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The Impact of Property Taxes in Metro

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The Ontario Committee on Taxation, a Royal Commission studying taxes and revenues available to the Province of Ontario and its local governments invited organizations to submit their views with respect to these matters. The Bureau's submission was concerned with public finance in Metro Toronto. It was based on three propositions:

(a.) that requirements in terms of financial resources and service responsibilities in Metro Toronto and region are extraordinary and require special arrangements;

(b.) that the financial resources available to the metropolis are shrinking in relation to need and that the revenue base of Metro must be broadened and made more flexible to accommodate the requirements of the future;

(c.) that the sharp distinction between responsibilities of the Province and municipalities, while still true in the case of most municipal governments, is outmoded in terms of Metro Toronto and the Hamilton-Toronto axis and that a formalized structure for a closer partnership arrangement between Metro, the Province, and when appropriate, federal authorities at a public-policy level is necessary.

This bulletin reproduces extracts of argument in the Bureau's brief supporting the second proposition. Five fiscal problems having a particularly sharp impact in the Toronto region are discussed.

TABLE I

EXPENDITURES OF LOCAL GOVERNMENTS
1955, 1961.

	1955 (000's)	1961 (000's)	Variation %	1955 Per capita expenditure*	1961 Per capita expenditure*	Variation %
PROVINCE	$448,183	857,717	+ 91%	$ 89.40	$145.00	+61%
METRO TORONTO ..	154,173	306,843	+ 99	118.41	198.00	+60
City	91,594	141,471	+ 53	134.30	220.00	+61
Inner Suburbs	22,640	38,843	+ 72	84.00	133.00	+58
Outer Suburbs	38,018	104,060	+274	108.00	168.00	+56
PROVINCE EXCLUDING METRO	294.010	550,874	+ 87	79.24	125.00	+58

Source: Municipal Financial Statistics — 1955, 1961, Department of Municipal Affairs, Toronto.

*Based on assessed population.

EXPENDITURES AND THE EXPLOITATION OF RESOURCES

The first fiscal problem involves the pattern of metropolitan expenditures and resources, and the relationship between them. In Table I, expenditures for all municipalities in the province, Metro Toronto, and its constituent parts, and municipalities in the province excluding Metro are shown for the years 1955 and 1961.

The Table shows that total expenditures in Metro increased substantially more, between 1955 and 1961, than was the case for municipalities throughout the province. They represent a higher per capita level of expenditures than elsewhere ($198-$145). However, it is interesting to note that the rate of per capita increase throughout was about equal, ranging between 56% and 61% in the six year period. Great though the difference in expenditure is, the heavy increase in Metro weights the provincial figure which, excluding Metro, is considerably less ($125).

By this measure, there is a spread of $73 per capita between Metro and municipalities in the balance of the province in regard to overall per capita spending.

Growth in Metro's expenditures has been great but there are wide divergencies within. Expenditures by the 'outer suburbs' increased by a staggering 274% during the period. This was more than three times the provincial average (excluding Metro). Expenditures in the City increased at a less rapid pace, growing by 53%. Yet in spite of this, per capita expenditures in the City far exceeded those in the rest of Metro and the province. This paradox is explained, in part, by the decline in population experienced by the City.

Table II illustrates how per capita expenditures, arranged according to services, vary between the large metropolitan area and small urban, and rural municipalities. Though the figures do not necessarily reflect levels of services, which usually are higher in the larger municipalities, they do

TABLE II

CURRENT EXPENDITURES PER CAPITA
For Select Urban and Rural Municipalities in Ontario, 1960.
($)

Municipalities	Metro Toronto	Cities (excluding Toronto) over 250,000*	50,000 to 120,000	20,000 to 49,999	under 20,000	Townships 5,000 and over	under 5,000
General Govt.	10.35	8.68	10.80	8.19	8.07	5.93	4.21
Protection	26.03	23.43	23.82	19.65	19.98	5.52	1.57
Public Works	14.72	9.17	9.05	11.72	11.57	17.49	26.61
Sanitation & Waste	11.17	7.66	9.14	6.53	5.38	.88	.17
Health	4.19	3.92	4.39	2.62	1.85	.38	.30
Welfare	10.64	8.73	9.02	7.24	4.85	2.54	1.56
Education	61.87	46.85	44.33	43.73	45.68	42.29	29.62
Recreation	9.43	5.19	6.98	6.14	5.24	1.35	.35
Debt	28.74	26.87	19.80	22.34	17.65	9.78	3.95
Total	188.69	149.82	146.14	138.48	127.24	105.38	86.59

*In 1960 there were no cities in Ontario in the population group 120,000-250,000.

Source: Local Finance, May 1962, Canadian Tax Foundation.

illustrate the spending desires of residents as interpreted by elected representatives.

The full effects of these expenditure levels must be measured against the resources by which they are supported. Table III shows expenditures for the year 1960 as a ratio of gross personal income and the assessed value of real property for all municipalities in the province, Metro Toronto, and the rest of the province (excluding Metro) thereby revealing the relative burdens which the financial requirements of local government places upon the tax-paying capacities of the jurisdictions shown.

As indicated in Table I, the proportion of expenditures of Metro Toronto, amounting to $307 million in 1961, represented 36% of total expenditures by municipal governments in the province. This high level of expenditure, which substantially exceeds the metropolitan area's share of population, also places a high but uneven burden on its tax-paying capacity. When these expenditures are related to resources, an amount equal to 9.7% of personal income in Metro is required to support expenditures. On the other hand, an amount equalling 7.8% of the assessed value of real property was dedicated to the provision of local services by Metro in 1960. By contrast, 9% of the personal income of the province's 6 million people and 8.8% of those living in municipalities outside Metro was required. The same division indicates that 8.4% and 8.7% respectively of the assessed value of real property was consumed. Variation in the ratio of assessment to expenditures decreased in 1962.

Thus, expenditures in Metro, in relation to personal income, were higher than the balance of the province, and expenditures, as a percentage of assessed values, were slightly lower.

The latter relationship is due in part to a higher per capita value of real property in Metro ($2,403) than in all other municipalities in the province ($1,620), and the province excluding Metro (1,345). In addition, Metro enjoys a very high level of business assessment ($305/cap.) which is not matched throughout the province ($178/-cap.), or in the province excluding Metro ($134). If the effect of business assessment is eliminated, the difference in the ratio of expenditures to the assessed value of real property is reduced to .4% in 1960 and .2% in 1962. But the lower than average burden on real property in Metro also reflects a generally higher level of property valuation in the metropolitan area than in the balance

TABLE III

LOCAL GOVERNMENT EXPENDITURES AS A BURDEN ON RESOURCES — 1960

	Total Local Govt. Expenditures* ($000's)	Ratio Expenditures to Personal Income (%)**	Ratio Expenditures to Value Real Property (%) 1955	1960	1962
Province	$790,070	9 %	6.8	8.4	7.9
Metro	285,616	9.7	6.0	7.8	7.6
Rest of Province	504,454	8.8	7.4	8.7	8.2

Source: *Municipal Financial Statistics, 1960, Department of Municipal Affairs, Toronto.
**Taxation Statistics, 1960, Department of National Revenue, Ottawa.

of the province requiring less intensive exploitation of the tax base.

In one respect at least, differences between levels of expenditure and fiscal burden are greater within the metropolitan area than is exhibited between Metro and the rest of the province. Unfortunately, data relating personal income to the various divisions of the metropolitan area are not available so that expenditures cannot be compared internally. But an analysis of 1961 expenditures as a ratio of assessment indicates that wide variations exist. The City of Toronto must dedicate 7.9% of the assessed value of its real property to support expenditures in spite of a very favourable balance of business assessment. The outer suburbs devote 7.3% and the inner 6.2%, indicating an overall range of 1.7%. To express this effect in dollars, the City of Toronto would have had to reduce its 1961 expenditures by $14 million dollars before reaching the average ratio of expenditures to assessment in Metro of 7.1%.

This analysis of expenditures and resources is revealing. In the first place, expenditures in Metro have increased more rapidly than is the case in relation to all municipalities in the province, presently accounting for more than one third of all municipal expenditures. Within Metro, the increase has been uneven. There have been extraordinary increases in the suburbs but this has been matched by population and assessment growth. The City has experienced a relatively modest increase in its level of expenditures but a declining population, and rising costs have resulted in high per capita outlays.

When expenditures are related to resources, expenditures in Metro are greater in relation to personal income than is the case throughout the province and, due to a high level of residential and commercial assessment, a slightly lower than average proportion of its real property assessment. However, significant variations within Metro indicate important differences in relative burden.

COSTS OF THE METROPOLIS

A second major area of fiscal significance lies in what might be called the inherent costs of the metropolis, or its financial efficiency. This general heading suggests a multitude of problems ranging from functional efficiency of civic administration to the application of the community's resources. But a further question of importance concerns the area of the metropolis in relation to the provision and cost of various services.

This is a matter about which little is known but in which interest is growing. Two recent studies, one in St. Louis and another in the New York Metropolitan Region, attempted analyses of this nature. While the conclusions of both studies apply only to the specific areas examined at a particular period of time, it is worth observing that variations in the per capita costs of the services studied depended more on tax paying capacity, service quality indices, and urban densities, than upon the geographic or population size of the functional area served. Somewhat similar conclusions were reached in both studies.

In any metropolitan community with divided jurisdiction, there is financial inefficiency — in the duplication of executive bodies, for instance, or possibly in the scale of functional administrative areas although there is no conclusive evidence of this. These costs should be recognized where they exist. At the same time, thoughtful consideration should be given to the "social" or "political" efficiency of administrative jurisdictions of varying size which may offer satisfactions and controls that are worth their economic

price to inhabitants of the metropolis. Nonetheless, there appear to be inherent costs in a decentralized distribution of public authorities in a large urban centre.

CHANGING SIGNIFICANCE OF REAL PROPERTY

Another problem resulting from the fiscal requirements of the metropolis arises from the fact that the significance of real property as a community asset is changing. This is occuring as technology alters the pattern of real property consumption by some land users and its location throughout the metropolitan area. In addition, personal wealth is now held more in other forms and less in real property than once was the case. The productivity of the property tax faces a long-term decline. The property tax does not reflect, and cannot be adapted to these changing conditions with a consequent alteration in the fiscal resources of various sections of the metropolis. A few examples will illustrate the point.

Automobiles and rapid transit have wiped out the earlier pattern of residential and employment location. Where workers once were required to live in the immediate vicinity of their place of employment, they can now scatter far beyond. In the same way, industrial and manufacturing concerns have been liberated from the core areas and can locate wherever they like in the knowledge that they will remain accessible to employees, markets and supplies. Thus, an inhabitant of the metropolis may live in one municipality, shop in another, and work in a third. Where at one time, a resident paid property taxes in the municipality providing him with the public services he consumed, this is no longer the case. The traditional balance of population, tax resources, and responsibilities has changed resulting in unequal burdens in some sections of the metropolis. For instance, some municipalities, especially the central city, derive no direct tax revenues from many of those who use their services intensively. This is reflected in the fact that 67% of the value of exempt properties in Metro (roads, public buildings, etc.) are located in the City of Toronto and 16% of the assessed value of property in the City itself is exempt from the property tax.*

It appears, as well, that with the changing pattern of industrial production, the property tax imposes a greater burden than in the past on the tax paying capacity of some types of businesses in relation to others. Extensive, single story structures now house industrial and manufacturing concerns which require the efficiency of one floor production. The consumption of land by such enterprises is great and the higher property taxes imposed cannot reflect the fact that there is not necessarily an accompanying increased ability to pay.

A further anomaly appears in regard to the changing function of the central core of the metropolis — its most productive tax resource. There has been a significant dispersal of manufacturing and industrial activity from the City to the suburbs and beyond. As the metropolis grows, as greater specialization in terms of selling, advertising, negotiating, research, and financing develops, service industries increase in importance replacing the earlier types of land uses. These industries must be in close proximity to one another and to the commercial and government concerns they service. Thus, they cluster in the central business district and in the future are likely to become the predominant function in the area.

Whereas relocated manufacturing concerns require expanded physical facilities and sites, service industries act in quite the opposite direction occupying much smaller physical facilities than industrial concerns

**Municipal Tax Exemptions, Bureau of Municipal Research, April 1963.*

in relation to the value of their production. As a result, while the central city may, in the future, increase the absolute number of businesses within its jurisdiction, their consumption of real property and consequently their contributions to public funds in terms of property taxes is relatively small. The changing function of the central business district has thereby been accompanied by an important shift in the balance of the tax base — and the trend is likely to continue.

In the face of these changes, to which the property tax is unable to adjust, it appears necessary that new flexibility be added to the taxing powers of municipalities. Tax strategy suggests that municipalities should be given access to, and should concentrate their taxation powers on those entities least able to flee the taxing jurisdiction. That is, taxes which recognize changes in the economic use of land and which reflect the ability of subjects to pay — as well as their consumption of public services — should be brought into play.

UNDESIRABLE CHARACTERISTICS OF THE PROPERTY TAX

A number of problems emerge as a direct result of the narrow and inflexible tax base available to the metropolis. Though the problems to be discussed are experienced in varying degree by different sized municipalities, they show up in their sharpest relief in metropolitan areas where the demand for services and pressure on revenue sources is greatest.

(i.) The property tax, with its differential feature and business surcharge, places a premium on non-residential assessment. The combination of such high tax, and, it is often assumed, low service-cost type development causes intense inter-municipal competition for this sort of assessment. Within the Hamilton-Toronto region, and within the metropolitan area itself, pressure for industrial development has encouraged 'fiscal zoning' whereby unimproved land is zoned to serve essentially fiscal objectives. The resulting pattern of development, dictated by dependence on real property taxes, may not accurately reflect economic factors which otherwise would result in quite different patterns of land uses. Thus, the overriding need for premium assessment may frustrate an efficient arrangement of economic activity in the region.

Competition for non-residential assessment, and fiscal zoning may result in the reservation of unrealistically large tracts of land for industrial development. This not only encourages sprawl but may also lead to the extension of services before they are economically justified, throwing an unnecessary burden on the community-at-large.

(ii.) The newer suburban fringe municipalities of Metro have not encouraged residential development of a type which is thought to require higher servicing costs and lower unit assessments. They would prefer high-value, residential development of low density, to more intensive types of land uses. Under present taxing conditions, this response to the pressure of rising expenditures makes financial sense as such development requires less servicing in terms of schools, welfare, and protective services. If there were less reliance on the taxation of real property, and a broader tax base were available to municipalities, the incentive to exclude higher density residential development that is more within the means of lower income groups would be reduced. The choice of living accommodation and location within the metropolis would be increased for a greater proportion of the population.

(iii.) Heavy reliance on the property tax also encourages municipalities to overzone land beyond reasonable foreseeable demand. Evidence of this tendency is quite widespread but shows most clearly in the 'grey' areas ringing the central core of the city. Here quantities of obsolete and decaying commercial and residential properties occupy areas which for years have borne premium zoning designations but for which there is little demand.

In the light of the emphasis that must be placed on the property tax by municipal authorities, the desire for high assessment redevelopment is understandable. Yet such overzoning not only deprives the city of areas which might be reconstructed with more modest, though still desirable types of development, but it also encourages speculation and retention of obsolete, low valued properties. Again, the constraints imposed by a narrow tax base are seen to have undesirable side effects.

(iv.) Finally, new development and certain existing types of land uses may be adversely affected — particularly in the core city and its surrounding 'grey areas'. It has already been noted that manufacturing concerns are leaving the City. This is due to a variety of economic forces but it is likely that high tax rates have served to loosen the already weak ties of such enterprises with the city environment. Smaller marginal commercial concerns have also been affected. Caught in the vigorous competition of the downtown retail giants and their suburban counterparts, these businesses find it increasingly difficult to shift higher property taxes to consumers in the price of their goods.

Though no specific evidence can be offered with regard to Toronto, it is likely that large redevelopment projects also will become more sensitive to municipal taxes as expenditure levels rise in the central city. Certainly, this has been the case in other cities where the amount of the municipal levy has been decisive in determining the economic feasibility of major redevelopment schemes. The problem has been that of guaranteeing an investor in extensive capital improvements, a return that would be proportional to the return realized by the owner of an older, depreciated property. One innovation developed to meet this problem is worth mentioning though it is no more than an expedient which seeks to circumvent the basic inability of the property tax to adapt to the changing fiscal realities of the metropolis.*

Facing the loss of a $100 million dollar redevelopment proposal because of high property taxes, authorities in Boston developed a method of taxation that was based on a 'reasonable return on the investment'. The project was exempt from normal property taxation and paid an excise related to anticipated earnings from the property. A similar accommodation was developed in New Jersey providing for fixed-term exemptions from property taxes and annual tax payments amounts to 15% of the gross rental income derived from redevelopment projects. Though a question arises as to whether such devices divert investment from other areas, the fact is that such large projects are relatively inflexible as to location and can only be constructed in the core of the metropolis and not in other municipalities. This form of taxation is important in so far as it is an attempt to tailor the fiscal machinery of the metropolis to changing conditions, and not the reverse.

(v.) A final note might be made of the apparent tendency of the property tax to penalize and discourage the rehabilitation and improvement of private property. If, as it is predicted, the rings of obsolete and decaying property presently surrounding the central core increase, it appears foolhardy not to seek out a means whereby the property tax, or some other fiscal measure, can be used as an instrument of social policy as well as a revenue raising device.

*The example is based on a description in Tax Policy, Volume XXIX, Nos. 7-8-9, 1962.

THE PROVINCIAL INTEREST

The final area of fiscal concern to the metropolis, arising from its peculiar revenue and expenditure requirements, involves its relationship to the Provincial Government. The interests of the Toronto metropolitan region and the Province are converging in many important functional areas. The day, when local governments administered and were able to finance a well-defined range of services, has passed. Rapid urbanization, the emergence of so-called 'positive' government, and technological change, have radically altered the former balance between municipal responsibilities and revenues. In the face of a more or less inelastic municipal tax structure, and the need to finance certain services from a much wider base, and from a different point in the income stream, there has been a continuous transfer of responsibilities from the local level to the Province. This has been accompanied by marked increases in provincial transfers to municipalities — usually in the form of conditional grants. But despite these adjustments, municipalities have laboured under mounting financial pressures which indicate increased direct provincial involvement in local financing in the future. The overall trend was recently summarized by Professor D. W. Slater:

*" . . . municipal government expenditures have increased more rapidly than the national output, rising from about 4.9% to 8.3% of GNP between 1950 and 1962. The revenues raised by municipalities have increased from about 3.5% to about 5% GNP. Despite the proportionately more rapid growth in the revenues raised by municipalities than in the value of the national output, the share of municipal expenditures financed by their own revenue-raising activities has fallen steadily, from nearly 70% in 1950 to about 60% in 1962. This growing gap has been filled primarily by increased reliance on transfers from provincial to municipal governments."**

These shifts of responsibility and intergovernmental transfers pose important questions relating to the financial and administrative viability of local government. They are particularly vital to metropolitan Toronto due to its unique role and dominant position in the life of the province and nation. Such a strong mutuality of interest has developed between the Province, the metropolitan area and the Hamilton-Toronto region, that a major realignment of fiscal powers and relationships seems unavoidable.

**Slater, D. W., Urban Growth and Municipal Finance,* The Canadian Banker, *Summer 1963, p.13.*

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BUREAU OF MUNICIPAL RESEARCH

Founded in 1914 by a group of public-spirited citizens — operating since then under provincial charter as a non-partisan, non-profit research agency — staffed full time by well qualified personnel — the Bureau of Municipal Research keeps local government operations in Greater Toronto under constant scrutiny.

The Bureau has gained wide recognition as an effective proponent of good government through its bulletin *Civic Affairs,* through the publicity given its statements, through its information and advisory services, and through the participation of the staff in the public discussion of municipal issues.

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