
Subject: Optional Small Business Tax Subclass Overview

Report to: Corporate Services Committee

Report date: Wednesday, February 17, 2021

Recommendations

1. That staff **BE DIRECTED** to monitor the implementation of the Optional Small Business Tax Subclass for consideration in future taxation years starting in 2022; and
2. That a copy of Report CSD 12-2021 **BE CIRCULATED** to the Local Area Municipalities.

Key Facts

- The purpose of this report is to provide committee members an overview of the optional small business property tax subclass as announced in the 2020 Ontario Budget.
- Included in the 2020 Ontario Budget is the ability for upper-tier municipalities to create a new small business tax subclass. The Region would need to determine eligibility requirements and amount of reduction. Regulations guiding the implementation have yet to be created by the Province. The Ontario Budget is currently the only information currently available to municipalities.
- Relief provided under this optional program as a tax policy decision is made by the Region and applicable to all Niagara lower tiers and results in a redistribution of both Regional and Municipal property taxes onto other property owners (predominately residential which represents 80% of the Region's tax base). Relief as a grant program requires a budget to fund the program and administration on the part of the local area municipalities.
- Regional finance staff have had discussions with the Local Area Treasurers as well as Ontario Regional Treasurers regarding the optional subclass and there is general agreement of the many concerns noted below with the implementation that should be fully analysed in advance of adoption as this is intended as a long term tax policy decision and not a COVID-19 relief tool.
- Municipal Finance Officers' Association (MFOA) has also provided preliminary comments to the Province and has expressed the need for caution and due care to

ensure both the regulatory framework and subsequent implementation of any subclass supports long term strategic objectives in an efficient and effective manner.

- Staff will continue to review the implications of this program including the apparent effectiveness and report back to Council in Q2 of 2021.

Financial Considerations

There are no direct financial implications associated with this report as the Region will still collect the total tax levy. There will be an impact on other property owners not included in the optional subclass as a result of tax redistribution.

For modelling purposes, if 10% of the taxes from the existing commercial tax class are encompassed in a small business subclass and provided with a reduction of 22.5% (similar to vacant/excess land subclass discount) it would create an estimated \$1.5 million saving for eligible properties but increase the tax burden for residential property owners by an estimated \$1.2 million and the remaining impact is to other property classes including commercial properties not captured in the subclass. This results in approximately a 0.4% increase in annual taxes for the average household in Niagara.

Based on the above example using 10% of the taxation, which actually incorporates approximately 60% of all commercial properties in the Region, the eligible commercial properties in that sample would have a maximum assessment of 393,000. A 22.5% reduction would generate a maximum relief for these properties of approximately \$900 and an average relief of \$400 per property.

Analysis

On December 8, 2020 Provincial Bill 229, Protect, Support and Recover from COVID-19 Act (Budget Measures), 2020 received Royal Assent. This omnibus budget bill introduced various amendments to existing property tax legislation for the 2021 taxation year. The more significant of these amendments is the optional small business tax subclass for which further discussion on implementation opportunities and challenges will follow.

Optional Small Business Tax Subclass Program Overview

- Upper-tier municipalities are able to adopt a new optional property subclass for small business properties starting 2021.
- Intended to target relief to small businesses.

- Municipalities will need to define small business eligibility.
- Province may consider matching any municipal property tax reductions adopted through this program.
- Any relief provided through the optional subclass using tax policy will shift added tax burden to other property owners (predominately residential owners which is 80% of the Regional tax base and other business properties that may not be eligible for the subclass).
- Any relief provided through an application based grant program for eligible properties would need to be funded through Regional and local budgets which would also be incorporated in the general levy distributed to all property classes.

Implementation Opportunities

- The ability to create the subclass gives municipalities a method to provide targeted relief to small businesses.
- The possibility of the Province providing equivalent matching relief by reducing education taxes for the new subclass would result in additional property tax relief for small businesses. This will likely be known with the release of the Provincial regulations and if not the Region would advocate for such relief.

Implementation Challenges

- Eligibility – The provincial government is proposing to allow the Region to define small business eligibility in a way that best meets local needs and priorities. The Region would need to consider how to define a “small business” in a way that can be captured in the MPAC assessment roll or through an application program. Although property classification is normally performed by MPAC, in this case municipalities may need to identify the roll numbers to be included in the small business class based on their chosen definition. Municipalities do not have broad experience in determining the eligibility of properties for a particular property class. Also, given the nature of small businesses eligible properties would need to be reviewed annually.

A small business can be defined in numerous ways including by number of employees, by property value, by a class of businesses, by businesses within a geographic area (e.g. located in a BIA), by sales revenue, etc. Most of this information is not part of the assessment roll. Input will be required from MPAC

as to how to define a small business and maintain the assessment roll in a practical manner.

- **Small Business Tenants** – It is not clear on how any tax benefit derived from the subclass may benefit the small businesses that rent building space for their operations. In many cases, small businesses are tenants in larger buildings and may not benefit from property tax savings directly or indirectly.
- **Inconsistency Across Municipalities** – Municipalities will need to determine eligibility criteria independently which will create a lack of consistency in application across the Province. Generally speaking, tax policy legislation is consistently applied for all 444 Ontario municipalities. The inconsistencies could create significant pressure for municipalities to adopt a subclass which may not align with long-term objectives or strategies.

It is also relevant to note that even the definition of a small business may be defined differently within Niagara municipalities. If a subclass were to be based on current value assessment, for example, this will create disparity across Niagara as a result of different assessment values. The average 2020 assessment for a commercial property in Niagara ranges from \$202,000 to \$1,452,000 depending on the municipality. Appendix 1 provides the average assessment range by municipality as well as the associated levy amounts.

The wide variation in assessment values for commercial properties in Niagara's municipalities would mean that in some cases, at a cap based on assessment of 393,000, approximate 70% of the existing commercial assessment base would be included in the new subclass for one municipality but only 4% for another. Therefore it would be challenging to create equity across Niagara municipalities and this has been expressed by Niagara's Area Treasurers as a priority principle for any tax relief program.

A preliminary review of the business types that would be captured in an assessment based program (used the property assessment of 393,000) shows that larger businesses that own multiple properties across the Region would likely benefit the most from the subclass. These larger business would include national telecommunication, energy, gas and larger real estate holding companies. Based on this, an assessment based approach may not be the most effective method of providing relief in comparison to a more targeted application based program which would require a greater implementation timeline and administration on the part of the local area municipalities.

- **Tax Shift to Other Property Tax Class** – The annual budget determines the amount of taxes to be levied and a variety of tax policies determines the property tax rates for each property class. Lowering the tax rate for a small business subclass shifts the tax burden onto other classes of property including residential, multi-residential, and other commercial/industrial properties that would not be eligible for the new subclass. The residential tax class represents 80% of the Region's assessment base. As such, based on the most recent BMA municipal study any shift in tax burden onto this class would further increase the relative tax burden as a percentage of household income for Niagara (Niagara = 5.2% compared to survey average of 4.8%).
- **Budget Implications** – Should the class be used for an application based relief program the funding requirement would be similar to that noted above regarding tax policy however it would require a budget funding source. For the Region and municipalities that have finalized their 2021 budgets this will require a change to approved budgets.
- **Timing/MPAC Support** – Staff do not believe that sufficient time is available in 2021 to properly implement such a subclass as the annual tax policy will need to be established by April. If implementation were to occur in 2021 there is a high risk that the program will not be successful in achieving desired outcomes. It may also result in in-year administrative complexities causing in-year budget impacts to municipalities in 2021 given that the MPAC assessment roll for 2021 has been finalized and delivered. It should also be noted that MPAC may not be supportive of adopting a subclass that has criteria based on anything other than assessed values or a common approach across all Ontario municipalities.
- **COVID-19 Impacts** – Some of the urgency of implementation may be tied to the impacts of COVID-19 on businesses. However, the financial impacts of COVID-19 are not just limited to small businesses but also effect larger business and residential households. This optional subclass would only address one subset of property owners at the expense of others.

Other Financial Programs Available to Businesses

While this new optional subclass represents another potential tool available for small business it will take time to implement. In the interim there are other supports for the business community that are currently being provided by the Province and Region specifically for COVID-19 assistance, including:

- Business Education Tax Reduction -
 - Addresses the wide range of business education tax (BET) rates across the Province by introducing a uniform rate for 2021.
 - Total annual business property tax saving across Province = \$450M
 - Niagara Commercial savings for 2021 = \$6.6M
 - Niagara Industrial savings for 2021 = \$2.8M
 - Total = \$9.4M
 - No action required for Region - provides property tax relief to non-residential properties without effecting Regional tax policy or other property classes.
- Ontario Personal Protective Equipment (PPE) Grant – provides small business with a one-time grant up to \$1,000 for PPE related expenditures.
- Ontario Property Tax and Energy Bill Rebates - Businesses that are, or were, required to shut down or significantly restrict services due to provincial public health measures can apply for rebates, provided in the form of grants, to help with their fixed costs including municipal/education property taxes and energy costs.
- Ontario Small Business Support Grant - Starting at \$10,000 for all eligible businesses, the grant will provide businesses with dollar for dollar funding to a maximum of \$20,000 to help cover decreased revenue expected as a result of the Province-wide Shutdown effective December 26, 2020.
- Tourism Adaption and Recovery Fund – will provide financial assistance ranging from \$2,500 to \$20,000 for tourism dependent businesses in Niagara to operate within Public Health protocols and thereby retain/create jobs.
- Canadian Emergency Business Account - The CEBA program offers interest-free credit of up to \$40,000 to eligible businesses through their financial institution. If the balance of the loan is repaid by the end of 2022, \$10,000 of the initial loan will be forgiven.
- Canadian Emergency Rent Subsidy - Canadian businesses, non-profit organizations, or charities who have seen a drop in revenue due to the COVID-19 pandemic may be eligible for a subsidy to cover part of their commercial rent or property expenses, starting on September 27, 2020, until June 2021.

Future Considerations

The decision to implement the optional subclass resides with Regional Council which is consistent with other tax policy decisions. The Treasurers from the Region and the Local Area Municipalities have had preliminary discussions on this item and will continue to do so during 2021. Preliminary discussions have also occurred between Regional finance and economic development staff. These preliminary discussions have focussed on both the opportunities and challenges outlined in this report, specifically the challenges that the redistribution of taxes from the subclass may have on other property owners and the disproportionate benefit by municipality that may occur if the subclass eligibility is based on assessed values only.

The Municipal Finance Officer' Association (MFOA) has also provided preliminary comments to the Province and has expressed the need for caution and due care to ensure both the regulatory framework and subsequent implementation of any subclass supports long term strategic objective. MFOA further has commented that municipalities will need time to understand the costs and benefits of the optional small business property subclass including the ongoing toll of administering this specialized class on already stretched resources. Further to this, MFOA notes the importance of ensuring that the solution matches the problem and that the implementation of the subclass is equitable, effective, and efficient.

The proposed changes affect businesses in the retail, food, and accommodation services industry. These businesses represent a significant part of Niagara's economy, and one that has been particularly hard hit by the COVID-19 pandemic. However, excluded from the proposed changes are businesses in the manufacturing, agriculture, and food processing sectors. As a result, the optional small business tax subclass change would favour one sector of the economy over another while at the same time shift the tax burden to residents, who are also being affected by the on-going pandemic.

Further reviews and recommendations may be developed once the Regulations have been published by the Provincial government.

Alternatives Reviewed

Council may provide direction to implement the subclass for the 2021 taxation year however this is not recommended due to the outstanding regulations and necessary analysis. Due to this delay, if implemented in 2021, could lead to delays in the tax rate by-laws for the Region and local area municipalities, tax billing and impact cash flow.

Alternatively, after tax rates are set, it would likely create a negative variance in the annual tax write-off budget as any change to be implemented after the 2021 roll return would cause in-year tax write-offs/adjustments.

Relationship to Council Strategic Priorities

This report addresses Council's priority of Businesses and Economic Growth.

Other Pertinent Reports

None.

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Appendices

Appendix 1 Average Commercial Property Assessment Values by Municipality