

Optional Small Business Property Tax Subclass - Update

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Report Summary

This report provides information regarding the new optional small business property tax subclass announced in the 2020/2021 Provincial Budget.

Relationship to the Strategic Plan, Health Impact Assessment and Community Energy & Emissions Plan (CEEP)

This report refers to operational matters.

Financial Implications

There are no financial implications regarding this item.

Background

As part of the 2020 Ontario Budget the Province announced the new optional small business property subclass. The purpose of the subclass is to provide municipalities with the flexibility to provide tax relief to eligible small businesses.

A report was brought to Council on April 27, 2021, which recommended staff prepare a report with recommendations for 2022 and subsequent taxation years once regulations by the province relating to this optional subclass were available.

On May 7, 2021, Ontario Regulation 331/21 was released, and a follow-up interpretation bulletin was provided by the province, please refer to Appendix 'A' and 'B'. There was also a collaboration with a number of organizations including the Municipal Property Assessment Corporation that published a document titled "Ontario's Small Business Property Subclass: Considerations for Municipalities" that was released in September 2021. This report is contained in Appendix 'C'.

Staff have had the opportunity to research and analyze the legislation and released information. Generally, the regulation is very broad on how the program can be applied and leaves much of the decision making to municipalities including the eligibility requirements and the definition of a small business.

Highlights of the program are:

- A reduced municipal tax rate can be applied to commercial and/or industrial properties that are deemed eligible for inclusion in the subclass as defined by the municipality.
 - The municipality is responsible to set the amount of reduction. This can be up to 35% of the municipal tax rate for the property class.
- All commercial and/or industrial properties (except properties that are or would be classified as large industrial, parking lot and vacant land) are eligible to be included in the subclass.
- Funding the subclass is the responsibility of the municipality. This funding can be completed through:
 - Absorbing the cost through the approved budget (could lead to a corporate deficit),
 - Broadly across all property classes or
 - Within the commercial and/or industrial property classes
- The municipality is responsible for defining a “small business”.
- The municipality is responsible for establishing detailed eligibility criteria for the optional small business subclass.
- The municipality must establish a process for identifying properties or portions of properties eligible for inclusion in the subclass. This can be:
 - application-based or
 - criteria-based not requiring individual applications or
 - both application and criteria-based
- A Program Administrator must be appointed by the municipality and be a municipal employee. The Program Administrator will:
 - Review and approve properties for inclusion in the subclass
 - Provide the Municipal Property Assessment Corporation (MPAC) with a list of properties or portions of properties approved for inclusion in the subclass for each taxation year; and
 - Make an electronic list of properties included in the subclass available for public inspection yearly.
- The municipality must establish a process for property owners to request a reconsideration of a decision on inclusion or exclusion from the subclass.
- An Appellate Authority must be appointed by the municipality and be a municipal employee. The Appellate Authority will be responsible for hearing appeals relating to the Program Administrator’s decisions on eligibility for inclusion to the subclass.
- A municipal by-law must be passed if the municipality chooses to implement the subclass that clearly defines the criteria of the program.
- The province has indicated that they may consider matching the municipal property tax reductions with education property tax reduction.
 - The municipality has a requirement to notify the Minister of Finance of their decision to adopt the subclass, submit their municipal by-law and estimated total municipal tax relief.
 - The municipality would have to conduct consultations with stakeholders.

- The Minister will review each submission and determine whether to match municipal reductions on case-by-case basis.

The review and research completed by staff revealed that there are several challenges that municipalities face in implementing the new optional small business property tax subclass. There are four major challenges:

- 1) Defining and determining the businesses to be included in the subclass.
- 2) Determining the amount of the discount for the subclass (up to 35% allowed).
- 3) Determining how to allocate/distribute the total discount to the other property classes.
- 4) Determining the administrative cost of the new subclass.

Challenge 1 - Defining and determining the businesses to be included in the subclass

One of the biggest challenges is defining and determining the small businesses that should be included in this new property tax subclass. Targeting the small businesses that the City of Greater Sudbury would want to provide tax relief, in the form of a discount, can be difficult and there isn't widespread consensus on how "small business" should be defined or identified. The definition could be based on an ownership model, total revenues, number of employees or number of locations that the business operates in, or the amount of floor space occupied.

Depending on the how the definition is determined an application process may be required to gather the necessary information. This would enable small business operations to be more specifically targeted but would require more extensive administrative procedures and labour resources, with data verification difficulties on an ongoing basis year after year.

The City could consider how to define a "small business" in a way that can be captured in the Municipal Property Assessment Corporation (MPAC)-managed assessment roll. Although property classification is normally performed by MPAC, in this case, municipalities would have to identify the roll numbers to be included in the small business subclass based on their definition. Municipalities do not have broad experience in determining the eligibility of properties for a particular property class. Input will be required from MPAC as to how to define a small business and maintain the assessment roll in a practical manner.

Whatever method is utilized to determine the small business subclass there will be several complexities and difficulties in achieving an equitable and fair system. One major difficulty would be in the circumstance where many small businesses that would be included in the subclass are tenants. Will the property owners pass on the property tax savings to the tenants or do the property owners feel they should be the beneficiary of the subclass?

With the difficulties and complexities in determining the subclass it is unclear as to whether the introduction of such a subclass will ultimately benefit small business owners.

There are also the issues that no matter how much effort is put into developing this new subclass there will likely be adverse reactions for those businesses that are deemed not to qualify.

Challenge 2 - Determining the amount of the discount for the subclass

Choosing a meaningful discount amount that helps the targeted businesses in the subclass can be difficult. If the amount is not substantial it will not be deemed beneficial to small businesses in the subclass. If the amount is substantial, it exacerbates challenge 3 in distributing this savings as a major increase to the other property classes.

This discount can be implemented at any percentage up to 35% of the full taxable rate that would be applied to commercial and/or industrial properties that are not eligible for inclusion in the subclass.

Challenge 3 - Determining how to allocate/distribute the total discount to the other property classes

As the Province does not fund this program, the responsibility would be with the municipalities to fund the program. Consistent with other property subclasses, municipalities can fund the small business subclass either by absorbing the cost through the approved budget or by funding it broadly across all property classes or by funding it within the affect tax classes.

The overall levy required will not change, it will simply shift the tax burden on to other property classes, such as residential and/or those commercial and industrial properties not eligible for a discount.

Challenge 4 - Determining the administrative cost of the new subclass

Determining the administrative cost of developing, implementing, and maintaining the new subclass will be difficult. If an application process is required, the additional labour costs would be substantial. The new subclass will generate ongoing appeals and require the confirmation of continued eligibility to the program and the addition of new eligible properties to the subclass. In addition, the program requires the municipality to appoint a Program Administrator and Appellate Authority.

As the City of Greater Sudbury has approximately 2,934 properties classified as commercial or industrial, with approximately 4,900 registered businesses the challenges listed are a factor when evaluating implementation of a new subclass.

An example of such challenge is a strip mall. This property may not qualify as a small business but there could be multiple units within the property and some or maybe all the units would contain tenants that may need to be classified as small businesses. This property could also have a mix of tenants where some would be classified as small business and others may fall under the regular commercial or industrial classifications. How are these units/tenants identified? Who benefits from the reduction, the property owner, the applicable tenant or all tenants? How is the distribution of this saving monitored or enforced?

As result the many challenges, determining the effect on the tax levy and shift of the tax burden along with administrative cost of this new subclass cannot be determined at this time. Implementation would require additional resources to support the program.

It is important to note that even though this new subclass was introduced by the province during the active COVID-19 pandemic, this is not a measure intended to provide COVID relief to small businesses. Should a municipality opt to adopt this new small business property tax subclass, it is a permanent measure that would require Council approving a by-law to discontinue the relief/use of the subclass.

The federal and provincial governments provided businesses with many different temporary funding options to assist with expenses such as property taxes throughout 2020 and 2021 to assist with difficulties experienced as a result of the COVID-19 pandemic.

Staff have researched and determined that most municipalities within the province are not implementing the new optional small business subclass. Like most other municipalities, staff recommend that the City of Greater not implement the optional small business property tax subclass due to the many complexities and challenges with the program.

To date, the City of Toronto and the City of Ottawa are the only two municipalities that staff are aware of that have opted for this new subclass. Both municipalities have set parameters using the MPAC managed assessment rolls to define their subclass.

The City of Toronto is implementing a 15% reduction for the new subclass for commercial properties. This new program is being funded by eliminating the graduated tax rates for the commercial property tax class and adopting a single tax rate. The definition of small business is based on a geographical approach that considers different factors based on location.

The City of Ottawa is phasing in a discount of 15% over two years. The new subclass is being funded through the elimination of the 30% commercial excess land discount and the 35% industrial excess land discount currently available through the excess land subclasses. This elimination is also being phased out over two years. The definition of small business considers many factors including property use and size.

Summary:

Municipalities and municipal working groups have discussed the implications and complications associated with the Optional Small Business Property Tax Subclass. To staff's knowledge except for Ottawa and Toronto, most municipalities have decided against implementing this subclass given the complexity of the program. They considered that additional staff will most likely be required to support the program, the potential for adverse reactions for those businesses that are deemed not to qualify, and the fact that all other tax classes, including residential, will need to adsorb the cost of not only the tax relief, but also the overhead cost of administering the program.

Overall, municipalities are unsure as to whether the introduction of such a subclass will ultimately benefit small business owners.

Staff is recommending that the optional small business property tax subclass not to be implemented for the 2022 and subsequent taxation years and that the property tax classifications remain status quo.

Staff will continue to monitor the legislation for changes that would alleviate or streamline the challenges with implementation and report back to the Finance and Administration Committee with any such updates.

Resources Cited

Ontario Regulation 331/21 – Appendix 'A'

Small Business Subclass Bulletin – May 2021 – Appendix 'B'

Ontario's Small Business Property Subclass: Consideration for Municipalities – Appendix 'C'