some municipalities — particularly those in the GTA — see Bill 98 as being tilted in favour of the development industry — but is it?

Three key elements of Bill 98 are: municipal contributions to the costs of services funded through development charges; limitations on the list of eligible services, and the use of past average levels of service as the basis for calculating future levels of service.

These three issues were all key elements of the development industry's position in discussions with the Association of Municipalities of Ontario (AMO) and the Province in the mid 1980s, prior to the introduction of the current Development Charges Act. However, the industry sought more: for example, a higher municipal contribution for some services and a more limited list of eligible services.

A major goal of the industry was and remains to ensure affordability (for development charges and facilities funded through them) and accountability (in the calculation, collection and spending of development charges revenues). It has become apparent that the existing DCA cannot ensure either.

The reality is that Bill 98 still falls short of the industry's position as put forward both in the 1980s and as recently as 1996. Bill 98 should be seen as a compromise between the industry and municipal positions, taking into account today's fiscal realities and the need to make home ownership more affordable.

50% in some areas

It's unlikely developers will be asked to directly provide infrastructure or facilities which are not related to their developments. They may be asked to pick up the full cost of improvements to arterial roads in the vicinity of their site or of a baseball diamond in their development; they are unlikely to be asked to provide a new town hall or land for a park far from their development.

Cost shifting may not be very significant in municipalities which have regularly asked developers for direct contributions to off•site capital works. Typically, municipal staff will argue that the works are necessary for a specific development to proceed and that the improvements were not included in the development charge calculations or that there are not sufficient funds to pay for the required improvements. Some municipalities allow a credit against development charges for some or all of the costs, while others do not.

Increased Resistance to Development and Growth

In some municipalities, the revenue stream from development charges has been an incentive for the approval of new development. Growth could fund municipal officials' pet projects, often with little or no direct impact on taxes. This incentive will be eliminated with Bill 98.

Rapidly growing municipalities with relatively small existing population and employment bases, could experience significant problems in financing the infrastructure needed to accommodate growth, as a result of Bill 98. This may make them more hostile towards new development, which in turn may make the development approval process more costly and time•consuming.

Improvements in Municipal Financial Planning and Management

Many Ontario municipalities do no capital planning beyond the annual budget. Other municipalities prepare very basic five or ten year capital forecasts but don't clearly define the scope and need for the planned projects, or don't assess the potential operating and maintenance costs.

Some municipalities are sloppy in the management and reporting of development charge reserve fund accounts. Municipalities have withdrawn funds for projects that are clearly not growth•related, such as fixing the roof of an existing arena, or replacing an aging fire truck. One municipality emptied its roads development charge reserve fund to pay for a bridge that was not constructed, did not return the money to the fund and actually charged interest to the fund to cover the "deficit" created by the withdrawal. Other municipalities do not prepare or do not release to the public annual development charge reserve fund statements.

Bill 98 will force lax municipalities to improve their standards of practice in the areas of financial planning and the management and reporting of development charge reserve funds.

In summary, Bill 98 will have benefits for Ontario residents:

- Better municipal financial planning and management
- Fewer unnecessary or gold-plated municipal facilities
- Lower prices for new homes and commercial and industrial space
- Increased construction activity – as lower prices encourage more buying and building – with spin-off benefits for economy, and
- A more competitive business climate – with lower housing prices and cheaper commercial and industrial space.

However, the benefits of Bill 98 will be obscured by other changes in the responsibilities and financing of Ontario municipalities, and by the recovery of the Province's real estate market.

On the down side, Ontario residents and businesses in many rapidly growing municipalities may face:

- Higher property taxes and user charges and/or
- Reduced levels of municipal service, and
- Municipalities which are hostile to new growth.

Jeannette Gillezeau is vice president of Clayton Research Associates Ltd., with a specialization in municipal finance and development charges. Robert Feldgaier is a senior associate at the firm, with primary responsibility for residential market analysis, and a member of the Ontario Home Builders' Association land development committee.

Highlights

Bill 98, as introduced in November 1996, will:

- Replace those sections of the 1989 DCA which govern **municipal development charges.** (Education development charges are not to be significantly altered at this time.)
- **Limit services** which can be financed from development charges, specifically excluding parkland acquisition, administration buildings, and cultural, entertainment, tourism and hospital facilities.
- Ensure that the level of service used in the calculation of capital costs will not exceed the **average level of service** over the previous decade.
- Provide that capacity available in **existing municipal facilities** and benefits to existing residents are included in the calculation of the charge.
- Ensure that the development charge revenues collected by municipalities are **spent only on those capital costs** identified in the calculation of the development charge.
- Require **municipalities to contribute funds** (e.g. taxes, user charges or other non-development charge revenues) to the financing of projects primarily funded from development charges. The municipal contribution is 10 or 30 percent, depending on the service.
- Permit (but apparently not require) municipalities to grant developers **credits for the direct provision of services** identified in the development charge calculation and, when credits are granted, require the municipality to reimburse the developer for the costs the municipality would have incurred if the project had been financed from the development charge reserve fund.
- Set out provisions for **front-end financing** capital projects required to service new development (apparently without requirements for municipal contributions.)
- Set out provisions for **appeals and complaints,** and **transitional rules,** including that municipalities will have up to 18 months from the date of proclamation of the new Act to establish new development charge bylaws, otherwise the old bylaws will expire.

Facilities management: an emerging service industry

by Judith Amoils

Facilities management as a profession is well established. What is new in this industry is the emergence of a service industry provided by a third party on a fee management basis. The catalyst for this in the Canadian market place has been fiscal pressures on all three tiers of government.

Canada Post, approximately three years ago, outsourced the facilities management of its real estate to the private sector. This contract effectively established the market in Canada for facilities management as a service industry. More recently, other major public sector owners and Crown corporations have announced their intent to outsource facilities management of their real estate assets. One example is the Department of National Defence, which recently outsourced the management of a number of sites in southern Ontario.

Facilities and property management: similarities and differences

Facilities management is often confused with property management. While there are some similarities, the differences are sufficient to distinguish facilities management as an industry in its own right. Both industries have some activities in common; for example, building systems maintenance, general maintenance, custodial services, waste management etc.

Property management is the management of real estate that is typically leased to/used by third parties, and therefore property managers are concerned with leasing activities, rent collection and management of a property for the purposes of improving financial performance. Their focus is maintaining or enhancing investment value for the owner.

Facilities management is the management of real estate for a corporation in support of its business mission. Facilities managers are responsible for corporate real estate, which may be both owned and leased. Their focus is the support of the company's business operations.

The evolution of an industry

A review of the facilities management industry in the United Kingdom shows an industry with many similarities to that emerging in Canada. The industry, as a service industry, grew from the Thatcher government's policies of retreating from delivering services that are not central to the government's raison d'etre. The industry rooted itself in public sector opportunities and once established began to offer service to the private sector. Today, the industry shows signs of maturity, having undergone a shake-out with those companies who have successfully established their niche offering their services internationally.

The Canadian marketplace seem to be following a similar course. The opportunity to provide services is currently being driven by the public sector, and the service provider community is structuring itself to respond accordingly.

The service provider community: organizing to respond

Facilities management is a heterogeneous industry, with companies offering services as diverse as the management of complex heavy industrial facilities, through to office buildings. A review conducted by the author recently of providers in Canada, the United States and the United Kingdom shows that providers have come from a number of different origins.

- **Engineering and Construction**
  These companies have entered facilities management from their design/build/operate activities — some companies have developed expertise in very specialized areas.
- **Property Management**
  These companies have expanded into facilities management by supplementing the activities that are common to both facilities and property management.
- **In-House Providers**
  In a number of cases, providers have their origins in an in-house facilities division

that has separated from the parent company and been set up as an independent service provider.

- **Specialist Providers**
  These companies have moved into facilities management from a specialist area such as food service, mail room management or laundry services.

Some service providers in the Canadian marketplace today have formed as consortia made up of companies from the areas described above. In addition, a number of foreign companies have entered or are currently looking to enter the Canadian marketplace.

Future opportunities: the owner's perspective

Facilities management as a service industry is just beginning to emerge in Canada. It represents a dynamic and exciting opportunity for service providers and owners alike. For owners, the future will lie in determining what the industry can offer by way of synergies and cost savings. Outsourcing may be a viable option to self-provision, although caution must be used. Outsourcing inappropriate activities, with insufficient protection for service levels, can result in more cost for poorer results. A thorough analysis should be undertaken prior to undertaking any kind of outsourcing. In addition, if outsourcing is used, care must be taken to thoroughly define scope, contract price, service levels and contract terms.

Future opportunities: the service provider's perspective

For providers, the immediate future will lie in capitalizing on opportunities and aggressively developing the volume of business that drives synergies and cost savings. In addition, the industry has yet to define niches. Other areas needing attention are improving quality of information systems and reporting capabilities, and improving quality assurance methods.

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NEXT DINNER MEETING

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Speaker-
Michael W. Freund
President and CEO
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What you've missed

Elizabeth Patterson, assistant deputy minister, property assessment division, Ministry of Finance, spoke to our membership on October 24, 1996, at the Adelaide Club. Elizabeth is part of a management team now preparing to implement the new market value assessment (MVA). This market-based system is to be province-wide with up to date market values.

In order to meet the provincial deadlines, effectively the entire province must be re-evaluated in approximately 18 months. Questions raised during the discussion focused on the complexity of performing such a mammoth task in such a short time frame, and the potential threat of quality control problems with the validity of the values being established. Elizabeth responded to all the issues raised, with a frank and remarkable focus to the salient concerns.

Tom McCormack, president, Strategic Projections Inc., spoke to our membership on November 28, 1996, at the Royal Canadian Yacht Club's mainland facility. Tom's background allowed him to field questions on demographics, the conclusions of David Crombie's Who Does What panel (which has been asked to disentangle provincial and municipal service responsibilities) and the Premier's Task Force on the Future of the Greater Toronto Area.

His address focused on key demographic trends which will shape Canada, Ontario and the GTA over the medium and long term. Some of the key conclusions presented can be summarized as follows:

- the average age of our population will continue to increase as the boomers head into their 50s and 60s
- Ontario, Alberta and British Columbia have the highest levels of average household income
- population growth in those three provinces will continue to outpace the rest of Canada
- employment sectors with the strongest growth have been finance, business services, health services, education and other service industries including accommodation, food and beverage.

by Bonnie Bowerman

Around Queen's Park

Who Does What Panel

Late last year, a number of Crombie's sub-panels issued recommendations on a wide variety of topics: social services, transportation and utilities, assessment, emergency services, and education. David Crombie himself chaired the assessment sub-panel which recommended that residential properties should be used as a benchmark in the setting of variable tax rates for multi-residential, commercial and industrial classes of property. For example, commercial would be taxed at 140 - 460 per cent of the residential rate. This would bring tax rates among the property classes closer together.

In terms of multi-residential properties, it was recognized that the rate can by five times higher than single-family residential, but the sub-panel suggested that it should be left up to the municipality to set the actual rates.

The education sub panel recommended that a substantial increase in the share of education funding be provided by the province, which logically would mean less reliance on residential property taxes.

Municipal and Provincial Responsibilities

In mid January, the Province made a series of announcements concerning the disentanglement of local and provincial responsibilities and media coverage has been intense. While some of the Crombie panel recommendations were followed, others were changed. Support has been mixed.

A critical reform for education will be the removal of this component from residential property taxes. Provincial grants will replace this source of revenue. If one follows this line of argument, then it makes sense to eliminate education development charges which buyers of new homes pay for school capital costs.

In return, municipalities take on greater fiscal responsibility for welfare and long term care, as well as all the costs of social housing, water and sewer works, library management, local policing, public health programs, municipal transit and airports, GO transit and provincial highways and ferries that primarily serve local needs.

It is clear that, from a gross ledger perspective, the shifting of costs should be fair, but there will be differential impacts. The difference between the 905 and 416 area codes comes to mind. There has been much debate on whether municipalities are in a position to assume a greater share in welfare and other social service costs.

Tenant Protection Act

On November 21, Minister of Municipal Affairs and Housing Al Leach introduced The Tenant Protection Act, 1996. It is expected that the Standing Committee hearings will begin in March because of the extended season for the House. Landlord groups continue to have concerns with the manner in which the vacancy decontrol provisions are being put forward. Market rent can be set upon turnover of a unit but once the unit is occupied, at whatever level — lower or higher — the rent increase guidelines will once again apply.

To help reduce the backlog in the courts, the Ontario Rental Housing Tribunal is being proposed to adjudicate landlord and tenant disputes. The Minister hopes to encourage private rental supply through these and other legislative amendments which will be considered by the Province.

Ontario Building Code

Most of the changes are editorial and ensure consistency with the model National Building Code of Canada and the rest of the OBC. A noteworthy change is a "roll back" of thermal insulation requirements to 1986 levels to make new housing more affordable to first time buyers. A basic energy labelling system is also being proposed which could increase the insulation level. The public comments are going to a government code committee for review.

Consultation on Reforming Environment and Energy Regulations

The Ministry of Environment and Energy received more than 300 responses to its paper on reform of 80 regulations. The new Minister, Norm Sterling, now has responsibility for implementing these reforms which will, among other things, reduce red tape.

A potential conflict is brewing, however. Eva Ligeti, Environmental Commissioner for Ontario with responsibility for the Environmental Bill of Rights, has written that the newly proposed laws and policies "seem at odds with the public's growing appreciation of the necessity of integrating environmental, social, economic and scientific factors in decision making. The EBR recognizes this requirement and requires that government honour it when it makes decisions that affect environmental quality. It is my job to insist that this requirement is honoured."

Development Charges Act

Introduced into the Ontario Legislature on November 25th, again by the Hone. Al Leach, the proposed changes to the Development Charges Act (DCA) have sparked controversy and, for a short period, Mississauga froze development approvals. The changes will bring greater fairness to the way services for new growth are financed and bring greater accountability into municipal decision-making by requiring municipalities to contribute between 10 and 30 per cent of the cost of eligible services. Materials released by the Ministry state that "new residents should not be expected to pay for the entire cost of new facilities as well as contributing, through their property taxes, toward the cost of existing facilities or their renewal."

Costs will be contained by restricting the types of eligible services funded through development charges. For example, municipalities will no longer be able to impose development charges for tourist or entertainment facilities, hospitals, city halls or parkland acquisition. For more details see the article in this issue.