SUBJECT: 2009 Tax Capping Policy for the Multi-Residential, Commercial and Industrial Property Classes (FCS09038) (City Wide)

RECOMMENDATION:

a) That, for the 2009 taxation year, the tax capping percentage for any assessment-related tax increases in the Commercial, Industrial and Multi-Residential property classes be set at 10%, the maximum allowed under Section 329.1 (1) 1 of the Municipal Act, 2001;

b) That, for the 2009 taxation year, any capped property in the Commercial, Industrial and Multi-Residential property classes that is within $250 of its Current Value Assessment (CVA) of taxes in 2009, be moved directly to its' full Current Value Assessment (CVA) of taxes, as allowed under Section 329.1 (1) 3 of the Municipal Act, 2001;

c) That, for the 2009 taxation year, the new construction / new to class treatment be phased out by establishing a minimum percentage of Current Value Assessment (CVA) taxes, such that eligible properties will be taxed at 100% of Current Value Assessment (CVA) taxes in 2009 and future years, as allowed under Section 329.1 (1) 8 of the Municipal Act, 2001;

d) That, pending Provincial regulation, for the 2009 taxation year, any property in the Commercial, Industrial and Multi-Residential property class which paid full Current Value Assessment (CVA) taxes in 2008, no longer be eligible for capping protection in 2009 and future years;

e) That, for the 2009 taxation year, the cost of the capping program be funded fully from the operating budget, requiring no clawbacks; and
f) That the City Solicitor & Corporate Counsel be authorized and directed to prepare the necessary by-law, for Council approval, for the purposes of establishing the capping policies for the 2009 taxation year.

EXECUTIVE SUMMARY:

Commencing in 2009, the Province has established a four-year phase-in of assessment increases. This assessment phase-in is applicable to all property classes, including the Commercial, Industrial and Multi-Residential property classes. As a result of extending the phase-in protection to these property classes, the Province subsequently announced significant flexibility with respect to the current mandated capping program (as of the writing of this report, the regulations are pending and expected to be passed shortly). Beginning in 2009, municipalities now have the option to remove properties from the capping program once they have reached their full Current Value Assessment (CVA) level of taxes in the prior year. Future assessment changes for properties that exit the capping program would be mitigated through the assessment phase-in, resulting in the movement towards equal treatment of assessment increases for all property classes.

Since assessment increases for all properties are being phased in over four years, staff are recommending to apply this new flexibility and, commencing in the 2009 taxation year, no longer cap properties in the Commercial, Industrial and Multi-Residential property classes if the property paid full CVA taxes in 2008. This would ensure greater tax equity in that all property classes would eventually be treated equally through the phasing in of assessment increases. Although this new flexibility does not allow for the general exit from the capping program, it ensures that as properties reach full CVA taxes, they remain there, regardless of the impacts of future reassessments.

If this new flexibility is adopted, the cost of the capping program would be approximately $610,000 (2008 capping = $1.5 million) and would result in the continued 100% flow-through of any assessment-related tax decrease (no clawbacks required). Ninety-six percent of all commercial, industrial and multi-residential property classes would be paying at full CVA taxes in 2009.

Staff’s recommendation is in agreement with the overall opinion of many municipalities, who, over the last several years, have requested the Province to change the capping legislation to ensure that once a property moves to full CVA taxes, it remains at full CVA taxes in subsequent years, regardless of the effects of future reassessments. The Province has now responded to this strong consensus among Ontario municipalities,
giving municipalities the option to no longer protect properties from normal economic assessment increases once they reach their CVA taxes. As stated in the January, 2009 newsletter from the Municipal Finance Officers’ Association of Ontario (MFOA), “The goal is to provide municipalities with flexibility to end tax capping and rely on assessment phase-in as sole means of providing tax protection”.

When originally established in 1998, capping was seen as a temporary tool to mitigate properties with large assessment-related tax increases gradually to full CVA taxes. Eleven years later, capping is still present, and, due to the impacts of a general reassessment, will most likely continue indefinitely if this new flexibility is not adopted. In the absence of a general reassessment, properties would move closer to paying full CVA taxes every year, with eventually all properties paying full CVA taxes. However, in a general reassessment (to occur every four years), capping requirements change dramatically. A property that paid full CVA taxes could then become capped or clawed back, a property that received capping protection may now be contributing to the cap through a claw back and visa versa (see example in the Analysis/Rationale section of this report). From a budgeting perspective, if a municipality relies on the general levy to fund all or part of the cap, as is the case in the City of Hamilton, there is great uncertainty in the capping requirements after a general reassessment.

Not extending capping protection to those properties which paid full CVA taxes in 2008 affects approximately 1% of the properties in the Multi-Residential property class, 4% of the properties in the Commercial and Industrial property class. Twenty-eight percent of these properties affected are vacant lots.

It should be stressed that exclusive of capping, all properties with an assessment increase will receive the benefit of the mandated four-year phase-in. In addition to the assessment phase-in, the commercial and industrial property classes continue to be protected against the full budgetary increase as a result of the mandated levy restriction (maximum allowed under the legislation is 50% of the residential budgetary increase).

BACKGROUND:

Capping of assessment-related tax increases for Commercial, Industrial and Multi-Residential property classes has been mandated by the Province since 1998. Through the years, some flexibility has been introduced in an effort to bring more properties to full CVA taxes, however, in a general reassessment, any progress made towards full CVA taxes is eliminated. The number of capped properties, as well as the cost of the capping program normally increases in a general reassessment. Municipalities have the option to fund the capping program by “clawing back” assessment-related tax decreases, by way of a provision in the budget, or a combination of both. As the commercial and industrial property classes are currently protected from the full budgetary increase, any budgetary assistance to fund the tax capping program is primarily funded by the residential property class.
The Province mandated assessment-related increases at 10% in 1998, 5% in 1999 and 5% in 2000. In 2001 through to 2004, the cap was mandated at 5%. Commencing in 2005, the Province provided some flexibility in that municipalities could establish the cap between 5% and 10%. In an effort to move more properties to full CVA taxes, the City of Hamilton approved a 7.5% cap in 2005 and a 10% cap (maximum allowable) for 2006-2008.

The following table provides a history of the capping program since 2001. As shown below, capping requirements have varied, with requirements typically increasing in a general reassessment year. The capping requirement shown for 2001-2004 would have been higher had it not been for an aggressive plan which significantly reduced both the municipal and education business tax rates, resulting in properties requiring less capping protection. The City of Hamilton has relied on both the general levy and the clawing back of assessment-related tax decreases to fund the capping requirements. Every effort was made to pass on as much of the assessment-related tax decreases, however some claw-backs were necessary, with the exception of 2007 and 2008, when the capping requirement reduced sufficiently to eliminate the need for clawbacks.

As shown above, the capping requirement from 2001-2008 was approximately $67.3 million. This was funded both from the general levy/Hamilton Future Fund and through the clawing back of assessment-related tax decreases.

**ANALYSIS/RATIONALE:**

Staff are recommending that Council employ all the options available in 2009 to reduce the amount of capping required and thereby ensure the greatest number of properties are paying at full CVA taxes. These options include:

- Set cap at maximum allowable = 10% (same as 2008)
- Establish $ threshold at maximum allowable = $250 (same as 2008)
- No capping protection for new construction/new to class properties (amendment)
No capping in 2009 if the property paid full CVA taxes in 2008 (new in 2009)

The end result would be approximately 300 properties being eligible for capping in 2009, at a projected cost of approximately $610,000, which represents a reduction of $900,000 from the 2008 capping requirement. The current (net) capping budget of $1 million (includes HFF of $500,000) is more than sufficient to fund this amount, therefore the City would be able to pass on 100% of the assessment-related tax decreases by not requiring clawbacks. Staff are not recommending reducing the levy contribution to capping at this time as appeals and other tax adjustments can impact the actual amount of capping funds required.

Adopting the staff recommended options would ensure that more multi-residential, commercial and industrial properties pay full CVA taxes, and ensures the movement towards the equal treatment of all property classes with respect to assessment changes. Assessment increases can eventually be solely mitigated through the four year assessment phase-in.

Removing properties from capping once they reach their full CVA taxes ensures that these same properties are then not subsequently capped or clawed-back in future reassessments. Eventually the capping program will, and should, come to an end.

Below is an example of the annual capping/clawback requirements for a business property in Hamilton. This property has assessment in both the commercial and industrial property classes, which are treated as two separate properties for capping purposes.

<table>
<thead>
<tr>
<th>Year</th>
<th>Commercial Portion</th>
<th>Industrial Portion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999</td>
<td>-</td>
<td>(2,028)</td>
</tr>
<tr>
<td>2000</td>
<td>930</td>
<td>(1,014)</td>
</tr>
<tr>
<td>2001</td>
<td>3,719</td>
<td>(1,005)</td>
</tr>
<tr>
<td>2002</td>
<td>221</td>
<td>-</td>
</tr>
<tr>
<td>2003</td>
<td>223</td>
<td>43</td>
</tr>
<tr>
<td>2004</td>
<td>(1,348)</td>
<td>(692)</td>
</tr>
<tr>
<td>2005</td>
<td>51</td>
<td>310</td>
</tr>
<tr>
<td>2006</td>
<td>2,278</td>
<td>(13,048)</td>
</tr>
<tr>
<td>2007</td>
<td>-</td>
<td>(12,444)</td>
</tr>
<tr>
<td>2008</td>
<td>-</td>
<td>(11,750)</td>
</tr>
</tbody>
</table>

negative = cap; positive = clawback

As shown above, both the commercial and industrial portions of this property have been both capped and clawed back at some point in time, with no real progression towards full CVA taxes. Changes in assessment; either as a result of a reassessment, successful appeal or growth/reclass; has resulted in varying degrees of capping/clawbacks. To illustrate the complexities of capping (looking at just the industrial portion of this property): this property received a capping benefit from 1999 to 2001; paid full CVA taxes in 2002; clawed back in 2003 (reassessment year); capped in 2004 (reassessment year); clawed back in 2005 (successful appeal) and finally, as a result of the 2006 reassessment, capped in 2006-2008. As clearly shown, not only does capping add further complexity to an already complex property taxation system, there is no real progression towards full CVA taxes.
Alternatives for Consideration:

Continuing to cap properties, regardless if the property was at full CVA taxes in the prior year, would result in a projected capping requirement for 2009 of approximately 600 properties at a cost of $1.3 million (using 2008 criteria and assumes no capping protection for new construction/new to class properties). This alternative would result in approximately 300 properties that were paying full CVA taxes in 2008, now being capped (28% of these being vacant lots). This alternative results in an increase of 160 properties and a reduction of $200,000 from the 2008 capping requirement.

The 2009 budget allows for funding of $1.5 million ($1 million from the general levy and $0.5 million from the Hamilton Future Fund). This would be sufficient to cover the 2009 capping requirement and therefore requires no clawback of assessment-related tax decreases.

Not modifying the current capping policy to incorporate the new criteria flexibility, would result in business properties continuing to receive the benefit of both the capping and the phase-in protection, in addition to the levy restriction. As such, this option is not being recommended by staff.

Another option would be to remove the budgetary provision and fund the capping program fully from clawbacks. The projected clawback percentages required to fund this $1.3 million capping requirement would be as follows:

- Multi-Residential 12% (528 properties)
- Commercial 34% (2,318 properties)
- Industrial 13% (138 properties)

The above clawback percentages represent the percentage of a property’s assessment-related tax decrease that is used to fund the capping requirement. For example, in the case of the commercial class, in order to fund the cap, the City would need to clawback 34% of the assessment-related tax decrease from 2,318 commercial properties, meaning these properties would only be entitled to 66% if their assessment-related tax decrease in 2009.

Financial/Staffing/Legal Implications:

There are no staffing implications. Current and future tax policies impact the City financially in terms of revenue streams and their sources. If staff’s recommendations are adopted, the current capping budget should be reviewed annually to determine if any reduction is warranted, as more properties exit the capping program and pay full CVA taxes.
POLICIES AFFECTING PROPOSAL:

This report deals with tax policies in relation to tax capping.

RELEVANT CONSULTATION:

Staff have consulted with Provincial staff to ensure that the recommended tax capping policy adheres to the Municipal Act.

CITY STRATEGIC COMMITMENT:

By evaluating the “Triple Bottom Line”, (community, environment, economic implications) we can make choices that create value across all three bottom lines, moving us closer to our vision for a sustainable community, and Provincial interests.

Evaluate the implications of your recommendations by indicating and completing the sections below. Consider both short-term and long-term implications.

Community Well-Being is enhanced. ☑ Yes ☐ No

Environmental Well-Being is enhanced. ☐ Yes ☑ No

Economic Well-Being is enhanced. ☑ Yes ☐ No

Does the option you are recommending create value across all three bottom lines? ☐ Yes ☑ No

Do the options you are recommending make Hamilton a City of choice for high performance public servants? ☐ Yes ☑ No