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Halifax Regional Council

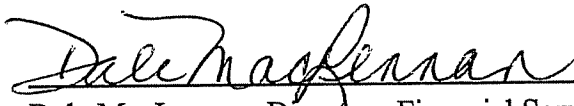
August 9, 2005

September 6, 2005

TO: Mayor Kelly and Members of Halifax Regional Council

SUBMITTED BY:


George McLellan, Chief Administrative Officer


Dale MacLennan, Director, Financial Services

DATE: August 3, 2005

SUBJECT: Revenue Strategy: Proposed Tax Reform Initiative

ORIGIN

This report originates with a motion of Council (April 16, 2004 by Councillors Uteck and Fougere) that staff investigate alternatives to the current property tax system and a staff recommended 2005/06 project to undertake a Revenue Strategy. Tax Reform is one of three key elements included in the Revenue Strategy.

Subsequent to that motion, staff discussed taxation and taxation issues at the Program and Service Review Committee and at the March 8, 2005 Committee of the Whole meeting. As part of the Revenue Strategy approved in the 2005-2006 Business Plan, staff committed to returning to Council with an overview of the issues and processes surrounding Tax Reform. Tax Reform is one of several key elements of the Revenue Strategy.

RECOMMENDATION

It is recommended that

- 1) Regional Council authorize staff to move forward with the Tax Reform initiative as outlined in the attached report,
- 2) Staff proceed to request broader tax powers from the Province of Nova Scotia including a one-year extension to the Temporary Tax Credit.

BACKGROUND

While market value assessment is the traditionally accepted method of levying property tax and, in Nova Scotia's case, the only significant tax power available to municipal government, there is increasing concern over the relevance of the market value approach in HRM.

In the past several years HRM has experienced unevenly distributed market value increases across the municipality. More and more these increases have a limited correlation to changes in services available, the cost of the relevant municipal programs or the ability of the individual homeowner to pay. In HRM, and a handful of other municipalities, citizens have become increasingly frustrated with the market value system. The manner in which tax rates and assessments are combined to produce a tax bill, lacks credibility.

The traditional tools available to municipal governments in terms of the number of tax rates and rebates or deferrals, are unable to respond adequately to these uneven changes in market value. On a per dwelling unit basis, HRM expenditures per dwelling unit have not risen dramatically in the last 10 years, rising only slightly more than inflation. Moreover, on average, residential taxpayers have seen very slow growth in the average tax bill. The average tax bill, however, disguises the sharp variations in increases and (to a lesser extent) decreases across the region. Individual tax bills can rise and fall (sometimes dramatically) due to changes in individual property assessments. These changes can occur regardless of the changes in HRM's expenditure levels. This leaves HRM in a quandary. To respond to those experiencing significant assessment increases, drastically cutting the budget would lower HRM's ability to deliver services to residents. If HRM ignores the high assessment properties and sets rates based on average assessment increases this ignores the legitimate concerns of some taxpayers over tax bill increases that relate only to market growth and lessens the predictability of the tax bill year over year.

All of this begs the question whether individual residential properties are paying the appropriate amount of tax. A wide variety of factors lead to changes in assessed values. This is especially true in a quickly growing municipality such as HRM where market values are being driven by factors such as low interest rates, solid economic growth and an attractive real estate market in certain neighbourhoods. As a result, the correlation to municipal services, costs and income are becoming weaker and weaker. Interestingly, these conclusions are not altered as assessed values comes closer to market values. In fact, to the extent that the increase in assessment values is related to factors other than increases in municipal services such as interest rates and real estate markets, the accuracy of assessment values to market values does not improve the appropriateness of tax bills to individual residents. All of this implies that some taxpayers are paying excessive amounts of tax while others are paying insufficient amounts of taxation. Without the means to improve the appropriateness of individual tax bills to residents, the risk exists that there will be a deterioration in the confidence in municipal government and fiscal instability.

For the immediate 2005-2006 fiscal year Council has approved a one-time Temporary Tax Credit to provide some relief to property owners with high assessment increases. This is only a temporary measure with the original intent being to replace it in 2006-2007 with permanent reforms to the

current municipal tax system.

DISCUSSION

As part of its 2005-2006 business planning objectives HRM is undertaking a medium term Revenue Strategy to address a number of interrelated issues. The purpose of the Revenue Strategy is relatively broad and includes:

- i Ensuring a competitive local government environment
- ii Allowing for an understandable and predictable tax system for residents
- iii Balancing the reliance on market-based assessment and other forms of taxation and charges, and,
- iv Providing consistent and sustainable revenues to support day-to-day and planned municipal operations.

There are three key areas that the Revenue Strategy is intended to focus on:

- (i) Property Taxation (Residential & Commercial)
- (ii) Other forms of Taxation & Charges (including Sewer Charges)
- (ii) Broad Fiscal Policies (including debt, reserves and capital)

It is anticipated that over time the Revenue Strategy will provide Regional Council with specific recommendations. These recommendations relate to:

- (i) Elimination of the Business Occupancy Tax (BOT)
- (ii) Sewer rates and Capital Cost Contribution (CCC)
- (iii) Support for the Long-Term Capital Plan
- (iv) Debt and Reserve policies
- (v) HRM's competitiveness

Several of these areas will require decisions by Council in 2005-2006. The elimination of the BOT and the establishment of long term sewer rates are both issues that staff intend to present recommendations to Council on during this year. Staff also hope to provide Council with the results of a study on Capital Cost Contribution and and the resulting recommendations. The creation of a longer term capital plan, revisions to debt and reserve policies and competitiveness are all issues that staff intends to present to Council during this year but not all recommendations will be finalized during the current year.

One of the key areas that the Revenue Strategy is intended to focus on is reducing HRM's reliance on the "market value" property tax system. This includes finding a replacement for the Temporary Tax Credit.

The Revenue Strategy was described extensively in the Draft Regional Plan but is not dependent upon approval of the Draft Regional Plan. Rather, Tax Reform has been discussed extensively at

Council and the current initiative is the direct result of Council's desire to see reform in this area.

There are a number of key stakeholders whose involvement is critical to the success of the Revenue Strategy. First and foremost amongst them is the general public, citizens, business groups and taxpayers who need to feel that the tax system serves their interests and provides for a fair balance between providing services and collecting revenues. This includes a wide variety of individual ratepayers and citizen groups that should be consulted on the direction of any tax reforms. There are also numerous business groups that have a keen interest in the Revenue Strategy as well as the Province of Nova Scotia, the Union of Nova Scotia Municipalities and a number of interested Nova Scotia municipalities. The success of Tax Reform relies upon strong stakeholder support that is representative of all areas and facets of HRM.

Public consultation, therefore, will be a critical element of Tax Reform. It is imperative that those consultations focus on the intended principles and outcomes of a prospective tax system. Once there is some agreement as to what HRM is trying to achieve through its tax system, those objectives can be evaluated against the various tax options.

The Principles of a Revised Tax System

Any Tax Reform initiative should have at its heart a series of principles that govern the evaluation of proposed reforms. The current market value system assumes there is a strong relationship between available services, the cost of services and the ability to pay. These relationships are unclear and there is no consensus amongst either academics or the public at large as to how strong or valid such relationships are. As discussed, such relationships are tenuous in practice in the HRM market.

Keeping in mind the need to balance service levels, cost of services and ability to pay, several foundation principles should underlie any public debate or discussion on Tax Reform. These principles are subject to open debate and may change as Council and the public engage in deeper discussions on what they wish to achieve through the tax system. As a starting point these principles can be described as:

1. **Transparency** - There should be a clear link between the package of services available, the taxes paid and how those taxes are calculated. Any tax system should be highly transparent and lend itself to high accountability.
2. **Equity** - Taxpayers benefitting from similar services at similar costs should expect to pay similar tax bills. Variations in services and costs may be reflected in the taxes levied. It follows that the principles of that tax system need to be consistently applied.
3. **Stability** - Taxes levied should increase and decrease in a predictable fashion so that taxpayers and government can understand and reasonably anticipate changes in taxation and so there are no sudden or unexpected shifts.
4. **Competitiveness** - Taxes levied should encourage sustainable, growth-oriented and appropriate behavior on behalf of both taxpayers and government.
5. **Simplicity** - Any reformed tax system should be capable of being easily administered by both taxpayers and government.

The Options for a Reformed Tax System

Once the foundation principles and any intended implications or outcomes become clearer, it will be necessary to debate the various tax mechanisms that exist. There are many possible options for a reformed tax system, all of which require extensive research, debate and consultation. These options could be used in whole or in combination. Most options will require some legislative changes in Provincial law so caution should be used in reviewing these options. Staff intend to work closely with Provincial officials to ensure that the appropriate tools are available.

It is also important to recognize that the dollar impact to individual citizens will vary depending on what changes from the existing system are considered and ultimately adopted. For every fewer dollars one individual might pay, these amounts will be paid by other taxpayers.

Five main tax mechanisms can be identified for municipal tax reform. These mechanisms can be combined to provide a number of alternative tax systems. These mechanisms can only be evaluated against the principles that HRM decides must govern its tax system.

1. **The Current Tax System** - While some aspects of the status quo appear unacceptable, it may be that after a series of research and consultation on the alternatives, that it becomes the preferred approach. Some changes such as a maximum tax or the use of area rates could be considered under the existing system
2. **A Modified Assessment System** - There may be options to reform the current assessment system. These might include using a standard cost for the value of land, using only the value of structures, or using other methods of valuation. These will require Provincial concurrence and may be difficult to implement.
3. **New or Swapped Tax Powers** - Municipalities could explore opportunities for new tax powers such as income taxes, sales taxes or fuel taxes or with unconditional grants. As part of these arrangements they might decrease their use of property taxes. These will require not only legislative changes but may require changes in Provincial tax and fiscal issues.
4. **User Fees** - HRM could increase its use of user fees such as for recreation, solid waste collection or roads. Property taxes could be accordingly lowered. The use of user fees could be used in combination with other options.
5. **Dwelling Unit and other Charges** - A variety of other levies and fees might be used alone or in combination to reduce dependence on the market value assessment. These include dwelling unit, frontage, property and acreage levies. They might also include such features as maximum and minimum taxes. Options affecting deed transfer taxes will be examined.

An important companion to any reformed tax system may be revisions to HRM's low income rebate and deferral programs.

The Process and Time line for Tax Reform

Staff had originally intended to complete the necessary work for Tax Reform in order to allow reform options to be available for the 2006-2007 fiscal year. A full range of public consultation is critical to the success of this initiative, therefore to ensure adequate time for meaningful input, this timeline is not recommended. Moreover, undertaking consultations in the Fall would be coincident with Regional Planning consultations and could be confusing to the public.

It is intended that there are six main stages for Tax Reform.

1. **Discussion Paper for Public** - In December, Staff intend to table a draft discussion paper with Council. The intent of the discussion paper is to outline issues, principles and options for tax reform.
2. **Tax Workshops** - Starting in January, a series of Tax Roundtables will be held throughout HRM to examine the issues, principles and options for Tax Reform.
3. **Tax Conference** - Following the completion of the Tax Workshops, a Tax Conference will be held. Invites will include Council, attendees at the Roundtables and others. The intent is to build a consensus on the tax system.
4. **Tax Proposal** - Following the Tax Conference, staff intend to return to Council with the results of the Tax Roundtables and Conference and with specific recommendations and implications of any changes to the tax system.
5. **Council Recommendations** - Council will debate the future of the HRM tax system. It is anticipated that a decision for the purpose of additional public consultations will be made by April of 2006.
6. **Community Council** - During the Spring of 2006 a second set of public consultations will take place before Community Council outlining the revised principles, options and the specific impacts of any recommendations.
7. **Final Recommendations** - In June staff will make final recommendations on the principles and on revisions to the property tax system for 2007-2008 and future years.
8. **Implementation** - Depending on the specific recommendations accepted and any legal or legislative changes required, implementation of any revised tax system will begin in 2007 although it may be phased in over more than one year. HRM may have to work with the Province on implementation issues.

Work on the commercial tax burden is underway at the moment and will continue. The issues surrounding commercial tax burden and their impact upon economic competitiveness are critical elements of the Revenue Strategy. These issues are to be linked into HRM's Economic Strategy.

It is intended that the Tax Reform initiative be led by a Revenue Strategy Steering Group headed by the CAO and senior staff. Councillors will be consulted through the Steering Group and through Program and Service Review. All councillors would be advised of meetings and would be free to attend.

In addition, there would be a Stakeholder Advisory Committee that would consist of citizen and business groups across HRM.

Legislative Issues

Initial research by staff has confirmed that HRM's taxing powers are relatively narrow in scope. For instance, the Municipal Government Act (MGA) does permit the use of dwelling unit, frontage, acreage and property charges in only very narrow circumstances. The Act does not permit the use of a maximum tax. It is recommended that HRM request amendments to the MGA to allow the broader use of such taxes. Regardless of whether these taxes form part of the solution to HRM's tax issues or not, it is important that the tax options available to HRM be as broad as possible. Additional legislative changes may also be requested.

In addition, HRM will request that an extension be granted to the Temporary Tax Credit. Currently, the credit is limited to one year only.

BUDGET IMPLICATIONS

There are no immediate budget implications to this report.

Funds for the Revenue Strategy (\$50,000) were added to the budget of Financial Services to assist in the development of this strategy. Financial Services expects to allocate other internal resources to the research and communication efforts involved.

FINANCIAL MANAGEMENT POLICIES / BUSINESS PLAN

This report complies with the Municipality's Multi-Year Financial Strategy, the Approved Operating, Capital and Reserve Budgets, policies and procedures regarding withdrawals from the Capital and Operating Reserves, as well as any relevant legislation.

ALTERNATIVES

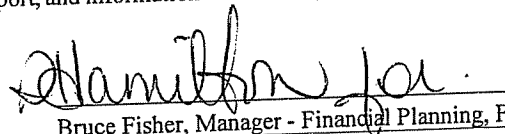
Staff could return to Council in the Fall with recommendations and options for Tax Reform. This may not allow for a wide range of public consultations.

ATTACHMENTS

None.

Additional copies of this report, and information on its status, can be obtained by contacting the Office of the Municipal Clerk at 490-4210, or Fax 490-4208.

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490-4493