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Considerations in Rate-Setting Policies for Dwellings

July 8, 2020 | ENID SLACK | INSTITUTE ON MUNICIPAL FINANCE AND GOVERNANCE | UNIVERSITY OF TORONTO | enid.slack@utoronto.ca

Issues to consider

- Nominal versus effective tax rates
- What criteria should be used to determine tax rates?
- Who should determine the tax rate?
- On what basis should the tax rate be set and how often?
- Should there be more than one tax rate?
- Should tax rates be uniform or progressive?
- How high can tax rates go?

Nominal Versus Effective Tax Rates

- Nominal rate is the tax rate set by the taxing authority
- Effective tax rate = (nominal tax rate X value of tax base)/market value
- Effective tax rate will differ from nominal tax rate depending on:
  - Portion of assessment base that is taxed
  - Difference between tax base and actual market value
  - Proliferation of tax relief schemes – e.g., exemptions, tax limits, tax reductions

Criteria for Setting Tax Rates

- Economic efficiency – minimize distortions
- Benefits received from local services
- Fairness based on ability to pay
- Transparency
- Administrative simplicity

Who Determines the Tax Rate?

- Local setting of tax rates:
  - places accountability at local level
  - responsive to local needs
- Central rate setting:
  - uniform rates across the country
  - reduce tax competition
- Centrally-imposed minimum and/or maximum rates for non-residential properties:
  - Minimum rate to reduce tax competition
  - Maximum rate to reduce tax exporting

On what basis is the tax rate set and how often?

- Tax rate = (expenditures – non-property tax revenues)/assessment base

- Annual determination to reflect budgetary requirements each year

Should there be differential tax rates for different types of residential property?

- Land versus buildings – higher taxation of land encourages development

- Single-family homes versus:
  - Apartments – do services cost less to deliver?
  - Second homes – do taxpayers have greater ability to pay? do they use municipal services?
  - Vacant land – do you want to encourage use of land?

Should there be differential tax rates for different taxpayers?

- Owners versus renters
- Seniors
- High-income versus low-income households

Alternatives to Differential Tax Rates

- Property tax deferrals for seniors
- Circuit breakers (property tax credits) for low-income households – owners and renters
- Relief schemes make tax more acceptable to taxpayers … but complicate the tax system

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Uniform or Progressive Tax Rates?

- Progressive tax rates: higher tax rates on higher-valued houses

- Advantages:
  - leads to progressive taxation of wealth; serves as a partial wealth tax
- Disadvantages:
  - high-income people may move out of the progressive tax rate jurisdiction and low-income people will move in, other things being equal
  - exacerbates liquidity problem faced by seniors on fixed incomes
  - potential increase in number of appeals
  - not as simple, transparent, and predictable in terms of the amount of revenue that will be collected as a uniform tax
- Alternative: property tax relief schemes

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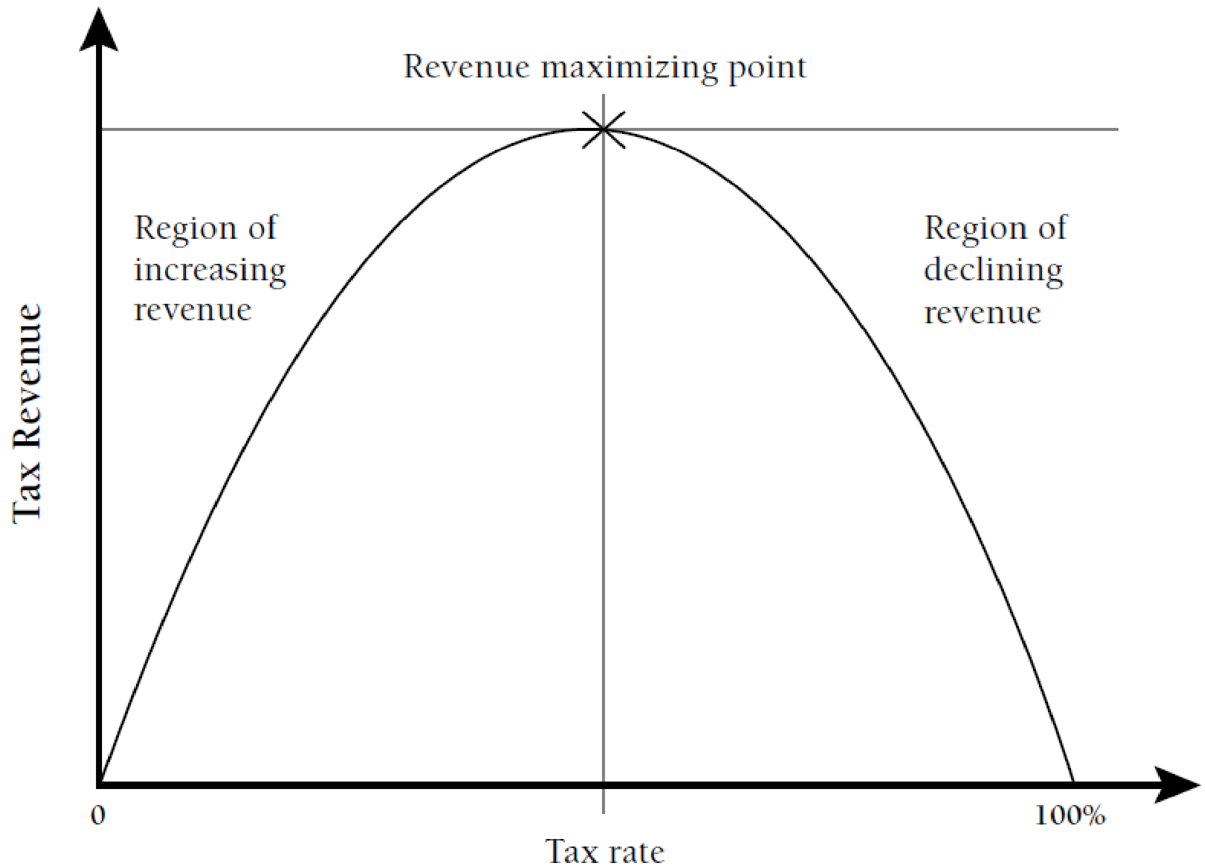
How High Can Rates Go?

Figure 1: A Revenue Hill



Thank you

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