

# NEWS BRIEF



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## A PARADOX IN ASSESSMENT REFORM

On January 1, 1970, the Province assumed responsibility for the assessment of all real property in Ontario. The takeover of the assessment function was the culmination of a long standing provincial-municipal struggle regarding assessment reform.<sup>1</sup> The Province was motivated by its own need for a standard measure of municipal tax bases for an evaluation of municipal needs and the establishment of priorities. The necessary standard was a uniform assessment at full market value of all real property in each municipality. Full market value was selected because of its wide acceptance as indicator of economic utility and as a measure for valuating and comparing all types of property. Despite the demonstrated poor quality of many municipal assessment programs,<sup>2</sup> the municipalities, resisted assessment reform, and appeared to be more interested in maintaining their own historically determined levels of assessment rather than undertaking improvements that might have resulted in drastic shifts in their municipal tax burdens. In the Assessment Act of 1968-69, the Province by-passed municipal intransigence to reform by centralizing assessment administration to the provincial level establishing market value as the criteria for fair and equitable assessment, and undertaking a program of reform in assessment practices.

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<sup>1</sup> Bureau of Municipal Research, Assessment Reform: Redistributing the Tax Burden, 1970.

<sup>2</sup> Bureau of Municipal Research, Assessment--The Recurrent Controversy, 1966



Symbolic of the reform approach of the Assessment Division in the Department of Municipal Affairs has been the abolition of land and building assessments on assessment rolls in favour of a single total assessment for each property. This is a change that has not gone unnoticed or unchallenged by municipal officials and tax agents. Prior to the provincial takeover, the division between land and buildings was an integral part of municipal tax structure. The assessment appeal procedure in particular was based on the separation of land and building values. Assessment appeals were often initiated on the basis of incorrect assessment of the land or the building portion of the total assessment, separate from any consideration as to the accuracy of the total assessment figure. Likewise, in reviewing the evidence presented in assessment appeals, the courts examined and based their decisions on the assessed value of the land and buildings more as discrete units than as interrelated in a total assessment.

The elimination of discrete values for land and building assessments on the assessment roll has been explained by the Assessment Division in terms of the theory of market value assessment. The theory suggests that the market value of a property cannot be properly apportioned between the land and the buildings because the two values are interdependent, not independent of one another. The value of the structure is in part determined by the nature of the site and its location; the value of the land is in part dependent on the characteristics of the structure and the economic use to which it is put. The value of the whole property, then, can be greater (or in some cases less) than the sum of the parts (considered independently of one another). Commercial properties in the downtown



business section are often examples in which the market value is greater than the cost replacement of the building (a measure of building value independent of site considerations) plus the market value of the land (considered as independent from the building, i.e. as a vacant lot). Because of the interrelationship between the land and building assessments, any apportionment of the total market value of such a commercial property is to a significant extent arbitrary and meaningless. The opposite situation can also occur. In a case where the potential economic use of the property cannot be achieved without demolition of the existing structures, the total value of the property is less than the sum of the parts.

Although the argument for a single recorded total assessment is a logical consequent of the theory of market value assessment, it is not a logical consequent of the realities of current assessment practices. The assessment of real property at the practical level has always functioned on the assumption that buildings and land could be valued in discrete units essentially independent of one another. This assumption is embodied in the assessment techniques for estimating replacement costs of any given structure plus the value of land on a pro rata basis to provide a total assessed value. Used by a trained and experienced assessor, these basic tools of analysis (in combination with rental and sales data where available) can be used to achieve a high level of precision ( $\pm 10\%$ ) in assessments at full market value.

The disjunction between the theory and the practices of market value assessment has created a paradoxical situation in the policies of the Assessment Division. On the one hand, they are eliminating separate land and building values on the assessment rolls in order to emphasize that



their sole concern is to provide market value assessment of whole properties which is not the same as assessing land and buildings separately and summing them together. On the other hand, they are forced to separate land and buildings in their own assessment practices because they lack the technical ability to do mass appraisal programs any other way. Why do they suggest on the one hand that apportionment between land and buildings is not relevant in the analysis of assessments and then on the other, give credence to the concept of apportionment in terms of their assessment practices? There are two possible reasons for the maintenance of the single total assessment in face of this paradox:

1) There is obviously a certain percentage of cases where the apportionment between land and buildings is meaningless (as argued above) such that any apportionment is not really defensible in its own terms. In these cases, the only meaningful assessments are full market value assessments of the total property. Previously, the owners of these properties were able to appeal either the land or the building assessment in hope of an ultimate reduction on the total assessment. In such cases the assessors were often able to defend the total assessment, but unable to defend the apportionments.

2) Although the procedures for assessing properties violate the assumption of interrelatedness expressed in market value theory, the Division has been refining a new system of working with exclusively market values through the application of existing sales data. If this system is implemented in the seventies, it will of course make obsolete the land and building approach to market value which has been depended upon to date. The policy on single total assessment, then, may be interpreted as a forward



looking policy which attempted to adjust people to the changing bases of assessment.

There is obviously some merit in these arguments, but for the more critical observers it might also be noted that:

1) The Assessment Division has the cart before the horse. There are strong arguments for keeping the policies of information disclosure on the assessment rolls consistent with assessment practice rather than assessment theory. As long as the Division continues to use assessment practices that make a substantive division between land and buildings, the results ought to be reported in a similar manner. The new policy has eliminated that proportion of appeals based on the separate land or building assessments. Appellants are now obligated to appeal the total assessment rather than tying the appeal directly to the land or the buildings.

The strategy of the Division in making their change to a single total reported assessment was politically opportune. It was lost in the shuffle and confusion of much more dramatic changes in assessment administration; had the change been made seven to ten years from now (when assessment techniques are estimated to catch up with assessment theory) its impact as a political issue would, no doubt, have been more dramatic.