

BUREAU OF MUNICIPAL RESEARCH
Submission to
THE ONTARIO COMMITTEE ON TAXATION

A REPORT ON THE TAXATION OF
PERSONAL PROPERTY INCLUDING STOCK-IN-TRADE

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TABLE OF CONTENTS

	Page
1.) History of Personal Property Taxes	1
2.) Present Use in Canada	4
(1) Newfoundland	4
(2) Prince Edward Island	5
(3) New Brunswick	5
(4) Nova Scotia	6
(5) Quebec	6
(6) Ontario	7
(7) Manitoba	8
(8) Saskatchewan	8
(9) Alberta	8
(10) British Columbia	9
3.) Value of Taxes Levied on Personal Property	10
4.) Some recent Canadian comment	11
5.) Present Use in the United States	13
6.) Philosophic Justification	15
7.) Shifting and Incidence of Personal Property Taxes	17
8.) Possible Application of Personal Property Taxes in Ontario	18

HISTORY OF PERSONAL PROPERTY TAXES

In early colonial times, little use was made of direct taxes. The tariff was almost the sole source of tax revenue though rudimentary property taxes appeared in one or two instances. The earliest of these were levied during the French regime. In 1716, an annual tax payable by the seigneurs of Montreal was levied to construct a stone wall around the City. In 1749, the inhabitants of Quebec City paid a tax on their land to finance the construction of barracks. But these were isolated instances and nowhere in Canada, until 1793, did direct taxes, particularly property taxes form a continuing source of revenue. In that year, Justices of the Peace, meeting in Courts of Quarter Sessions, were permitted to levy crude forms of property taxes in Upper Canada. This marked the start of the first continuing levy of direct taxes in British North America.

Following the passage of the Baldwin Act in 1850 which transferred the responsibility to levy property taxes from the justices of the peace to municipal councils, the Assessment Act of 1850 was passed. This Act replaced the crude system of property assessment and taxation that had developed since 1793 with a relatively sophisticated local tax system. The Act provided that all lands and a limited amount of personal property and income in excess of £50 a year were to be subject to municipal property taxes. Procedures for assessment, appeals and so on, established at the time, shaped the local tax system to such an extent that its essential features still form the basis of municipal taxation today.

The Assessment Act accorded an important place to the personal property tax in Ontario. At the start of the Confederation period (generally considered to be the period of 1867 to 1890), the general property tax was levied on all real and personal property, with the exception of household effects and personal property valued at less than \$100. The importance of the property tax at the time was natural enough in so far as the vast majority of municipal services were directly related to property and, as was the case throughout North America, most wealth was in the form of tangible personal property in one form or another. In taxing personal property, Canadian municipalities followed an American rather than a British practice. Throughout the Confederation period in Canada, most American states levied general personal property taxes whereas property

taxes in Britain had been limited to real estate since 1700.

But as the confederation period progressed, the same factors that led to a general dissolutionment with the property tax in the United States gained momentum from Ontario to the west. The tax failed in an economy and society in which wealth was increasingly taking the form of easily concealed intangible personal property. Resistance to disclosure, difficulty of valuation, the unpopularity of the tax, and haphazard administration created a situation in which the tax resolved itself largely as a levy against the inventory of merchants. The intangible wealth of bank deposits, securities and mortgages largely escaped valuation and assessment. The inequity of the tax essentially as a levy against business inventories, was widely recognized. Not only did the 'business tax' discriminate against a particular class of industry but its incidence was also unfair between merchants within the industry itself. The inadequacy of stock-in-trade as a measure of ability to pay was made manifest by the fact that many profitable businesses were quite capable of paying taxes, while some of those with large inventories had very little ability to bear property taxes.

The pressure in Ontario for reform and eventually the abolition of the personal property tax was reflected in testimony before a number of enquiries into the tax structure of the province. The Committee on Exemptions in 1878 heard evidence opposing the tax. The Commission on Municipal Institutions in 1888 and 1889 examined several alternate forms of taxation. In 1893, the Commission on Municipal Taxation condemned the personal property tax as did the Assessment Commission in 1900. Finally, a special committee of the legislature, appointed to review the report of the Assessment Commission recommended the abandonment of the personal property tax altogether and the substitution therefore of the present Ontario municipal business tax based on a varying proportion of the assessed value of properties. The recommendation was accepted by the Government in 1904. It is interesting to note that in establishing a classified business tax graded according to the type of business, an attempt was made to reproduce the approximate amount of personal property tax that previously had been paid by each class of business.¹

¹ McClelland Report.

Growth in the popularity of property taxes in Ontario closely followed the experience of the United States. The abolition of the personal property tax in Ontario and other Canadian province came at a time when the tax was under heavy attack in the United States. In contrast to Canada, however, personal property taxes were retained by most states, usually in a modified form.

The theory of the original property tax was that within any taxing district, property of every description was to be taxed unless a particular class was expressly exempted. All rates levied on any property were to be uniform and there was to be a standard basis of assessment. This was known as the 'uniform rule' of taxation.

Toward the middle of the nineteenth century, however, the emergence of the country from a pioneer to an industrial economy caused severe stresses on the property tax. Property wealth was no longer held solely in the form of tangible, visible, and reasonably well appraised goods. Land, livestock, merchandise and a limited amount of mercantile credits were augmented by a great variety of new and complicated investment and commercial instruments which became the predominant form in which wealth was held. The gross inequities that this development brought about due to the inability or disinclination of assessors to value personal property for purposes of taxation, resulted in major modifications in the nature of the property tax base. The most important development was the adoption of the classified property tax. Property was divided into various classes each of which were taxed at varying rates. This measure was intended to reduce the tax burden on intangible forms of personal wealth in order to reduce the incentive to evade taxation. It was also intended to promote more complete and more equitable assessment, and in the long-run, produce more revenue by bringing into the open the mortgages, securities, and savings that comprised the wealth of the commercial state.

The most frequent classification was between tangible and intangible property with the latter tax at a substantially lower rate than the former. But throughout the United States, there was no unanimity respecting the form that property taxation should take, its administrative feasibility or even its justification in terms of equity.

Since each State is responsible for direct taxation, as many forms of the tax have developed as there are taxing jurisdictions. Today, the present scope of the property tax legally ranges from broad coverage of real property in tangible and intangible personalty in two or three States, to the exclusion of all classes of property as a subject of taxation, except real property, in four others.¹

Present Use in Canada ↓

Four provinces in Canada authorize the use of both real and personal property taxes -- Prince Edward Island, Nova Scotia, New Brunswick and Manitoba. In the remaining provinces, the definition of real property includes some elements of personal property -- usually machinery and equipment. In addition, the business tax in some provinces may be based on stock-in-trade which again is normally regarded as personal property. Thus, in each of the ten provinces, in one form or another, personal property may be assessed and taxed for municipal purposes.

In the following, the nature of personal property taxation in Canada is surveyed and recent comment by provincial enquiries on its suitability as a municipal tax is summarized.

1.) Newfoundland

There is no general provision for personal property taxation in Newfoundland. However, manufacturing machinery is assessable as real property. The Assessment Act (1958) defines real property so as to include "all buildings and any part of any building and all machinery and fixtures erected or placed therein or thereon, in, over or affixed to land".²

A second form of personalty that may be taxed is stock-in-trade. However, its assessment and taxation are conditional. If a council is not assessing real property, a stock-in-trade tax may be imposed. But both may not be taxed at the same time. If the stock tax is levied, it must be set at a rate of not less than 20¢ and not more than \$1.00 for every \$100 of the value of the stock-in-trade held

¹

Delaware, Hawaii, New York, Pennsylvania.

²The Assessment Act (1958) Ch.5.

at the end of the preceding year. It is imposed on the occupier of shops, stores, warehouses, storage yards and factories. In so far as the assessment of the tax is not in some way based on an average annual or monthly value of stock, it is at variance with assessment procedures in other provinces.

2.) Prince Edward Island

The Town Act provides for a broadly based personal property tax. Included in the definition of personal property are household furniture, moveable property, goods, wares and merchandise, or stock-in-trade.¹ The basis of assessment is 'actual cash value'. Specifically excluded is intangible personal property -- stocks, bonds, money and the like. The proceeds of personal property taxes are limited to general municipal purposes and may not be used for school expenditures. As is the case in Manitoba, municipal councils must elect to levy either a business tax (flat rate on a classified list of businesses), or a personal property tax, but not both.

3.) New Brunswick

The personal property tax in New Brunswick, with certain exceptions, is levied against all property other than real estate.² Stock-in-trade, assessed at the average annual value of goods used during the year, is included. Accepted from the definition of personal property is personal clothing, domestic, household and natural products acquired under any intent in a lease, licenses or permits issued by the provincial government and a variety of intangibles including money, debts, mortgages, stocks and bonds. Personal property owned by a resident which is located outside the province and personal property owned by a non resident located in the province is taxable. Personal property is assessed at 'real and true' value.

Under special legislative provisions, the personal property tax is no longer levied in the cities of St. John and Fredericton.

1

The Town Act, R.S.P.E.I. 1951, Ch. 162 as amended
The Village Service Act

2

Municipal Rates and Taxes Act, R.S.N.B., Ch.1191, S.1(e) as amended.

4.) Nova Scotia

The basis of the personal property tax in Nova Scotia includes all personal goods and chattels, valued at their 'actual cash value', one half of the value of all ships and, in the case of banks, their annual income valued, for purposes of assessment, at \$20 for each \$100 of net income. The average annual value of stock-in-trade of merchants, traders, manufacturers, tradesmen or mechanics, valued at cost, is also included as personal property.¹

The City of Halifax no longer levies a tax on personal property having substituted a business surcharge which is equivalent to 50% of the assessed value of real property assessment.

5.) Quebec.

No general legislative authority exists in Quebec for the assessment and taxation of personal property. However, real property, as defined in the Cities and Towns Act, includes machinery used in manufacturing so that this class of personal property is subject to general municipal taxation in urban areas.² Rural municipalities, on the other hand, are not empowered to assess machinery as real property. In addition, the councils of cities and towns may, at their own discretion, exempt manufacturing machinery.

Stock-in-trade may be assessed as a basis for business taxation. Alternate, and frequently used business tax bases are the rental value of business property, and a flat rate levy. If the stock tax is levied, it may not exceed 1% of the average annual value of stock-in-trade in cities and towns or, in villages and rural municipalities, 1/10 of 1%.

The Cities and Towns Act also authorizes urban areas to levy a special tax on motor vehicles. ✓

1

The Assessment Act, R.S.N.S. 1954, Ch. 15, as amended.

2

Cities and Towns Act, R.S.Q., 1941, Ch.233, as amended.

6.) Ontario

Personal property, as a class, is excluded from the definition of real property in Ontario.¹ Farm and manufacturing machinery and fixtures, on the other hand, are specifically included in the definition of real property but are exempt from property taxation:

S.4 "All real property in Ontario

17 All machinery and equipment

..... power or other service." ²

This clause has sharply restricted the inclusion of machinery and fixtures in the definition of taxable real property. But there has been a persistent trend toward broadening the types of property liable to taxation. Two recent decisions of the Supreme Court of Ontario included as fixtures in the definition real property, certain radio broadcasting equipment and bowling alleys.³ It is thought by many assessors that as a result of a still more recent case, *Richmond v. City of London*, all machinery and equipment not used for manufacturing which is located in a permanent structure and which is not intended to be moved during its period of usefulness might well be classed as real property and liable to taxation. In his judgement, Mr. Justice Gale referred to the likelihood that equipment, such as printing presses, might fall into this class. ✓

At the present time, the extent to which machinery and equipment can be subjected to property taxes is not settled in Ontario. In its brief to the Ontario Committee on Taxation, and in a resolution placed before the annual convention of the Ontario Municipal Association, the Municipal Institute of Assessors recommended either that the legislation dealing with the liability of machinery and equipment not used

1.

The Assessment Act, R.S.O., Ch.23, as amended S.1(i).

2.

The Assessment Act, S.4(17)

3.

Northern Broadcasting Co. Ltd. v. District of Mountjoy, 1950, S.C.R. p.502 and *The Municipality of Metropolitan Toronto v. Eglinton Bowling Co. Limited*, 1957, O.R., p.621.

for manufacturing either be clarified or that its assessment be abolished altogether.

7.) Manitoba

Municipalities in Manitoba may levy either a tax on personal property or, alternatively, a business tax but not both. No matter which tax is chosen, personal property, in the form of machinery and equipment used in the marketing of oil, for instance, and other particular types of property must be assessed and taxed as real property. In addition, oil, gas or salt production equipment and other personal property, determined by the municipal council, is assessed and taxed as personal property.

Personal property is defined as meaning 'goods and chattels' and, in addition to a variety of tangible personalty, includes such intangible assets as shares and stock of corporations.¹ Household effects, farm produce, stock and farm machinery are exempted from personal property assessment and taxation.

Stock-in-trade is assessed at the amount of the average stock kept on hand during the twelve months immediately prior to the time of the assessment.²

8.) Saskatchewan

Together with Ontario, the assessment and taxation of personal property appears to be more restricted than in the other provinces. There is no legislative provision for personal property taxes and machinery is specifically excluded from the definition of real property. The only vestige of personalty that enters the municipal tax base is the plant and equipment of mines, oil and gas wells and gravel pits.

9.) Alberta

Though there is no personal property tax in Alberta, machinery and equipment are classified as real property and taxed for municipal purposes. 'Improvements' in the province are defined to include

1.
The Municipal Act, Ch.173, S.983(i)
2.
The Municipal Act, Ch.173, S.1014

"machinery and equipment, appliances and other things that form an integral part of an operational unit designed for or used in (a.) processing or manufacturing, or (b.) the production of natural resources or the transmission of natural resources by pipeline etc."¹ However, councils are given the option of levying a business tax. In such a case, personal property of such a nature is exempted and a business tax substituted therefore based on rental value, area of premises occupied or storage capacity.

10.) British Columbia

Commercial and industrial fixtures, which are not removable by a tenant, and fixed machinery are classed as improvements to land and may be assessed and taxed for general municipal purposes.² For purposes of school rates, the definition of improvements is expanded to include fixtures and machinery that could be removed by a tenant. However, the initial \$1,500 of assessed value of such portable personal property is exempt for school purposes. If two-thirds of a municipal council wish, the definition of improvements for general municipal purposes may be broadened to include all commercial and industrial fixtures and machinery taxable as real property for school purposes.³

Thus, in all provinces of Canada, various elements of personal property may be subject to municipal taxation. Where specific authority to levy a personal property tax does not exist, personalty is taxed through its inclusion in the definition of real property or as a particular class of personal property -- usually stock-in-trade -- which is subjected to supplementary business taxation.

1.
R.S.A. - The Assessment Act
The City Act

2.
Taxation Act

3.
Public Schools Act.

Value of Taxes levied on Personal Property

In spite of the wide taxation of personal property in Canada, the relative value of taxes raised on this basis is small.

This is so if revenues derived from taxes levied against personal property which is classed as real property, and revenues derived from business taxes whose base includes personalty are excluded. Of the four provinces levying general personal property taxes, only two, Nova Scotia and New Brunswick derive significant proportions of their total tax revenue from personal property. The proportions in Nova Scotia, based on estimated tax receipts in 1963 was 15%. In New Brunswick, 17% of total estimated tax revenues were derived from the personal property tax.¹ The following Table shows these proportions and figures for estimated tax revenues.

Gross Current Taxation Revenue (Est.1963)
\$000's

	<u>Prince Edward Island</u>	<u>New Brunswick</u>	<u>Nova Scotia</u>	<u>Manitoba</u>
real property	\$2,751	\$23,738	\$33,997	\$72,037
personal property	162	5,877	6,840	(1)
business	280	2,576	1,744	6,204
other	138	3,110	1,633	491
special assessments	48	111	480	7,508
Total taxation	<u>\$3,379</u>	<u>\$35,412</u>	<u>\$44,694</u>	<u>\$86,240</u>

(1) "personal property tax" included in "real property tax".

Source: Dominion Bureau of Statistics, Financial Statistics of Municipal Governments 1962-63. Revenue and Expenditure, p.20.

The bulk of tax revenues raised from personal property undoubtedly are derived from taxes levied on stock-in-trade and on machinery and equipment. The former tax may be levied in six provinces.

1. Dominion Bureau of Statistics. Financial Statistics of Municipal Governments 1962-63. Nbr. 68-203. p.20.

In another five provinces, machinery, fixtures and equipment may be classed as real property and taxed on that basis. It is not possible to determine the relative share of tax revenues attributable to either tax base.¹

Where it is subject to taxation, machinery and equipment is taken into and becomes indistinguishable from taxes levied on real property. Stock-in-trade, on the other hand, either is taken into personal property or is not separated from other business tax revenues.

Some recent Canadian comment.

From 1902, when the McLennan Commission recommended the abolition of the general personal property tax in Ontario, until the post war years, little was said by commissions of enquiry in condemnation of the tax. In 1947, a commission of enquiry into the tax structure of the City of Fredericton, New Brunswick, recommended against use of the tax in the province with the exception of the taxation of bicycles and motor vehicles. This recommendation was subsequently adopted by the City though use of the tax continues throughout the rest of the province.

In Nova Scotia, the report on the Reorganization of Provincial Municipal Relations recommended "either that the personal property tax be abandoned or that a system be developed for assessing business and household equipment more accurately"². As indicated previously, the personal property tax is still widely employed by municipalities in the province in spite of this advice tendered in 1949.

In 1958, the personal property tax was withdrawn in Alberta after many years of use. Ten years previously, a Royal Commission on Taxation in the province endorsed its continued use on the grounds that the tax base available to municipalities would be too restricted if limited to taxes on real property.³

1.

An exception is the proceeds of the Newfoundland stock-in-trade tax which in 1960 contributed \$4,334 to total municipal tax revenues.

2.

The Re-organization of Provincial-Municipal Relations in Nova Scotia, The Nova Scotia Municipal Bureau, 1949, p.302.

3.

Report of the Royal Commission on Taxation 1948, p.42.

More recently, two Royal Commissions, in two provinces in which personal property taxes are levied, have recommended the withdrawal of the tax. In Manitoba, the Royal Commission on Local Government Organization and Finance found the tax "difficult to collect, expensive to administer and may be subject to abuse". The Commission also recommended that oil, natural gas, salt production equipment and gas transmission lines also be removed from the category of personal property.¹ Similarly, the 'Byrne Commission' concluded that since "it has been found impossible to devise a system of personal property taxation which will provide even the roughest measure of justice and equity we recommend that the personal property tax be abolished forthwith in all municipalities."²

Thus, with one or two exceptions, commissions of enquiry throughout Canada have condemned the general personal property tax. In many instances, business taxes have been proposed as alternate sources of revenue. Yet in recommending business taxes or in commenting on the taxation of personal property, the various commissions have had little to say about the inclusion in the tax base of various types of tangible personal property, particularly stock-in-trade and the classification of machinery and equipment as real property. This apparent anomaly is perhaps due to the emphasis given to the administrative difficulty of equitably assessing and taxing personal property. The inference perhaps may be drawn that if other types of personal property were as easily detected and readily assessed as stock-in-trade, and machinery and fixtures, commissions would be far less unanimous in their condemnation of the tax. The fact remains however, that in those taxing jurisdictions in which such personalty is taxed its detection and valuation is by no means single, certain and equitable.

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1. Report of the Manitoba Royal Commission on Local Government Organization and Finance, Winnipeg, April 1964.
 2. Report of the New Brunswick Royal Commission on Finance and Municipal Taxation, Fredericton, Queen's Printer 1963, pp.87 and 93.

Present Use in the United States

It is not intended to give an exhaustive survey of the personal property tax in the United States. However, some recognition should be given to its prevalence since the personal property tax is an important revenue source in all but a few states.¹

Use of the property tax ranges legally from broad coverage of real property and tangible and intangible personalty in some states to the exclusion of all but real property in others. Between these poles, property is classified in some jurisdictions so as to exclude various types of personal property or property may be taxed on the basis of differing proportions of value. Even in the four states which limit the property tax to real property -- Delaware, Hawaii, New York, Pennsylvania -- the definition of real property differs and the proportions of value on which taxes are imposed differ considerably.

Over half of the states tax intangible personal property at full value though all but eleven of these have established different rates for intangibles than the rates levied on real property. In these cases, taxes are usually set at low fixed rates or the property is assessed at greatly reduced percentages of full value.

The base for taxing tangible personal property has been removed in most states. This has been done by providing exemptions so as to exclude small items, exempting altogether property whose assessment is particularly annoying to the public and by limiting the taxation of tangibles to property used in business.²

Though legislation directing full ad valorem taxation of personal property remains in the statute books of most states, the extent to which the law is observed is very restricted. The difficulty of the task confronting legislators and assessors is such that the base has been eroded by extralegal means. The arbitrary measures adopted by those responsible for the administration of the tax to obtain a semblance of

1.

Much of the following is based on a report of the Advisory Commission on Intergovernmental Relations, June 1963. The Role of the States in Strengthening the Property Tax.

2.

Ibid p.31

compliance and equity is reminiscent of conditions which led to the abandonment of the tax in various Canadian provinces.

The general property tax in the United States has been progressively narrowed over the past century as already noted. During the period, the tax has been roundly condemned in every quarter. Yet more recently, an occasional voice has been raised, not in defense of the personal property tax in its present form and as it is administered in many taxing jurisdictions, but as it might be if its limitations were recognized in legislation and modern techniques of detection, valuation and collection were adopted.¹ The Advisory Committee on Intergovernmental Relations argues that present personal property tax laws are outmoded and impracticable. If a tax base were defined which could be fairly administered, the present prospect of losing completely personal property as a municipal tax resource would be averted. In addition to realistic property tax laws, the Committee suggests that improvements in administrative arrangements -- skilled assessors and central, mechanized assessment and collection -- would do much to reverse public aversion of the tax.

The urgency in effecting such changes in the United States stems from two considerations.² First, the inequities of present personal property taxes are so gross that far reaching improvements must be made if present injustices are to be prevented. Second, it seems inevitable that for a number of reasons, the personal property tax will persist. There is no obvious alternative revenue source available to municipalities;² the tax is suited to financing local needs; it is one of a number of taxes that offers local authorities diversity in their

1.

Ibid. p.33.

2.

Interim Report of the Committee on Personal Property Taxation, Proceedings 1952, National Tax Association. p.74.

3.

In 1956, it was estimated by the U.S. Census Bureau that personal property assessments in the United States, of \$47.2 billion, represented 17.4% of all property assessments. Cited in Personal Property Taxation Today, B. H. Schoffer, Municipal Finance, Vol. 32, No. 3 P. 142.

tax base; the property tax is virtually the only tax which does not entail competition with senior governments.

Philosophic Justification

The basic theoretical justification of property taxation is traditionally tested against the canons of ability to pay and benefits received. More often than not, simple recognition is made of expediency in justifying the levy against property.

Students of public finance are in general agreement that the burden of property taxes is not distributed according to the ability of subjects of the tax to pay. Ownership of property does not necessarily indicate tax paying capacity. Levies on consumer goods and real property bear little consistent relation to income and, because property taxes imposed against income producing properties may be shifted to consumers, in whole or in part, the income of the produces need bear no relation to the tax.

Though there is no dependable relation between property ownership and ability to pay taxes, there is a tacit presumption that property indicates a greater measure of taxable capacity than that of one who does not own property. There is an inference that this measure is roughly proportionate to the value of property to which title is held. But because there is no accurate means by which this presumed capacity can be translated into a scale of ability to pay, there is little to justify property taxes on the basis of the ability principle. Further, since the property tax is regressive to income, it violates the principle of ability to the extent to which income measures ability.¹

On the benefit side, it is plain enough that property owners are beneficiaries of many direct public services financed from levies on property. In addition, owners of property benefit from increases in the value of their land and buildings resulting from the expenditure

1.

Goffman I.

of revenues derived from property taxes. Therefore, the benefits received by owners of property should not be ignored in the analysis of property taxes. However, the extent to which the tax can be justified on the grounds of benefit and protection is restricted. Benefits to property are subjective, uneven as between properties and classes of property, and difficult to measure. Furthermore, benefits resulting from the expenditure of public funds are not limited to property owners but may be widely diffused. Taxes may also be shifted with the result that, direct monetary burdens may be imposed on non owners. In the face of these limiting factors, the case for the taxation of property is restricted. In spite of the fact that only the most tenuous justification for the property tax can be made on grounds of ability or benefit, the ownership of property does indicate some taxable capacity of the owner to contribute to the cost of government and to the cost of benefits he receives from public services. At best, these measures are no more than a crude justification for the taxation of property.

Because of its significance in Canada, the taxation of tangible personal property used in business, particularly machinery, equipment, and inventories or stock-in-trade might be singled out. Traditional tax theory assumes that the value of machinery and equipment is as adequate a measure of taxable wealth as the value of real property; that it has the same general capacity to support taxation. Like real property, the value of machinery and equipment bears no direct relation to the ability of the owner to bear taxes. Yet it reflects some capacity and assumes receipt of some benefit. So that while the theoretical justification for taxing such fixed assets as machinery and equipment is no stronger than that for taxing real property, it appears to be as strong.

On the other hand, the nature of stock-in-trade or inventory is such that there are strong arguments against its taxation. Inventory, as opposed to realty and tangible personal property of a fixed asset variety, is a current asset which is in no way related to the income and taxable capacity of its owner. Nor does it bear a fixed relation to total property value or net worth. Therefore, taxation of inventory causes considerable variation in tax burden between industries and

between firms within the same industry. Because these and other factors related to valuation would contribute to great burden variations that could well be incurred by the assessment process, the principle of equity appears to be overriding.

Current tax theory is agreed that at best, the grounds for taxing property, in this case personal property, are tenuous. The tax cannot be defended on grounds of ability or tax capacity though there is a clear inference that ownership of property indicates some capacity. In terms of benefits received, the tax finds only partial justification and then only for tangible personal property of a fixed asset variety.

Shifting and Incidence of Personal Property Taxes

For purposes of examining the shifting and incidence of taxes levied on personal property, each of several kinds of property should be considered separately. Personal property can be divided into three classes: a.) personalty in the form of inventories, machinery and other items used in the productive process, b.) tangible consumer goods such as furniture and jewellery, c.) intangibles which might be mortgages, stock certificates, bank balances. The question is whether the monetary burden of tax on property in each of these categories remains at the initial point of impact or whether it is shifted. In addition, whether the burden of the tax is shifted or not, what is the relation of the incidence of the tax to the income from which it is paid.

The tax is shifted, in whole or in part, if it causes a direct increase in the price of a good or a direct decrease in the price of a factor of production. Since all costs of production must eventually be included in the price of goods if production is to continue, taxes on personal property used in the productive process are likely to be shifted. However, the market price of commodities may not always be elastic enough to permit the inclusion of all costs involved in their production. But because supplies of personal property may be altered in the short-run, the owners of taxed personal property may make adjustments which will permit them to pass on the burden of the tax in the price of their goods.

This is in contrast to opportunities for shifting available to owners of productive properties, such as land and buildings, which are in fixed supply.

Because these adjustments may be made, there is a strong tendency for taxes on personal property used in production to be shifted forward to consumers in the short-run, particularly under full-cost pricing.

Taxes on tangible personal property of a personal nature are simply a levy on consumption. There are no opportunities to shift the tax since there is normally no further transaction following the imposition of the tax and consequently no opportunity for the owner to pass on the burden of the tax.

Similarly, taxes on intangible personal property are not shifted. In the long-run, the price of securities may be pushed down or its return upwards, but the incidence of such taxes is typically on the owner.

A note might be made here with respect to the impact of the personal property tax in terms of the income from which it is paid. A tax on personal or real property tends to be regressive to income. This is due to the improportional nature of property taxes which are in no way related to the income against which they are levied. If taxes imposed on business properties used in the production of consumer goods are shifted forward, the burden of the tax falls on the consumer without regard to his income. If the incidence of the tax in the short-run is on the owners, it is again unrelated to income. Similarly, there is no reliable correlation between taxes levied on tangible personalty and the income of consumers.

Possible Application of Personal Property Taxes in Ontario

In theory and on the basis of its practical application, the personal property tax has met with such universal condemnation that its use in any form is hard to justify and more difficult to imagine. The tax cannot be justified on grounds of the ability principle and its use -- like taxes on real property -- can be only partially justified

on the basis of benefits received by taxpayers. It is acknowledged to be regressive to income and its incidence is uncertain due to secondary and tertiary effects. Furthermore, its failure to contribute to economic stability is recognized and its administration leads to serious injustices.

Because of this, the selection of classes of property for taxation is practically a matter of applying the tax in a manner which offends least against considerations of philosophic justification, equity, and administrative feasibility.

The exemption of intangible personal property from the property tax base is everywhere to be recommended. Experience has shown that intangible property cannot be fairly detected or assessed and all attempts to include it in the tax base have led to extreme injustices. Intangibles were the first class of property to be dropped in the early experiments with the general property tax. It became clear that the taxation of intangibles was administratively unfeasible.

It has been suggested that with centralized collection -- presumably at the provincial level -- the same methods of detection, assessment, and collection utilized in the administration of the federal income tax could be brought into play to greatly increase the chances of equitably taxing intangibles.¹ But it is questionable whether this is so. Notwithstanding administrative problems, the question of source and situs of intangible property is a complex one. Of greater importance, looking at the tax structure as a whole, it is likely that taxes on income are a better device to tap this type of wealth.

In terms of philosophic justification, as good a case can be made for the taxation of tangible consumer goods or personalty as can be made for any other class of property. However, the ability of assessors to detect and value such property is so limited that administratively, and in terms of equity, the tax would fail. In many tax jurisdictions in which tangible consumer goods are taxed, even the provision of high exemption to pass over basic household goods has not resulted in equity

1.

Advisory Commission on Intergovernmental Relations, The Role of the States in strengthening the Property Tax, Vol. 1, Ch.3.

in assessment and taxation of the more valuable types of personalty. The tax is impossible to administer fairly, it would be expensive to apply with any thoroughness, and it is extremely unpopular. Since the tax is one on consumption, another type of tax, the sales tax, perhaps must be relied on.

Tangible personal property used in business includes machinery, equipment, and inventories or stock-in-trade.

Of all classes of personal property, perhaps the best case can be made for the taxation of machinery and equipment. On theoretical grounds, the justification for taxing this category of tangible personal property is no stronger than that for the taxation of real property. But nevertheless, the grounds seem just as strong. Such wealth as property, it has definite location and situs. It is also "the beneficiary of governmental services which give protection to merchandise and machinery quite as much as to buildings. The whole governmental and social scheme is as helpful and as beneficial to the owner of tangible personal property as to the owner of land. Consequently, if there is to be, as part of the general plan of taxation, a tax on property on the grounds of governmental benefits, it may well be applied to tangible personal property."¹

The case for taxing stock-in-trade which, like machinery and equipment, is tangible personal property of an income yielding variety is not strong. Inventory is in no way related to income or taxable capacity and since there is so much variation between industries of the same kind and between types of industry in the nature and use of inventory, its taxation invariably leads to major injustices. The equitable valuation of inventory -- raw material, goods in process, and finished goods is fraught with the uncertainty that the tax cannot be justified.

Machinery and equipment is subject to property taxation in several Canadian provinces. Certain types are already classed as real property in Ontario and the trend is toward broadening the types of machinery and equipment liable to property taxation. If the property

1.

Lutz, H.L., Public Finance, Appelton - Century, New York, 1947, p.412.

tax base is widened in any way, the inclusion of machinery and equipment, but not stock-in-trade, is the least offensive addition that could be made.